

**PUBLIC UTILITIES COMMISSION**

505 VAN NESS AVENUE  
SAN FRANCISCO, CA 94102-3298

January 3, 2012

TO PARTIES OF RECORD IN RULEMAKING 11-05-005.

At the Commission Meeting of December 15, 2011, Commissioners Michael R. Peevey and Timothy Alan Simon stated that they would file concurrences in Decision 11-12-052. The decision was mailed on December 21, 2011.

The concurrence of Commissioner Michael R. Peevey is now available and is attached herewith.

/s/ KAREN V. CLOPTON  
Karen V. Clopton, Chief  
Administrative Law Judge

KVC:lil

Attachment

**Concurrence of Commissioner Michael R. Peevey on Item 47,  
Decision 11-12-052**

I believe as a general principle that regulatory flexibility tends to achieve regulatory goals at lower cost. When we contemplate various constraints to the way entities may comply with the regulatory regimes we create, we should think carefully about whether the objectives the restrictions are intended to achieve are worthwhile, whether the restrictions are necessary to achieve the objectives, and whether other options may achieve the objectives at lower cost. The restrictions on the use of tradable Renewable Energy Credits (RECs) advocated by some parties do not meet these tests. Many of the efforts to limit the role of open and liquid REC markets in the Renewables Portfolio Standard (RPS) program seem to stem from three misplaced fears: one, that REC marketers and brokers will exercise market power and drive up compliance costs; two, that use of unbundled RECs necessarily undermines the long-term hedging value of fixed-price renewable energy; and three, that giving retail sellers the option of relying on unbundled RECs will undermine the overall attainment of the RPS target because retail sellers will refuse to sign the long-term contracts that renewable energy project developers need to secure financing. Rather than tackle these issues directly, parties that seek to minimize the role of tradable RECs in the RPS program would throw the baby out with the bathwater.

As originally issued, the proposed decision would have restricted the use of unbundled RECs in two ways that I found objectionable because I believe they would increase the cost of compliance with no offsetting benefit. The first objection is that the proposed decision would have imposed unnecessary requirements for transactions to qualify for Category 2, the firming and shaping category. I appreciate revisions to the proposed decision that relaxed some of these requirements. In particular, I am glad to see a clarification that parties other than California retail sellers may serve as intermediary providers of the energy and RECs from out of state facilities. I also support other changes eliminating the requirement that contracts for substitute energy be filed concurrently with the firmed and shaped renewable energy contract, at least for electric service providers (ESPs) and community choice aggregators (CCAs). The revised decision allows these retail sellers to execute the initial contract for substitute energy at any time prior to the first date of deliveries under the contract with the renewable facility, providing additional flexibility to structure firming and shaping deals. However, I am concerned that the revised decision

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imposes a simultaneous contract submission requirement and minimum substitute energy contract duration on the utilities but not ESPs and CCAs.

Commissioner Ferron and Administrative Law Judge (ALJ) Simon properly rejected some parties' requests to impose additional restrictions, such as suggestions that substitute energy must come from the same subregion of the Western Electricity Coordinating Council interconnect, that the substitute energy contract must offer fixed-price energy, or that the substitute energy contract must cover the same duration as the renewable energy contract. These efforts to tightly constrain the procurement activities of California's retail sellers are, in my view, misguided and would almost certainly raise the overall cost of compliance.

