BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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Order Instituting Rulemaking to Develop Additional Methods to Implement the California Renewables Portfolio Standard Program.	Rulemaking 06-02-012 (Filed February 16, 2006)

POST-WORKSHOP REPLY COMMENTS OF AGLET CONSUMER ALLIANCE ON TRADABLE RENEWABLE ENERGY CREDITS

Pursuant to the October 16, 2007 ruling (Ruling) of Administrative Law Judge (ALJ) Anne Simon, Aglet Consumer Alliance (Aglet) submits these post-workshop reply comments on the use of tradable renewable energy credits (TRECs) in the California Renewables Portfolio Standard (RPS) program. Several parties filed opening comments on November 13, 2007. Reply comments are due Wednesday, December 5, 2007. Aglet will file this pleading electronically on the due date.

1. Overview

Aglet has three major questions about the concept of tradable RECs that are unbundled from energy. These concerns are:

1. Will REC trading interfere with the goal of procurement of additional renewable power? That is, will some entities buy renewable credits as a substitute for procuring renewable power?
2. How will the Commission protect the interests of bundled service ratepayers are if RECs are traded?
3. Will TRECs result in the development of new renewables resources in California?

Two facts have emerged from the recent workshops: (1) entities will purchase TRECs as a substitute for procuring renewable power; and (2) TRECs will increase ratepayer risk. Therefore, Aglet recommends that the Commission not authorize TRECs for compliance purposes.

Aglet does not believe that the trading of RECs will have a significant positive impact on the development of new renewable resources in California. If the investor-owned utilities (IOUs) purchase RECs and the moneys paid by IOUs are recovered in rates, the trading of RECs will constitute an additional subsidy of existing renewable resources by ratepayers. RECs are not analogous to long-term renewables contracts because ratepayers receive neither an energy benefit nor an economic benefit from the trading of RECs. California already subsidizes the development of some renewable resources through supplementary energy payments, the California Solar Initiative and the Emerging Renewables Program.

Before the Commission establishes an additional subsidy, it should determine: (a) whether or not the subsidy is legal; and (b) whether or not the subsidy is justified by the economic condition of renewable developers. A subsidy may be justified if existing renewable plants are facing imminent economic failure. Currently, there is no information in the record of this proceeding to support that proposition.

2. Effect of TRECs on Development of Renewables

Calpine has pointed out:

> Uncertainty is a barrier to investment and the boom/bust cycle inherent in the spot tradable REC market, as discussed by Dr Weiss, could add uncertainty to the life cycle value of new investments in renewable resources. This risk will become more significant if investor owned utilities ("IOUs") and other large LSEs decide to procure most (rather than a residual amount) of their RPS obligations from a spot tradable REC market. In such a case, investors will have to rely on the volatile price signals from this spot market for RECs in order to recover their investments and the uncertainty created by that bimodal pricing outcome could

> make funding of such projects more difficult. (Calpine Comments, p. 2.)

The Independent Energy Producers Association (IEPA) argues that:

> We may not know for sure whether contracts for RECs during the 2008-2011 timeframe will provide necessary additional resources, but not knowing that answer precisely in advance is no reason not to implement the policy and see if it is helpful. (IEPA Comments, p. 14.)

Ratepayers should not be exposed to a risky TREC experiment. If the Commission allows TRECs to be used for compliance purposes, ratepayers will pay the cost of the TRECs, regardless of how high the cost. The Commission has an obligation to protect ratepayers from unnecessary risks such as TREC risks and should not conduct another market experiment like the one that led to the California financial crisis of 2000 and 2001.

3. The Price Cap

The Energy Division's Straw Proposal suggests a price cap of $35 per megawatt-hour (MWh) for TREC transactions. The Commission has previously adopted an upfront and automatic penalty of five cents per kilowatt-hour for failure to meet annual procurement targets, with an overall annual penalty cap of $25 million. (See Decision 03-06-071, Ordering Paragraph 23, slip op. at 74.)

Calpine argues that the $35/MWh price cap may be too low:

> The $35/REC price cap proposed in the Straw Proposal is based on recent contracts for renewable energy and does not take into account rising costs of new supplies. In addition, such a price cap ignores that the cost to develop new renewable resources going forward will increase as the best locations for renewable development are developed. (Calpine Comments, p. 2.)

Calpine also points out, "IOUs will have an incentive to drive the price of RECs above the penalty rate if shareholders bear the cost of the penalty but ratepayers bear the cost of REC purchases." (Calpine Comments, p. 4.)

