

long-term contracting by entities possessing that capability. And obviously, prohibiting RECs will in no way ensure that ESPs are able sign long-term contracts.

TURN cites an LBNL report in supporting its statement that long-term contracting “has suffered under a REC trading system.” (TURN, at p. 10) But the report contains no cause-and-effect conclusion. While there has indeed been a lack of long-term contracts in some other states which has created problems in financing new renewables development, the problem stems not from the availability of RECs, but rather from weaknesses in the states’ RPS laws and regulations. Among the problems cited by the LBNL report in the case of Massachusetts, for example, is that the “provider of last resort” (PLR) is allowed to pay a fee in lieu of compliance which it may pass through to the ratepayers (i.e., there are no real non-compliance consequences). The PLR has also been unable (or unwilling) to sign long-term contracts and regulators have failed to encourage them to do so.¹

Enabling the tradability of RECs would not undermine long-term contracting. The utilities will still have that ability (and the Commission should ensure that they use it²) and they, and ESPs, will have a natural incentive to employ long-term contracting as a price hedge against potentially volatile spot REC prices. What the Commission and the ESPs need to assess is whether there will be sufficient RECs in the market to enable ESP compliance. These RECs could come from the substantial number of existing facilities that will come off of their QF contracts over the next several years, from new merchant facilities, or from “excess” utility RECs. The Commission also needs to take measures to foster the availability of RECs, such as making noncompliance penalties automatic, which will provide the impetus to ESPs to procure RECs (which, in turn, should promote merchant development). If, despite these measures, and the good-faith compliance efforts of the ESPs, there remains a significant risk that insufficient RECs will

¹ *Evaluating Experience with Renewables Portfolio Standards in the United States*, by Ryan Wisser, Robert Grace, and Kevin Porter, Lawrence Berkeley National Laboratory, LBNL-54439, March 2004, p. 20 (as clarified by Ryan Wisser in a personal communication, February 11, 2005).

² The Massachusetts Commission has not encouraged or required their Providers of Last Resort to enter into long-term contracts. This Commission must not make that mistake. There are many reasons to require the IOUs to rely on long-term contracts to meet the majority of their RPS requirements. As TURN notes (at p. 13), for example, consumers are likely to benefit from the hedge value of bundled renewables purchases as compared to short-term REC-only purchases.

materialize, other means of facilitating ESP compliance must be explored so that the RPS goals are timely met.³

2. Facilities Generating RECs Must Comply with All RPS Eligibility Requirements

AReM states (at p.7) that a “bundled delivery requirement would ... preclude the use of RECs associated with remote and out-of-state projects that otherwise promote the goals of SB 1078.” AReM is presuming that (a) facilities generating RECs need not comply with RPS eligibility requirements, which require in-state delivery of power, and (b) out-of-state projects necessarily promote the goals of the RPS. But RECs are not a free pass for avoiding RPS eligibility requirements, and out-of-state projects that do not deliver energy to California do not provide local environmental benefits.

Indeed, AReM and PG&E call straight out for the Commission not to “tie” RECs to in-state generation, arguing that it would not be advantageous to do so (AReM at p. 7; PG&E, at pp. 3 and 9). As TURN points out (at p. 15), the RPS statute requires in-state delivery of out-of-state power. The CEC adopted the details of this requirement after much consideration and discussion.⁴ These requirements have a strong policy foundation, as reflected in Decision 03-06-071 (at pp. 6-7), which noted “the public health and environmental benefits anticipated by the RPS statute.” Without an in-state delivery requirement, Californians would lose out on the local air quality benefits associated with reduced in-state gas generation. Instead of encouraging new renewable facilities in indigenous resource areas like Tehachapi, we very well may see the importation of RECs from neighboring states where the cost of doing business is less expensive than in California.

In opposing an in-state delivery requirement, PG&E states (at p. 9) that “there is

³ For example, TURN suggested the designation of a “procurement entity” to conduct long-term procurements on behalf of ESPs. See the January 18, 2005 “Opening Brief of The Utility Reform Network on Phase 2 RPS Issues,” p. 6.