Because the hedging value of renewable energy has been a particular concern to some parties, I will elaborate on my reasons for opposing a fixed-price substitute energy requirement on firming and shaping transactions. First, negotiating a contract for fixed-price substitute energy is not necessary for California retail sellers to extract the long-term hedging value from out-of-state renewable facilities. California retail sellers may simply purchase the electricity from out-of-state facilities at a fixed-priced and resell it at the market price. If the market price rises over the long-term, the cost of substitute energy will rise, but those costs will be offset by increasing revenues from the resale of energy from the renewable facilities. Second, the long-term price stability of most sources of renewable energy may offer some hedging value, but determining how much that hedging value is worth rests on extremely speculative predictions about the cost of electricity from other sources ten to twenty years in the future. Third, evaluating the value of deals that do provide price stability versus those that do not may be complex, but prohibiting all firming and shaping transactions that do not provide long-term price stability is a blunt response to that complexity. ESPs and CCAs should be allowed to make that determination for themselves. As for the investor-owned utilities, the Commission may need to refine its methodologies to compare the costs and benefits of arrangements that provide price stability to those that do not when it evaluates firming and shaping deals.

The second objection I had to the proposed decision is that it would require all RECs used for Category 1 compliance to be purchased on a bundled basis. All unbundled RECs would fall in Category 3, even if the RECs are associated with deliveries of electricity that otherwise meet the criteria of Category 1. While I appreciate Commissioner Ferron's willingness to collaborate

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with me on this decision, I am disappointed that we could not reach agreement on this issue. Commissioner Ferron and ALJ Simon maintain that all unbundled RECs should be relegated to Category 3 because they believe there is stronger support for that position based on statutory interpretation and the legislative history. However, I believe the statute is ambiguous as to whether all unbundled RECs must be placed in Category 3, and prohibiting the use of any unbundled RECs for Category 1 will increase compliance costs for no discernable purpose.

Placing all unbundled RECs in Category 3 is likely to increase costs because doing so reduces compliance flexibility. Retail sellers needing to buy a Category 1 compliance product must purchase the underlying electricity as well as the associated RECs regardless of whether the buyer actually needs the underlying electricity or whether the underlying electricity is the lowest-cost option to meet the buyer's load. Additionally, because the ultimate user of the Category 1 RECs must buy the underlying electricity in real time, this restriction eliminates the opportunity for any *ex post* transactions to achieve Category 1 compliance. Retail sellers who are short on Category 1 RECs must anticipate their short positions and find a willing seller in advance because once a MWh of electricity has been generated, any subsequent use of the associated REC would be considered Category 3.

I expect that retail sellers will adapt to these needless restrictions by finding relatively efficient ways to exchange bundled products. This may entail arrangements under which the buyers purchase the bundled energy and RECs and, if the buyer does not need the energy to meet its load requirements, it will simply resell the energy to another entity or into the California Independent System Operator market. In the end, the same amount of energy from directly connected facilities and imports meeting the Category 1 criteria will be produced while higher costs result from these redundant electricity transactions.

If the legislature introduces a clean up bill for SB 2 1X, I would like to suggest that it consider clarifying whether unbundled RECs may qualify for Category 1. I note that the criteria listed in Sec. 399.16(b)(1) pertain to the nature of the facilities and their deliveries of electricity to a California balancing authority - namely, that the electricity must be delivered in real-time by virtue of being directly connected or having a dynamic transfer agreement in place or, if neither condition applies, the electricity must be delivered within the hour it is generated. Nothing in this section of the statute describes the contractual

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relationship between an RPS-eligible facility and the ultimate retail seller using its RECs. If the legislature wants to ensure that a certain percentage of the RPS goal is met with electricity delivered to a California balancing authority within an hour or less of being generated as required by this section, it can clarify that the percentages indicated in this section of the statute be met by RECs, whether bundled or unbundled, associated with such deliveries. This revision would provide additional compliance flexibility while ensuring that the product category procurement targets are still met.

While I strongly support Category 1 permanence for RECs associated with deliveries of electricity meeting the Category 1 criteria, I have concluded that it is preferable to vote out the decision now rather than issue an alternate decision and prolong the uncertainties hanging over retail sellers and renewable energy markets. It is time to resolve this matter and give the market some certainty about the structure of the RPS program as it applies to the retail sellers under our jurisdiction.

Date January 3, 2012, at San Francisco, California.

/s/ MICHAEL R. PEEVEY  
Michael R. Peevey  
Commissioner