The Center for Energy Efficiency and Renewable Technologies (CEERT) argues that "*no price cap* be placed on REC procurement prices." (CEERT Comments, p. 14, emphasis in original.)

The Joint Solar Parties argue that "the best course of action is to set up a clear, transparent market for RECs, encouraging as many participants as possible to ensure liquidity, and then only intervene in that market if a clear market failure occurs." (Joint Solar Parties Comments, p. 5.)

Aglet strongly disagrees with the standard suggested by the Joint Solar Parties. The Commission should attempt to anticipate future problems, and not passively wait for the next crisis to arise.

If the Commission allows TRECs, it must protect ratepayer interests by establishing an absolute maximum price cap, and it must not allow IOUs to recover costs above that cap. If the Commission fails to do so, TREC prices will quickly rise to the penalty amount of $50/MWh as suggested by Dr. Jurgen Weiss. (Ruling, Attachment C, p. 4.)

4. RPS and REC Supply

Evolution Markets (Evolution) argues, "TRECs will necessarily INCREASE the available supply, and thus, will have a balancing effect on the current supply/demand imbalance." (Evolution Comments, p. 5.) TRECs only exist when a plant begins commercial operation. Therefore, TRECs will have no effect on the existing supply/demand imbalance.

Evolution also claims that "almost all REC markets (Massachusetts, Rhode Island, and Connecticut are the exceptions) have lower renewable pricing than California and Arizona." (Evolution Comments, p. 8.) Evolution bases this statement on its experience and proprietary data. Because the data are proprietary, Aglet is unable to confirm whether California and Arizona have higher renewable pricing than other states.

Pacific Gas and Electric Company (PG&E) argues:

> In addition, PG&E questions how relevant Dr. Jurgen Weiss' analysis of the elasticity of REC supply and demand and its effects on REC prices is for the California market. Given that RECs would not be the sole RPS compliance mechanism for most LSEs, and given California's flexible RPS banking and compliance rules, market participants will never know with certainty what supply or demand for RECs will be in any given year. Consequently, demand for RECs will be much more elastic than Dr. Weiss postulates and the boom-bust cycle he predicts is unlikely to occur in California. (PG&E Comments, p. 2.)

PG&E misunderstands Dr. Weiss' analysis. The boom-bust cycle observed by Dr. Weiss is not dependent on perfect information on the part of market participants. If extreme price spikes were a function of perfect information, commodity markets would provide consistently low and stable prices.

Dr. Weiss points out that the "boom-bust feature of markets created by fixed demand created by regulatory mandate is not new – it has been prominent in capacity markets for energy for a while, and the discussion of how to address the problem in those markets has been active." (Ruling, Attachment C, p. 6.) There is no reason to believe that a California TREC market would not also be characterized by a boom-bust cycle.

Southern California Edison Company (SCE) argues:

> Furthermore, and as discussed in more detail below, Dr. Weiss's assumption of a perfectly inelastic demand curve based on an ACP is fundamentally incorrect. California's RPS program is not based on an ACP [Alternative Compliance Payment] scheme. Instead, California LSEs are potentially subject to penalties and cumulative deficits from past shortfalls. Under such a scheme, the LSEs have the perverse incentive to pay any amount for RECs in order to avoid a penalty. Thus, unlike the demand curve set forth by Dr. Weiss, the demand curve for RECs in California will not be perfectly inelastic at an ACP or even a penalty amount. (SCE Comments, p. 9.)

SCE's analysis ignores the fact that IOUs have the ability to spend ratepayer dollars in order to avoid shareholder penalties. The economic effect of an ACP is no different from the Commission's existing non-compliance penalty system. Thus, SCE's statements about an ACP scheme are also relevant to California. That is, IOUs have an incentive to pay any amount for RECs in order to avoid a penalty.

5. TREC Risk

IEPA argues, "Non-compliance penalty costs should be borne by shareholders." (IEPA Comments, p. 13.) Unfortunately, this is not possible. Aglet is concerned that IOUs will have the option of spending ratepayer money for high-priced TRECs in order to avoid shareholder penalties. Therefore, ratepayers not shareholders are effectively paying for compliance penalties.

The IEPA also argues:

> RECs should not be viewed as a tool that increases ratepayer risk. The mere fact that RECs may be used for RPS compliance purposes does not, per se, suggest greater ratepayer risk. Rather, RECs provide relatively cost effective means to achieve RPS goals in light of delivery requirements. (IEPA Comments, p. 13.)

Aglet disagrees. RECs increase ratepayer risk when compared to RPS contracts. RPS contracts typically offer energy on a long-term, fixed price basis. TREC prices are highly volatile and may cost up to $50/MWh in California. Ratepayer risk will increase if volatile TREC prices replace fixed-price RPS contracts.

