

Decision 06-02-011 February 16, 2006

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking Regarding Policies,
Procedures and Incentives for Distributed
Generation and Distributed Energy Resources.

Rulemaking 04-03-017
(Filed March 16, 2004)

**OPINION DENYING THE PETITION OF TECOGEN, INC.
FOR MODIFICATION OF DECISION 04-12-045**

This order denies the petition of Tecogen, Inc. (Tecogen), for modification of Decision (D.) 04-12-045 to increase incentive payments for certain distributed generation projects to \$1 per watt.

Background

This proceeding was established to develop and oversee a program for providing incentives to distributed generation technologies of all kinds. In this proceeding, the Commission has set incentive levels, developed interconnection rules, set target funding levels for each qualifying technology and implemented legislation designed to promote air quality standards for distributed generation projects, among other things. We have referred to this program as the "Self-Generation Incentive Program," or SGIP.

D.04-12-045 reduced incentive levels for all technologies because the SGIP program overall had been oversubscribed, suggesting some incentives were higher than they needed to be to motivate investment. Among other things, the decision reduced the incentives from \$1 per watt to \$.80 per watt for nonrenewable projects.

Tecogen's petition asks the Commission to reinstate previous incentive levels of \$1 a watt for "Level 3" technologies, which are microturbines, internal combustion engines, and small gas turbines. It believes the higher incentives are justified because the price of natural gas has increased substantially since the issuance of D.04-12-045 and because related projects are now subject to more stringent air quality rules.

Tecogen's Petition to Modify

Tecogen's petition asks the Commission to reinstate the previous level of incentives at \$1 per watt for Level 3N technologies not utilizing renewable fuel, as adopted in D.01-03-073 and modified in D.02-09-051. D.04-12-045 set them at \$.80 a watt and adopted air emission standards set forth in Assembly Bill (AB) 1685. Tecogen believes the previous funding levels for Level 3N technologies are justified because natural gas prices have increased in the past two years and because California efficiency and emission requirements for Level 3 technologies are more stringent than they have been in the past.

Tecogen observes the Commission's order set SGIP levels for renewable technologies based on previous installation cost experience; customer subscription levels; ability to meet ultra-clean emissions; overall efficiency criteria; as well as an exit strategy that would wean technologies off the incentive program over time.

Tecogen states that members of the SGIP Working Group reported that the new incentive levels were established based on "historical SGIP installation cost data which demonstrated that the installation costs for microturbines were higher than the installed costs for engine systems." Tecogen states that the statewide SGIP statistics posted through January 2004 on the San Diego Regional Energy Office (SDREO) website not support this conclusion. Tecogen suggests

the difference in the cost of microturbines and comparably-sized internal combustion engine systems is very small. It believes the discrepancy in incentives for these two technologies is inequitable and discriminatory and, therefore, will not serve the overall objective of the Commission to encourage the widespread installation of distributed generation technologies in the State of California. Tecogen states Level 3-N technologies have been undersubscribed for the last four years by over \$30 million,¹ supporting its view that incentive levels will not stimulate market demand for CHP technologies.

Response of Parties

The SGIP Working Group (comprised of Southern California Edison Company (SCE), Pacific Gas and Electric Company (PG&E), San Diego Gas and Electric Company (SDG&E), the SDREO and the staff of the California Energy Commission) filed a response to Tecogen's petition, objecting to its proposal. The Working Group observes that at the existing incentive level of \$.80 per watt, the SGIP has awarded more than \$40 million to Level 3N projects and that increasing the incentive to \$1 per watt would have increased the total pay-out by more than 50% without increasing the power supply or benefits to ratepayers.

¹ The following reallocations for Level 3 have been posted for 2001 - 2004 on the following websites: pge.com/selfgen/; socialgas.com/business/selfgen/; sce.com/RebatesandSavings/SelfGenerationProgram/; sdeenergy.org/; energy.ca.gov/distgen; cpuc.ca.gov/static/Industry/electric/distributed+generation/index.htm.

In total (Statewide), Level 3 technologies were under-subscribed by \$31.2 million:

SCG	+10.5 million
SDREO	-10.2 million
SCE	-13.1 million
PG&E	-18.7 million

The Working Group also states the data show that the median incentive for Level 3N internal combustion engines is \$.64. It believes the Commission should await a cost-benefit analysis to determine whether to modify the existing incentives for Level 3N technologies.

Ingersoll Rand Energy Systems (Ingersoll-Rand) also objects to the petition to modify, arguing that the differential the Commission adopted between internal combustion projects and microturbines is justified, contrary to Tecogen's assertion because internal combustion projects employ a mature technology, while microturbines are still being developed.

Discussion

The existing incentive levels for distributed generation technologies are not perfect but they are a reasonable estimate of the level of incentives required to motivate investment in distributed generation projects. Tecogen has not made a convincing case to increase incentives to projects for fossil fuel-based projects. Tecogen's view that we should increase incentives to account for increases in natural gas prices is logical if our only objective is to increase supply. However, we also consider the longer term impacts on utility customers of increasing gas-fired generation. From that standpoint, increases in natural gas prices actually justify phasing out or reducing incentives to projects using natural gas fuels in favor of projects that rely on alternative resources.

We also decline to increase incentives on the basis that Level 3 projects are subject to more stringent air quality standards. Nothing in AB 1685 suggests the Legislature intended projects that create air pollution to be compensated by way of SGIP incentives for the costs of reducing that pollution. In general, Tecogen has presented no evidence to suggest a 20% increase in incentives is required at this time to maximize cost-effective investments in Level 3N projects.

We retain our option to reconsider incentive levels at a future date but decline to increase them at this time based on Tecogen's Petition.

Assignment of Proceeding

Michael R. Peevey is the Assigned Commissioner and Kim Malcolm is the assigned Administrative Law Judge (ALJ) in this proceeding.

Comments on Draft Decision

The draft decision of the ALJ in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7 of the Rules of Practice and Procedure. Comments were received and the Commission did not change this decision in response to parties' comments.

Findings of Fact

1. Increases in natural gas prices do not justify incentives that would promote more investment in natural gas projects.
2. AB 1685 does not state an intention that the costs of the air quality regulations it imposes should be offset by higher SGIP incentives.
3. Tecogen has not made a convincing case for increasing incentives to Level 3 SGIP projects.

Conclusion of Law

The Commission should deny the petition to modify D.04-12-045 filed by Tecogen on February 22, 2005.

O R D E R

IT IS ORDERED that the Petition to Modify Decision 04-12-045 filed by Tecogen, Inc. on February 22, 2005, is denied.

This order is effective today.

Dated February 16, 2006, at San Francisco, California.

MICHAEL R. PEEVEY

President

GEOFFREY F. BROWN

DIAN M. GRUENEICH

JOHN A. BOHN

RACHELLE B. CHONG

Commissioners