BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement the California Renewables Portfolio Standard Program.	Rulemaking 04-04-026 (Filed April 22, 2004)

COMMENTS OF THE ALLIANCE FOR RETAIL ENERGY MARKETS ON ACHIEVING A 33% RENEWABLE ENERGY TARGET

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In accordance with the direction provided in the November 18, 2005 email from Mr. Andrew Schwartz of the California Public Utilities Commission ("Commission" or "CPUC"), the Alliance for Retail Energy Markets ("AReM")[1] hereby submits these comments on the November 1, 2005, report entitled "Achieving a 33% Renewable Energy Target" (the "Report"). Mr. Schwartz also recommended that comments "should be organized in a manner that makes it clear which section of the report is being addressed. I recommend using the report's table of contents as the organizing framework for your comments. In other words, use the section titles in the TOC as the section titles in your comments." The comments below conform to that directive, with the essence of AReM's position conveyed in a subtitle format. It should also be noted that our silence on any particular issue or recommendation raised in the Report does not signify either agreement or disagreement. Rather, AReM is merely taking the opportunity afforded by comments to highlight the issues most important to our membership that we have identified to date.

[1] AReM is a California non-profit mutual benefit corporation comprised of electric service providers that serve the majority of the state's direct access load. The comments contained in this filing represent the position of AReM, but not necessarily the view of any affiliates of its members with respect to any specific issue.

Introduction

As noted in the forward to the Report, it was requested by the Commission and funded by the Energy Foundation. The Report was developed to assist the Commission in its responsibilities as part of the California Climate Action Team ("CAT"), and as an input to the CAT January 2006 report to the Governor on implementation of the state greenhouse gas reduction target. The purpose of the Report is to "assess how to accelerate and expand the current CPUC Renewable Portfolio Standard (RPS) and related programs to achieve the Governor's goal of meeting 33 percent of statewide electric power supply with renewable energy by 2020."[2] The Report identifies what the Commission can do within the scope of its current jurisdiction, as well as what changes in law are needed to expand renewables procurement efforts to meet the Governor's goal. It also discusses "the necessary implementation steps, barriers that must be overcome and a step-by-step schedule for implementation and adoption of policy changes needed to accelerate California's RPS program to the 33 percent level."[3]

AReM believes that the Governor's goal of increasing the renewable energy standard for all load-serving entities ("LSEs") to 33% by 2020 is laudable. Furthermore, we congratulate the authors of the Report for drafting a thorough and thoughtful study that accurately reflects the challenges that must be overcome if such a goal is to be implemented successfully. The Report is only the first step, however, in assessing the feasibility of achieving that goal. As the Report notes, California's current RPS of 20% is the most ambitious state RPS in the nation in terms of potential capacity additions. Before reaching any conclusions or adopting any final recommendations with respect to increasing the RPS, the Commission and interested parties

[2] Report Preface at p. i. (footnote omitted).
[3] Ibid.

need to obtain more experience with the existing RPS, in order to identify what works and what does not.

By doing so, the state can hopefully adopt successful practices and avoid prolonging unproductive procedures, while crafting a new RPS goal that can be implemented efficiently and successfully. The Commission should also carefully consider the potential impact of increased reliance on intermittent renewable resources on system reliability. Importantly, any recommendations the Commission eventually makes regarding increasing the RPS should take into account the differences between the state's LSEs such as electricity service providers ("ESPs") and investor-owned utilities ("IOUs" or "utilities"), as recently recognized by the Commission in D.05-11-025.

Further, AReM urges the Commission to commence a formal Order Instituting Rulemaking ("OIR") proceeding before formally adopting a new 33% renewables target. Such an OIR should provide the opportunity at least for testimony by all interested parties and possibly hearings, should they be necessary. The Report represents an extremely strong foundation for analysis of the proposed 33% target, but its obvious strengths do not, however, make up for the absence of opinions from all other interests groups and/or the rigors of cross-examination. While this comment process is helpful and will be informative to all concerned, it simply doesn't rise to the level of a formal Commission proceeding. As the Commission more seriously considers a 33% renewables target (as well as when it has gained significantly more experience with the issues extant in the existing 20% RPS standard), AReM recommends an OIR be convened prior to any formal decision on the proposed 33%renewables target.

In the following comments, AReM addresses the following topics of significance with regard to attaining a 33% renewables target:

- the economic feasibility of a 33% renewables target
- the need for LSEs to be able to use out-of-state resources
- reliability and resource diversity considerations
- resource adequacy implications of adopting a 33% renewables target
- the technical feasibility of a 33% renewables target and the need for significant transmission infrastructure additions
- the need for a system of tradable renewable energy credits ("RECs")
- the treatment of ESPs vs. utilities and <u>the need to develop an RPS that works for the State's ESPs and CCAs.</u>

Each of these issues must be considered carefully before the state permanently adopts a more aggressive renewables target. All parties recognize the value of renewables development in terms of environmental benefits and diversity of supply. However, as with many policy initiatives, a final decision must rest on a careful weighing of various societal goals that pertain to the energy market. In this case, we suggest that such goals include the need to hold down costs for consumers, the need to provide reliable supplies and the need for customers to have a meaningful right of choice with regard to their electricity supplier.

<u>Results of Cost Analysis [p. 2]</u>

> **"The Economic Feasibility of achieving a 33% Renewables Target must be a Significant Consideration."**

Economic feasibility and the impact on ratepayers will be an important factor in determining whether the State should adopt a 33% renewables target. The Report analyzes this subject carefully and provides the following summary Cost Analysis:

> The *33 Percent Renewables Base Case* analysis shows that the RPS will result in small average rate increases through 2021, and beyond that will produce long term rate savings. On a net present value basis (2011$, 9% discount rate), the RPS will increase costs to California IOU rate payers by $1.26 billion over the period 2011 to 2020, or roughly an average 0.57 percent rate increase over the period. However, these cost increases are offset by ratepayer savings that accrue in the years 2021 to 2030, after the initial capital investments of the RPS have been completed. The net present value of RPS rate payer impacts for the period 2011 to 2030 is - $175 million (2011$, 9% discount rate), in other words a net savings.[4]

AReM does not challenge the accuracy of this summary and in fact hopes that it may prove to be accurate. It will certainly be beneficial to the state from an environmental perspective if a 33% renewables target can be implemented on a basis that minimizes rate increases for customers. Rather, we simply note that the accuracy of the Report's conclusions regarding the economic feasibility of achieving a 33% renewable energy supply by 2020 depend in large part on the accuracy of its assumptions about the price of natural gas….and this is a matter of concern. Put simply, any assumptions about gas prices ten to twenty years from now are highly speculative. One only need look at gas price forecasts of a few years ago to see that few if any forecasters predicted today's historically high prices. Conversely, a look back at the late 1970s saw gas price forecasts that proved to be absurdly high given the plummeting of gas prices that occurred after the passage of the Natural Gas Policy Act in 1978.

In other words, the only thing we can be sure about with regard to a forecast is that it will undoubtedly be wrong. That is not to suggest that the use of forecasts lacks value. Rather it simply reiterates a point all market observers recognize – that forecasts by their very nature are fallible and that decision making premised solely on forecasts is risky. In short, it is far too early to reach any useful conclusions about the costs or economic feasibility of increasing the RPS standard. This fact argues for the state not engaging in a "rush to judgment" as to the economic

[4] Report at p. 2.

impacts of achieving a 33% renewables target, when we have only just begun to implement the existing 20% target and essentially have next to no practical experience with the economic impacts that may be caused by LSEs (utilities and non-utilities alike) attempting to comply with that standard. AReM also notes that urging caution is not the same as urging rejection. Rather, as noted earlier, we find the 33% goal to be laudable and wish to assist the state and other market participants in conducting a sober and rational study of the matter.

Process and Policy Changes [p. 12]

"It will be Necessary to Allow LSEs to Use Out-of-State Resources."

The Report concludes that it will be necessary to consider allowing LSEs to use RECs from out-of-state resources. For example, among the recommended actions in the Report are, "Allow generator delivery to out-of-state hubs, with purchaser delivery into state" and "Allow out-of-state unbundled RECs, possibly with restrictions."[5] AReM believes this will certainly be the case. It simply is not realistic to assume that all the additional renewable capacity that will be needed to meet a 33% requirement would be built in California.

Further, limiting the renewables available to California LSEs for compliance purposes has the clear potential to drive up cost by eliminating competition from cheaper, out of state suppliers. The Report in fact acknowledges when it observes that, "On the other hand, allowing greater competition from out-of-state renewables can exert downward pressure on renewable prices."[6] In conclusion, as noted in the Report, "While the projections of new renewable energy needs for a 33 percent RPS are quite large, they are well within the capacity development potential of California **and neighboring state resources**."[7] [Emphasis added] AReM concurs

[5] *See*, Report, Table 4, at p. 14.
[6] Report, at p. 16.
[7] Report, at p. 5.

and urges the Commission to avoid a parochial mandate that only California renewable resources may be counted to demonstrate an LSE's compliance.

Renewable Energy Resource Mix [p.41]

"Reliability and Resource Diversity Considerations are also Critical."

The Commission should carefully consider whether increasing the RPS to 33% will produce the optimal resource mix for California. The state should be careful not to divert investment away from clean coal technology and other alternatives that might produce the desired environmental and societal benefits at cost that is lower cost than new renewables, particularly when the relative RA value of the resources (and the cost of back-up capacity) is taken into account. The Commission should not recommend increasing the RPS if it would undermine system reliability or detract significantly from the continued existence of a diverse generation resource mix for the State.

Resource Adequacy [p.51]

"The Adoption of a 33% Renewables Target will have Resource Adequacy Implications that Weigh More Heavily on ESPs than on Utilities."

The Report's assumptions about the resource adequacy value of intermittent renewable resources may prove to be inaccurate and understate the amount and/or the costs of capacity that LSEs would need to procure as a back-up for such resources in order to ensure system reliability. Should this prove to be true, the economic impact of such a development will be disproportionately borne by ESPs, who do not enjoy the utility benefits of guaranteed rates of return and flow-through cost-of-service tariffs.

It should also be recognized that non-utility LSEs are placed in a particularly more uncertain position with regard to resource adequacy requirements than are investor-owned utilities ("IOUs"). IOUs have guaranteed rates of return and the ability to flow through in Commission-approved rates the costs incurred to achieve resource adequacy. For example, if the Commission were to determine that intermittent resources are to be discounted for assessing whether an LSE has met its resource adequacy requirement and/or require non-renewable resources to back up renewable resources, the costs for the IOU will generally simply be flowed through to the ratepayer and the utility's profitability would be unaffected.

ESPs, by contrast, have no such assurances. They have to comply with the same resource adequacy requirements that are imposed on the utilities, yet they have no guaranteed right to have their costs paid for by their customers. Instead, the ESP must endeavor to negotiate contracts with each of its customers that cover the costs of procuring the necessary power, whether renewable, non-renewable or, more likely, a mix of both. The risk of regulatory changes that modify resource adequacy requirements is therefore much more keenly felt by ESPs.

A Commission decision to discount the full capacity of renewable resources or to require non-renewable back-ups to renewable power could have an extremely negative economic impact on an ESP's ability to remain in business. These considerations need to be recognized by the Commission with regard to the implementation of a 33% renewables target and the effect such a target would have on the definition of resource adequacy compliance rules.

Expand Transmission Capacity [p. 71]

> **"The Technical Feasibility of Achieving a 33% Renewables Target Requires Significant Increased Transmission Infrastructure Additions."**

The Report concludes that accessing renewable resources to meet a 33% RPS will require expanding transmission capacity, increasing system operational flexibility and changes to tariffs and rules governing use of the transmission system. AReM strongly supports increased investment in transmission resources and many of the Report's other recommendations, not only to enable LSEs to access resources to meet their RPS requirements, but also as a way to enhance system reliability and reduce the need for investment in RA units. The Commission should encourage investment in new transmission resources regardless of whether the RPS is increased above the current 20%.

Provide Delivery Flexibility, and Allow Unbundled RECs [p.103]

> **"Development of a Tradable Renewable Energy Credits Market that Would Permit RECs to be used to Demonstrate Compliance with a 33% Renewables Target is Essential."**

The Report concludes that it will be necessary to allow LSEs to use unbundled Renewable Energy Credits ("RECs") to meet a 33% portfolio requirement. AReM wholeheartedly agrees. Indeed, it will be very difficult, if not impossible, for most ESPs to meet the current goal of 20% by 2010 if they are not allowed to use unbundled RECs for compliance. The Report's findings concerning the benefits of allowing RECs for compliance should serve to reduce the Commission's concerns in this regard. Further, it is in accordance with the Commission's direction in D.05-11-025, in which it is stated that, "We determine that the current RPS law allows the Commission to explore utilizing unbundled and tradable RECs for RPS

compliance by all entities, including ESPs, CCAs, large utilities, and small and multi-jurisdictional utilities."[8]

For ESPs, allowing unbundled RECs is simply critical for their participation in the RPS program. While none of AReM's members anticipate relying exclusively on unbundled RECs to meet their RPS obligations, unbundled RECs will provide ESPs with a flexible compliance tool that significantly reduces the risks of forward procurement of renewable resources and provides protection against the exercise of market power by renewable generators and marketers during times of scarcity. Long term power purchase agreements may be much longer than the average portfolio commitment of the ESP, leaving the ESP exposed to risk. A simple, annual compliance method based on retirement of RECSs allows ESPs to contract for shorter terms, to separate RECs from power purchases, to buy in small, odd lots as the market evolves and could easily allow out of state renewables to participate. Altogether, this would allow for lower compliance costs, while benefiting the renewables market by providing liquidity.

Unbundled RECs will also enable ESPs to manage their renewable portfolios more efficiently, thereby reducing the costs of RPS compliance for their customers. Further, the use of RECs also enables a cost-effective response to any load migration that may occur. Indeed, allowing unbundled RECs will have significant benefits for all retail suppliers, as well as renewables generators, developers and marketers.

<u>Develop an RPS that Works for the State's ESPs And CCAs [p. 119]</u>

> **"The Adoption of a 33% Renewables Goal Should Reflect the Differences between Different Types of LSEs."**

The Report recognizes that ESP compliance will pose special challenges because the loads served by ESPs are relatively small and ESPs are not all in a position to commit to long-

[8] D.05-11-025, at p. 2.

term renewable electricity contracts. The Report also recognizes that because ESPs will be starting with a smaller percentage of their supply coming from eligible renewable sources than the IOUs, it will be more difficult for ESPs to achieve the 20% target by 2010, much less meet a 33% target thereafter. The Report therefore recommends that ESPs be allowed some additional degree of procurement flexibility, including: (1) allowing unbundled RECs, (2) allowing shorter-term contracts, and/or (3) waiving the detailed procurement process requirements imposed on the state's IOUs. AReM supports this recommendation, which is consistent with the Commission's recent decision on ESP participation in the RPS program. Moreover, it is consistent with the Commission's findings in D.05-11-025 issued on November 18, 2005.

In that decision, the Commission observed that:

> ESPs and CCAs each are subject to separate and distinct legal and regulatory requirements. Although they are each subject to certain requirements of this Commission as assigned by the Legislature, neither is regulated as a "public utility" as defined by the Public Utilities Code, nor are they subject to Commission regulatory authority as a matter of course. Instead, the Commission is granted specific regulatory authority over these entities for particular issues, in this case, RPS. Because of this, each of these entities in existence or planned operates under a business model that is different from a regulated public utility.
>
> For example, as AReM argues, this Commission does not set rates or rates of return for ESPs, or review their overall procurement plans, and ESPs are currently limited in their ability to sign up new customers. Likewise, there is merit to Los Angeles and Chula Vista's fundamental point that CCAs are more akin to local publicly-owned utilities than they are to the investor-owned utilities.[9]
>
> This Commission has less overall control over how ESPs and CCAs operate than we do over how utilities operate. Also, to the extent we consider ESP and CCA operations, our concerns about their operations differ somewhat from our concerns about the operations of the investor-owned utilities. In the context of the RPS program, our primary concern is to ensure that ESPs and CCAs do in fact

[9] We note that the structure of the RPS program, with its calculation of a Market Price Referent, and contract prices above that level paid from Public Goods Charge funds, appears to have been designed specifically to deal with legal issues that are more applicable to utilities than to ESPs or CCAs. [footnote in original]

> reach the goal of 20% renewable energy by 2010.[10] We are, however, somewhat less concerned about the details of how they get there.
>
> Therefore, we do not believe it is reasonable to require these entities to be subject to the exact same steps for RPS implementation purposes as the utilities we fully regulate.[11]

As noted in Ordering Paragraph ("OP") 3 of this decision, a process and schedule for further exploration of the manner in which ESPs, CCAs, and small and multi-jurisdictional utilities should participate in the RPS program is to be developed. ALJ Simon in fact issued on November 28, 2005, a ruling scheduling a December 14 prehearing conference to begin this process. As noted in OP 3, "This process shall include, at a minimum, an opportunity for ESPs, CCAs (or potential CCAs), small and multi-jurisdictional utilities, and any other interested parties, to submit detailed proposals for the manner in which these entities should participate in the RPS program."[12]

The results of this process and the ultimate Commission direction that stems from it should be considered in the adoption of a 33% renewables target. The Report recognizes that ESP compliance may be different from IOU compliance and the forthcoming proceeding should be helpful in distinguishing the differences between utility and non-utility LSE compliance requirements.

Conclusion

As noted above, AReM believes that the Governor's goal of increasing the renewable portfolio standard for all load-serving entities to 33% by 2020 is laudable. However, in order to more accurately assess the feasibility of achieving that goal (the most ambitious state RPS in the

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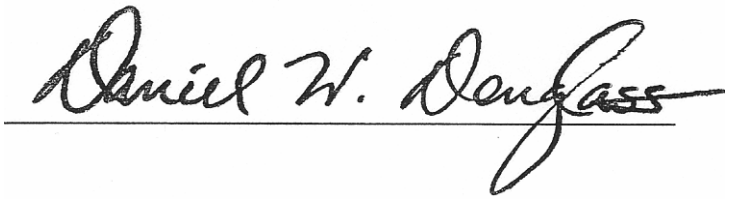
[10] The annual procurement targets are a means of ensuring that goal is reached in a relatively orderly fashion. [footnote in original]
[11] D.05-11-025, at pp. 12-13.
[12] Id., at p. 26.

nation), the Commission and interested parties need to obtain more experience with the existing RPS, in order to identify what works and what does not. Implementation of a 33% renewables target may prove to be both economically and technically feasible, however, there is time to evaluate and appraise LSE compliance with the current 20% by 2010 standard before rushing to adopt the higher goal.

AReM further suggests that a number of other issues needed to be carefully considered, such as the resource adequacy implications of adopting a 33% renewables target; the need for a system of tradable RECs, the necessity for LSEs to be able to use out-of-state resources and the treatment of energy service providers and other non-utility LSEs vis-à-vis the utilities. Each of these issues is discussed above in greater detail. Finally, as the Commission more seriously considers a 33% renewables target and gains more experience with regard to satisfying the existing 20% RPS standard, AReM recommends a formal OIR be convened prior to any formal decision on the proposed 33% renewables target. AReM thanks the Commission and Commission staff for their attention to these comments.

Respectfully submitted,



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