Energy Current has reported:

> Christian Blattenberger, manager of energy procurement at Cadence Network, a consulting firm in Cincinnati that specializes in helping companies manage energy costs, expects the average price of renewable energy credits to double or even triple within the next three years.

* * *

> The price of a generic REC has risen approximately 35% over the past 12 months, while the cost of more certifiable credits has nearly doubled, according to Blattenberger. (Jennifer Zajac, "Consultant expects REC prices to soar within next three years," Energy Current, October 31, 2007, copy attached to this pleading.)

6. Hedge Value of Renewables

Central California Power (CCP) incorrectly states:

> The only way RPS procurement can become an effective hedge against natural gas price volatility is in the event renewable energy negates the need for natural gas fired generation. That is not viable in the foreseeable future. At present there is only a small percentage of "reliable renewable energy" even being conceived, the greatest percentage of renewable energy is As Generated. (CCP Comments, p. 6.)

Renewable energy contracts reduce an IOU's overall need. Because the vast majority of an IOU's energy and capacity needs are filled through contracts with natural gas-fired plants, any renewables contract will effectively reduce an IOU's exposure to volatile natural gas prices. The fact that many renewables contracts provide energy on an as-generated basis does not reduce the hedge value of renewables contracts.

Renewables contracts typically offer a fixed price with contract durations of 10 to 30 years. RPS contract prices are not based on the spot price of natural gas. In contrast, the prices of non-renewables contracts are typically based on the spot price of natural gas. For example, an IOU might sign a must-take contract with a generator in which the IOU will buy electricity on a given day at ten times the natural gas price plus a fixed price. Natural gas prices change quickly, and thus total contract prices of a non-renewables project are unknown.

Renewables contracts reduce an IOU's exposure to natural gas price risk in two ways: (1) they reduce an IOU's need to buy energy from gas-fired plants; and

(2) fixed-priced RPS contracts reduce the overall commodity price risk of an IOU's portfolio.

7. TREC Evaluation

CEERT recommends that the IOUs select TRECS by comparing TRECS to renewables contracts using a least-cost best-fit analysis. (CEERT Comments, p. 15.) Aglet doubts that it is possible for the IOUs to make such a comparison. In part, RPS contracts are evaluated by comparing the cost of the RPS contract to actual or expected forward prices. Aglet is unaware of any organization that publishes forward prices for TRECs. If the Commission authorizes the use of TRECs, each IOUs will have to use its best judgment in determining which TRECs to select in a given solicitation.

8. Conclusion

For the reasons stated above, the Commission should not adopt a system of TRECs that can be used for RPS compliance purposes.

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Consultant L. Jan Reid drafted this pleading on Aglet's behalf.

Dated December 5, 2007 at Cool, California.

/s/

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ATTACHMENT

"Consultant expects REC prices to soar within next three years"

Energy Current, October 31, 2007

CERTIFICATE OF SERVICE

I certify that I have by electronic mail this day served a true copy of the original attached "Post-Workshop Reply Comments of Aglet Consumer Alliance on Tradable Renewable Energy Credits" on all parties of record in Rulemaking (R.) 06-02-012, R.06-03-004, R.06-04-009, and R.06-05-027, or their attorneys of record. I have served paper copies of the pleading on Assigned Commissioner Michael Peevey, Administrative Law Judge Anne Simon, and nine parties for which no e-mail address is listed on the Commission's website: David Coyle, Anza Electric Coop, 58470 Highway 371, Anza, CA 92539; William Cronin, Energy America LLC, One Stamford Plaza, 8th Floor, Stamford, CT 06901; Larry Eisenstadt, Dickstein Shapiro LLP, 1825 Eye Street, Washington DC 20006; Donald Furman, PPM Energy Inc., 1125 NW Couch Street, Suite 7700, Portland, OR 97209; Richard Lehfeldt, Dickstein Shapiro LLP, 1825 Eye Street, Washington DC 20006; Jeanne McKinney, Thelen Reid, 101 Second Street, Suite 1800, San Francisco, CA 94105; Michael Meacham, City of Chula Vista, 276 Fourth Avenue, Chula Vista, CA 91910; Terence Parker, United Solar Ovonic LLC, 3800 Lapeer Road, Auburn Hills, MI 48326; and Andy Wuellner, Mountain Utilities, PO Box 1, Kirkwood, CA 95646.

Dated December 5, 2007 at Cool, California.

/s/

James Weil