⁴ See “Renewables Portfolio Standard Eligibility Guidebook,” California Energy Commission, August 2004, p. 18. Unfortunately, the CEC appears not to be directing the WREGIS system to automatically track in-state deliveries. As TURN suggests (at p. 15), the Commission should consider whether the ability to automatically track deliveries is necessary before out-of-state power (and associated RECs) are accepted for compliance. (Manual tracking may be possible if the instances are small.)

little evidence on the record that any significant supply of unbundled RECs is likely to be developed within California borders.” This statement ignores the huge base of existing capacity that will be coming off of QF contracts over the next several years.

Without commenting on the legal permissibility under the current RPS statute of unbundled RECs serving as a means of RPS compliance, we note that if the power associated with RECs meets all of the RPS eligibility requirements, there would be no difference in the practical outcome. The same practical result would occur also under various proposals for limited application of the REC concept (which CalWEA supports), such as those that would allow retail sellers to procure bundled energy, take the RECs, but remarket the power instead of taking delivery of it (see TURN at p. 7; PG&E at p. 8).⁵

3. The Commission Should Be Very Cautious in Adopting (REC) Market Power Mitigation Measures

AReM (at p. 6) calls for the Commission to "adopt REC market power mitigation measures that are similar to those applicable to long-term contracting by the utilities, i.e., temporarily excuse compliance with incremental RPS requirements where market power has been exercised to increase the price of all available RECs to unreasonable levels, thereby depriving the market manipulators of the windfalls they would otherwise receive." The Commission should be aware that waiving compliance penalties could undermine investment in merchant facilities.

Merchant generators may charge a premium for RECs based legitimately on the increased risks of building a merchant facility. It will be difficult, if not impossible, for the CPUC to distinguish between a legitimate premium and the exercise of market power based on a demand for RECs that is greater than supply, which might allow sellers to charge prices that are just short of the cost of the non-compliance penalty. If the CPUC were to waive the penalty based on claims of market abuse, it would further undermine investment in merchant facilities and eliminate an important means of ESP compliance. Conversely, high REC prices -- even those produced by demand-supply

⁵ These proposals would unbundle the RECs and the power, but only after bundled procurement takes place.

imbalances – will encourage merchant plants. The Commission must be very careful, therefore, to waive penalties only in the most extreme circumstances.

To put it another way, if the ESPs wish to live by the market, they must be prepared to suffer the realities of the market (which is bounded by the size of the noncompliance penalty). Merchant generators relying on short-term REC sales to cover their costs are incurring significant risks, and therefore deserve premiums when they can get them (because they may get little or nothing at other times, or even most of the time). The ESPs, on the other hand, can buy and bank RECs when prices are low, and can also take advantage of the compliance flexibility rules which will give them some protection from market vagaries. Therefore, the Commission should set the penalty, step back, and let the market work. If there is clear evidence that RECs are not available despite the ESPs' best efforts (e.g., a showing that ESPs have made sound offers for multi-year advance REC purchase agreements), then other means of facilitating ESP compliance must be initiated (such as third party procurement, or requiring the utilities to sell excess RECs to ESPs at fair prices).

4. Supplemental Energy Payments Should Not Be Applied to RECs

AReM (at p. 8) calls for Supplemental Energy Payments (SEPs) to be applied to RECs. This is not justified. First, it would be impossible to determine the “above-market” price that is to be covered by the SEPs on short-term REC purchases that represent a small fraction of a facility's generation over the long-term. Second, by definition, REC purchases deserve no SEPs because the very existence of the merchant facility is evidence that investors believe the facility will be supported by the market. There is little risk that the facility would be shut down without SEP payments, given the low operating costs of most renewables facilities. Third, as TURN stated (at p. 17-18), as long as long-term renewables contracts are being signed by the utilities at under the Market Price Referent, there are no “above-market” costs of renewables. This should remain the case at least until we work our way much farther up along the supply curve of renewables. If necessary, SEPs can be made available to ESPs in association with long-term renewable energy purchases made by third parties made on behalf of ESPs.

We look forward to continued discussion on these important topics.

Respectfully submitted,



Nancy Rader
Executive Director
California Wind Energy Association

February 18, 2005

Certificate of Service

I hereby certify that I have this day served a copy of the

***Reply Comments of the California Wind Energy Association
Regarding Tradable Renewable Energy Credits***

on all known parties to R.04-04-026 by sending a copy via electronic mail and by mailing a properly addressed copy by first-class mail with postage prepaid to each party named in the official service list without an electronic mail address.

Executed on February 18, 2005, at San Francisco, California.


Parashita Marschall