BEFORE THE PUBLIC UTILITIES COMMISSION OF

THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Continue Implementation and Administration of California Renewables Portfolio Standard Program	Rulemaking 11-05-005 (Filed May 5, 2011)

RESPONSE OF THE UTILITY REFORM NETWORK TO THE APPLICATION FOR REHEARING OF DECISION 11-12-052 BY COWLITZ PUBLIC UTILITY DISTRICT

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Pursuant to Rule 16.1(d) of the Commission Rules of Practice and Procedure, The Utility Reform Network (TURN) hereby submits this response to the application for rehearing of Decision 11-12-052 (*hereafter* "the Decision") filed by the Cowlitz Public Utility District. The Commission should deny the application because it does not demonstrate legal error and merely restates the policy preferences of the Applicant.

I. THE CONTRACT EXECUTED BY COWLITZ PRECEDED THE ENACTMENT OF SBX2, WAS EXPLICITLY SUBJECT TO GRANDFATHERING UNDER §399.16, AND WAS UNAFFECTED BY THE ADOPTION OF DECISION 11-12-052

Cowlitz alleges impermissible discrimination against out-of-state resources based on its own experience with a contract for the sale of renewable power between Pacific Gas & Electric (PG&E) and Shell (the counterparty) executed in late 2009. Specifically, Cowlitz claims that the contract was later withdrawn by PG&E "because of uncertainties and changing RPS compliance requirements applicable to transactions of the type PG&E proposed for purchases of out-of-state generation."[1] Cowlitz offers no evidence in support of this claim, fails to cite any relevant law or Commission decision, and ignores the possibility that Commission approval of the contract may have been delayed for reasons entirely unrelated to the location of the renewable generator.

Cowlitz's contract complaint is unrelated to the legal conclusions of D.11-12-052 or the statutory provisions of SBx2. Cowlitz seeks relief for actions not taken by the Commission and for issues not within the scope of D.11-12-052. These claims cannot properly be raised in an application for rehearing because the contract was terminated prior to the Decision being adopted by the full Commission. The

[1] Cowlitz application, page 5.

Decision does not either address the contract or adopt any specific findings that disadvantage the now-defunct transaction. In short, there is no rational nexus between the Decision and PG&E's prior termination of the contract.

Cowlitz's argument that the contract was delayed due to "uncertainties and changing RPS compliance requirements" finds no support in the relevant statutory provisions. The enactment of SBx2 revised a variety of code sections and created new restrictions applicable to procurement transactions executed after June 1, 2010.[2] However, the bill exempted transactions from these restrictions if executed prior to June 1, 2010.[3] Any pre-existing power transaction is not subject to the product category limitations outlined in "399.16(c) and should "count in full towards the procurement requirements established pursuant to this article".[4] Because the Shell/Cowlitz contract was originally executed prior to June 1, 2010, the product categories established in D.11-12-052 are not even applicable to this transaction. Since the Shell/Cowlitz transaction was "grandfathered", there was no legitimate uncertainty regarding eligibility and no product category limitations on procurement from the underlying resource.[5]

Cowlitz essentially argues that the Commission is obligated to approve the Shell contract. This claim ignores the Commission's statutory and constitutional responsibility to protect ratepayers and ensure that rates are just and reasonable. The Commission is not required to approve any contract simply because an Investor Owned Utility (IOU) submits the proposed transaction for approval via advice letter. Adopting the preferred position of Cowlitz would expose the Commission to litigation by IOU counterparties every time a contract is not approved. Such an outcome is neither reasonable nor legally required.

[2] Cal. Pub. Util. Code "399.16(c).
[3] The law applies this treatment to contracts executed by the retail seller prior to June 1, 2010 even if Commission approval occurs at a later date.
[4] Cal. Pub. Util. Code "399.16(d).
[5] The Decision challenged by Cowlitz does not even address the applicability of "399.16(d) to the contract cited in the application.

No revision to the Decision can alter the fate of the now-withdrawn contract. Rather than blaming the Commission or state law, Cowlitz should instead focus on serving its own customers with its abundant supply of windpower and offering any future renewable power transactions to California retail sellers consistent with the product categories defined in the Decision.

II. THE DECISION AND SBX2 DO NOT VIOLATE THE DORMANT COMMERCE CLAUSE

Cowlitz argues that the product category limits established in SBx2 and implemented in the Decision "applies in a fundamentally different manner to in-state verses out-of-state generation."[6] Specifically, Cowlitz asserts that "few out-of-state transactions are likely to be able to qualify for Category 1" and in-state facilities "will easily qualify for Category 1."[7] As a result, Cowlitz claims that the Decision and the underlying statutory scheme represents *facial discrimination* against generation located outside of California and results in unequal treatment for the procurement of identical products based solely on the location of the underlying renewable facility.

Cowlitz misstates the relevant facts and law and offers a narrow and incomplete understanding of the relevant tests applied by courts under the dormant Commerce Clause. The Commission should reject this one-sided characterization in favor of a more comprehensive and accurate analysis that includes all relevant precedents and considers the actual facts and law at issue in this case.

Under the dormant commerce clause, state policies that facially burden interstate commerce are subject to strict scrutiny by the courts. If a state policy discriminates against a service or good based solely on its geographical origin, then the courts will treat the action as facially discriminatory. Facially discriminatory measures must be

[6] Cowlitz application, page 10.
[7] Cowlitz application, page 10.

justified by □a valid factor unrelated to economic protectionism□[8] and supported by measures that are the □least discriminatory alternative.□[9]

Policies that do not facially discriminate (and are therefore non-discriminatory) but have an incidental effect on interstate commerce are valid if the state can demonstrate a link to legitimate benefits for its citizens.[10] Non-discriminatory regulation is defined as policy that places the same requirements on all similarly situated entities regardless of their geographical location. These policies are distinguished from facial discrimination because they □regulate evenhandedly□ rather than engage in □simple protectionism□.[11] By treating matters of intrastate commerce as identical to interstate commerce, the state avoids the strict judicial scrutiny that accompanies facial discrimination.

State regulation applied in a non-discriminatory manner in support of a legitimate public interest is reviewed by the courts under a balancing test. