



**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

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Order Instituting Rulemaking on the
Commission's Own Motion into
Combined Heat and Power Pursuant to
Assembly Bill 1613.

Rulemaking 08-06-024
(Filed June 26, 2008)

**COMMENTS OF THE CALIFORNIA CLEAN DG COALITION
REGARDING PROPOSED DECISION ADOPTING POLICIES
AND PROCEDURES FOR PURCHASES OF EXCESS ELECTRICITY
UNDER ASSEMBLY BILL 1613**

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Coalition**

November 19, 2009

SUMMARY OF RECOMMENDATIONS

- Adopt Pricing Option 1 as set forth in Energy Division's Final Staff Proposal
- Adopt a location bonus that appropriately rewards a CHP project based on location
- Ensure that CHP systems participating in an AB 1613 program receive fair compensation for GHG emission reductions and renewable attributes
- Provide that certain provisions of the simplified contract do not apply to CHP systems sized 500 kW or less.

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Pursuant to Rule 14.3 of the Rules of Practice and Procedure of the California Public Utilities Commission ("Commission" or "CPUC"), the California Clean DG Coalition ("CCDC") submits the following comments regarding the Proposed Decision Adopting Policies and Procedures for Purchases of Excess Electricity Under Assembly Bill 1613 ("Proposed Decision").¹

1. Introduction.

The Legislature was crystal clear that it enacted the Waste Heat and Carbon Reduction Act ("AB 1613") to help solve two critical issues facing California. AB 1613 explicitly promotes the capture and use of waste heat to (1) "help offset the growing crisis in electricity supply and transmission congestion in the state," and (2) "reduce[] emissions of carbon dioxide and other carbon-based greenhouse gases."² In furtherance of these goals, AB 1613 authorizes the Commission to require electric corporations to purchase excess electricity delivered by combined heat and power ("CHP") systems that meet certain sizing, energy efficiency, and air pollution control requirements (the "AB 1613 Program").

In many ways, the Proposed Decision purporting to implement AB 1613 gets it right. Unfortunately, the Proposed Decision's approach to pricing utterly fails to capture the value of

¹ CCDC is an ad hoc group interested in promoting the ability of distributed generation ("DG") system manufacturers, distributors, marketers and investors, and electric customers, to deploy DG. Its members represent a variety of DG technologies including CHP, renewables, gas turbines, microturbines, reciprocating engines and storage. CCDC is currently comprised of Capstone Turbine Corporation, Cummins Inc., DE Solutions, EPS Corporation, Hawthorne Power Systems, Holt of California, Peterson Power Systems, RealEnergy, LLC, SDP Energy, Solar Turbines Incorporated, and Tecogen, Inc.

² Pub. Util. Code § 2840.6(a) and (b).

CHP recognized by the Legislature (and sought by the California Air Resources Board in the AB 32 Scoping Plan). The Proposed Decision provides no incentive for deployment of CHP pursuant to AB 1613, with the result that the state is no closer to achieving the vital goals of reduced GHG emissions and improved energy delivery.

CCDC urges the Commission to focus on the simple, clear goals of AB 1613 and modify the pricing methodology in the Proposed Decision in a manner that at least has a fighting chance of effectuating the Legislature's intent.

2. *The Pricing Proposal in the Proposed Decision is Contrary to the Goals of AB 1613.*

The Proposed Decision correctly recognizes that AB 1613 requires that CHP systems (1) "be sized to meet the eligible customer-generator's thermal load," and (2) "operate continuously in a manner that meets the expected thermal load and optimizes the efficient use of waste heat" in order to be eligible to sell excess energy to the investor owned utilities ("IOUs").³ The Proposed Decision further recognizes that "eligible CHP systems under this program are likely to operate as if they were a firm resource, in order to provide consistent thermal and electrical output to the host."⁴ These statements are consistent with California's "long history of CHP facilities," which "shows that CHP facilities of all sizes provide firm, reliable sources of generation."⁵ Nonetheless, the Proposed Decision would reduce by 60% the fixed cost component of Pricing Option 1.

CCDC agrees with the Proposed Decision that Pricing Option 1 is preferable to Pricing Option 2. Pricing Option 1 incorporates many of the inputs from the 2008 Market Price Referent ("MPR"). Unfortunately, the Proposed Decision would substantially reduce the 2008 MPR. Under the Proposed Decision, the price for excess energy would reflect just 40% of the fixed component of the 2008 MPR, plus a variable energy price component that is based on the product of the monthly bidweek burnertip gas price and the 2008 MPR model heat rate (*i.e.*, 6,924 Btu/kWh), plus a variable operations and maintenance adder of \$4.51 per MWh (for contracts starting in 2010). Without a 60% reduction in the fixed price component, eligible CHP

³ Proposed Decision, p. 35 (*citing* Pub. Util. Code § 2843(a) (2) and (3)).

⁴ Proposed Decision, p. 35.

⁵ Reply Comments of California Cogeneration Council, Energy Producers and Users Coalition, and Cogeneration Association of California, 9/3/09, p. 4.

would have received a price approaching the all-in costs of a combined cycle gas turbine (“CCGT”) modeled by the 2008 MPR.⁶

The Proposed Decision makes the faulty assumption that excess energy sold by eligible customer-generators to the IOUs is an as-available product that is not as valuable as a “fully dispatchable CCGT.”⁷ Relying on this faulty assumption, the Proposed Decision errs in not developing a price that reflects the firm supply of energy that small CHP will produce in aggregate. This error is notable, particularly considering that the Proposed Decision recognizes that eligible systems are likely to operate as if they were firm resources.⁸ CCDC fundamentally disagrees that sales of excess energy under AB 1613 should be assigned such a low value.

The Proposed Decision conflates excess energy sales and as-available capacity, with disastrous results. When new CHP is constructed at a site, an IOU avoids the need to provide a firm baseload supply of power to that site and to its customers who are served by the new CHP facility. Moreover, the aggregate production of excess electricity by many eligible CHP facilities can be counted on as a firm energy supply.

The Proposed Decision’s myopic focus on as-available contracts is not only erroneous, it is also poor policy. Neither the Order Instituting Rulemaking nor the Scoping Memo even hint that such a narrow focus is appropriate. Further, the Legislature clearly intended a different result. AB 1613 *requires* that the IOUs’ procurement plans incorporate cost effective, technologically feasible, and environmentally beneficial CHP solutions.⁹ Additionally, AB 1613 provides that the physical generating capacity of the CHP system *shall* count toward the resource adequacy requirements of IOUs.¹⁰ These requirements expressly implement the Legislature’s desire to realize the capacity value of eligible CHP. In light of the value of such capacity, eligible CHP should receive the full fixed capacity payment proposed by Energy Division.

In addition to this fundamental misunderstanding about the value of excess energy, which on its own is sufficient to justify rejection of the Proposed Decision’s 60% reduction in the fixed

⁶ CCDC notes that Finding of Fact 31 erroneously states that Energy Division staff proposes to apply an as-available capacity derating factor of 40%. Energy Division’s Final Staff Proposal contained no downward adjustment to the fixed component of the 2008 MPR. The only suggestion to apply a 40% derating factor came from San Diego Gas and Electric Company and Southern California Gas Company. (Comments of SDG&E and SoCal Gas, 8/24/09, pp. 3-6.)

⁷ Proposed Decision, p. 35.

⁸ Proposed Decision, p. 35.

⁹ Pub. Util. Code § 2842.

¹⁰ Pub. Util. Code § 2841(f).

component of the MPR, the Proposed Decision relies on an estimated value of as-available energy that is far too low. CCDC observes that the proposed 60% reduction is based on an out-of-date price for as-available energy, taken from D.07-09-040. That Decision adopted a firm capacity price of \$91.97 per kW-year and an as-available capacity price of \$32.53 per kW-year.¹¹ The as-available price adopted in D.07-09-040 was based on a combustion turbine (“CT”) with a capital cost of \$523 per kW.¹² This figure is woefully outdated. For example, the California Energy Commission’s August 2009 study, *The Comparative Costs of California Central Station Electricity Generation*, indicates an installed cost of at least \$1,277/kW for a sample of 50 MW CT units.¹³ Thus, the CT cost estimate that forms the basis of the Proposed Decision’s 60% reduction in the MPR fixed component is less than half the value of current CT cost estimates.

In essence, the Proposed Decision would adopt a combination of the low heat rate (6,924 Btu/kWh) for a new CCGT and a fixed component based on capital costs for a new CT unit. CT units, used to meet peak demands, are less expensive to build, but more expensive to run, than CCGT units. As a result, it is simply wrong to combine the lowest cost elements of each type of unit to calculate a price for sales under AB 1613. While a CT may be the least expensive unit to build to meet an increment of peak load, it is not what will be built to serve an increment of baseload demand, which is what CHP serves.

The pricing methodology in the Proposed Decision very likely will result in a price that is less than the price paid to traditional existing Qualifying Facilities (“QFs”). Assuming a \$6.00 per MMBtu burnertip price for natural gas, the Proposed Decision would result in a price of \$55 per MWh, whereas the energy and as-available capacity price paid to QFs would be 6% higher, at a price of about \$59 per MWh.¹⁴ This is an absurd outcome, and contrary to the direction in AB 1613 to encourage and support the development of new CHP capacity. Offering a price to

¹¹ D.07-09-040, pp. 96, 99.

¹² *Id.* at 96 and R.04-04-003, Exh. 149, App. B.

¹³ *The Comparative Costs of California Central Station Electricity Generation*, Table C-25 (CEC, 2009) (CEC-200-2009-017-SD; this report is available on the CEC’s web site:

<http://www.energy.ca.gov/2009publications/CEC-200-2009-017/CEC-200-2009-017-SD.PDF>.)

¹⁴ IER values contained in posted SRAC prices for October 2009 averaged 8,744 Btu/kWh for the three utilities. The Variable O&M Adder starts at \$4.43 per MWh in 2009 under the AB 1613 proposal, and is about \$2.80 per MWh in October 2009 for QF energy prices. The AB 1613 fixed price component of \$9.44 per MWh in 2009 compares to as-available capacity prices of \$32.53 per kWh for QFs, or about \$4.04 per MWh for a QF with a 92% capacity factor. Thus, the comparison is an AB 1613 price of \$56 per MWh = \$6/MMBtu x 8,677 Btu/kWh + 2.80/MWh + 4.04/MWh = \$59/MWh and a QF price of \$56 per MWh = \$6/MMBtu x 6,924 Btu/kWh + \$4.55/MWh + \$9.44/MWh.

new CHP that is lower than the price offered to existing CHP thwarts, rather than promotes, the important policy goals the Legislature seeks to achieve through increased installation of new clean CHP sized to meet thermal load.

CCDC also notes the importance of clearly identifying the Time of Delivery (“TOD”) factors in Appendix A. To the extent the TOD factors reflect a different mix of energy and capacity than in the AB 1613 price, it may be necessary to revise the applicable TOD factors to ensure that the blended TOD factors for energy and capacity reflect that mix, and adequately promote use of waste heat as envisioned in AB 1613. If capacity prices are significantly derated, TOD factors will need to recognize that fact, in order to preserve the appropriate allocation of energy prices to the TOD periods and, in particular, that the off-peak TOD factor is not too low to provide adequate incentives for using waste heat during nighttime hours.

The flawed assumptions and formulas used in the Proposed Decision result in a price that undervalues CHP output and provides a very poor price signal for CHP development, rendering the important goals of AB 1613 meaningless. CCDC strongly urges the Commission to reject the pricing methodology in the Proposed Decision and adopt Pricing Option 1 from the Energy Division Final Staff Proposal.

3. The Arbitrary and Erroneous Location Bonus Threshold Should Be Rejected.

In the July 31, 2009 “Energy Division Staff Proposal: Standard Contract Terms and Pricing for Eligible Combined Heat and Power (CHP) Systems \leq 20 MW,” staff proposed that eligible CHP located in a distribution or transmission constrained area receive a generation location bonus of 10%.¹⁵ The Proposed Decision appears to inadvertently misconstrue the staff proposal, providing that a 10% location bonus shall be applied to CHP located in areas where the nodal location marginal price (“LMP”) is 10% higher than the zonal LMP.¹⁶ The Proposed Decision provides no rationale for the requirement that the nodal LMP exceed the zonal LMP by 10% in order for the location bonus to apply.

CCDC is concerned that this arbitrary threshold will render the proposed location bonus meaningless. CCDC submits that a better approach would be to adjust all prices by the ratio of nodal to zonal average prices in the California Independent System Operator (“CAISO”) energy market. This would either reward or penalize a CHP project based on its location. In addition,

¹⁵ Energy Division Staff Proposal: Standard Contract Terms and Pricing for Eligible Combined Heat and Power (CHP) Systems \leq 20 MW, pp. 11-12.

¹⁶ Proposed Decision, p. 37.

an upward adjustment is needed for CHP facilities that locate on the distribution system, beyond the CAISO-controlled transmission system, because such facilities also reduce line losses on the distribution system, as recognized in the distribution line loss factors in the IOUs' existing Wholesale Distribution Access Tariffs. Without such an adjustment, the Proposed Decision would assign no value to CHP facilities that interconnect to the utility distribution system rather than the higher-voltage transmission system.

4. *Eligible CHP Must Be Compensated for GHG Emission Reductions.*

CCDC supports the conclusion in the Proposed Decision that GHG compliance costs should be passed through to the buyer of excess energy, *so long as* the Commission adopts Pricing Option 1 as proposed by Energy Division (*i.e.*, without a 60% reduction in the fixed price component).

CCDC is concerned that the reduced price in the Proposed Decision does not accurately reflect the value of the GHG emissions reductions associated with eligible CHP systems. For example, AB 1613 explicitly recognizes the potential of CHP to reduce GHG emissions.¹⁷ Additionally, the California Air Resources Board's ("CARB") *Climate Change Scoping Report* sets a target of adding 4,000 megawatts of new CHP capacity to reduce GHG emissions by 6.7 million metric tons of carbon by 2020.¹⁸

If CHP is to be part of the solution to climate change issues, as envisioned by the Legislature in AB 1613 and CARB, then the price paid for excess energy under AB 1613 must account for the value of CHP-related GHG emission reductions. Energy Division's proposed Option 1 arguably implicitly captures at least some of that value (and so a cost pass-through is appropriate). The Proposed Decision's approach to pricing does not. It is arbitrary and unreasonable to require sellers of excess energy under AB 1613 to transfer GHG benefits to the buyer for no compensation. The Proposed Decision's unsupported assertion that GHG emission reductions cannot be calculated only for excess energy deliveries is incorrect. A calculation could in fact be developed to apportion GHG reductions between energy consumed on-site and excess energy delivered to the buyer.

In order to ensure the seller is compensated for the value of GHG emission reductions associated with energy delivered to the purchasing utility where the price for excess energy is

¹⁷ Pub. Res. Code §§ 2840.6(b), 2845.

¹⁸ *Climate Change Scoping Plan*, pp. 43-44 (CARB, 2008); this report is available on CARB's web site: http://www.arb.ca.gov/cc/scopingplan/document/adopted_scoping_plan.pdf.

lower than Pricing Option 1 as proposed by Energy Division, the Proposed Decision should be revised to include an adder for the GHG emission reduction benefits associated with eligible CHP, such as the GHG adder forecast contained in the MPR model. Alternatively, CCDC requests that the Commission adopt Energy Division's Pricing Option 1, with the GHG cost pass-through.

5. *Eligible CHP Must Be Compensated for Other Green Attributes.*

The Proposed Decision concludes that the value of other green attributes are included in the price proposed in the Proposed Decision and, therefore no increase in the price is required to reflect the value of green attributes.¹⁹ CCDC disagrees that the proposed price contains any, much less an adequate, value for other green attributes. It is poor policy to effectively exclude renewable CHP from an AB 1613 program where such CHP furthers the efficiency goals of AB 1613.

A seller should be compensated for the products it delivers to a buyer. Here, if the Commission determines that all of the benefits associated with the use of renewable fuel should be conveyed by seller to buyer, then CCDC requests that the AB 1613 contract provide that buyer must compensate seller for such benefits at market prices, or contain some other mechanism to ensure that the seller is fully compensated for using renewable fuel. The input of CARB and/or the California Energy Commission should be sought regarding a verified GHG reduction calculation methodology for CHP systems on renewable fuels.

6. *It is Appropriate to Further Simplify the Simplified Contract for Systems Less Than 500 kW.*

CCDC has noted that some of its members operate CHP systems that are 500 kilowatts ("kW") or less ("very small CHP").²⁰ Such systems have minimal, if any, effect on the distribution system, and are not even required to be scheduled with the California Independent System Operator ("CAISO"). Accordingly, CCDC has requested that the Commission adopt an even simpler AB 1613 contract, *or identify specific provisions of the simplified contract that do not apply to very small CHP*, to efficiently and equitably address the concerns of very small CHP customers and the utilities.²¹

¹⁹ Proposed Decision, pp. 47-48.

²⁰ Comments of CCDC Regarding Energy Division Final Staff Proposal, p.3.

²¹ *Id.* See also, CCDC Comments, 6/1/09, p. 6 and CCDC Comments Regarding Simplified AB 1613 Contract, 7/10/09, pp. 9-10.

7. Conclusion.

CCDC respectfully requests that the Commission revise the Proposed Decision as set forth herein. Proposed Findings of Fact and Conclusions of Law are set forth in Appendix A hereto.

DATED: November 19, 2009

DAY CARTER & MURPHY LLP

By: /s/ Ann L. Trowbridge
Ann L. Trowbridge

APPENDIX A

Proposed Findings of Fact and Conclusions of Law

Findings of Fact

New 28. The long history of CHP facilities in California shows that CHP facilities of all sizes provide firm, reliable sources of generation.

29. Eligible systems under this program are likely to operate as if they were a firm resource, in order to provide consistent thermal and electrical output to the host. ~~Since the thermal requirements of the host customer may vary, the excess electricity produced by an eligible CHP facility may also vary.~~

Delete 30.

Delete 31.

40. CCDC has ~~not~~ presented persuasive arguments to justify the need for an even more simplified contract.

51. Pricing Option 1 as set forth in Energy Division's Final Staff Proposal includes some value of ~~for~~ the green attributes associated with the excess electricity delivered to the grid.

Conclusions of Law

Delete 9.

10. Staff's proposal to include a 40% location bonus to encourage optimal siting of CHP facilities should be adopted.

11. Prices should be adjusted by the ratio of nodal to zonal average prices in the CAISO energy market and an upward adjustment should be applied for facilities that locate on the distribution system, beyond the CAISO-controlled distribution system. ~~The location bonus should be applied if an eligible CHP system locates in an area where the nodal day-ahead price is 10% higher than the zonal price, when averaged over the summer peak period for each IOU.~~

New: It is reasonable to identify certain provisions of the simplified contract that do not apply to systems participating in the AB 1613 program that are 500 kW or less in size.

CERTIFICATE OF SERVICE

I, Paula S. Hefley, hereby certify that I served a copy of the **COMMENTS OF THE CALIFORNIA CLEAN DG COALITION REGARDING PROPOSED DECISION ADOPTING POLICIES AND PROCEDURES FOR PURCHASES OF EXCESS ELECTRICITY UNDER ASSEMBLY BILL 1613** on November 19, 2009, on all known parties to Service List for r.08-04-024 via electronic mail to those whose addresses are available and via U.S. mail to those who do not have an electronic address as follows:

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The Honorable Amy C. Yip-Kikugawa
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I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Executed on this 19th day of November, 2009, at Sacramento, California.

/s/ Paula S. Hefley

PAULA S. HEFLEY

AMENDED
CERTIFICATE OF SERVICE

I, Paula S. Hefley, hereby certify that I served a copy of the **COMMENTS OF THE CALIFORNIA CLEAN DG COALITION REGARDING PROPOSED DECISION ADOPTING POLICIES AND PROCEDURES FOR PURCHASES OF EXCESS ELECTRICITY UNDER ASSEMBLY BILL 1613** on November 20, 2009, on all known parties to Service List for R.08-06-024 via electronic mail to those whose addresses are available and via U.S. mail to those who do not have an electronic address as follows:

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The Honorable Amy C. Yip-Kikugawa
California Public Utilities Commission
Division of Administrative Law Judges
505 Van Ness Avenue, Room 2106
San Francisco, CA 95102-3214

I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Executed on this 20th day of November, 2009, at Sacramento, California.

/s/ Paula S. Hefley
PAULA S. HEFLEY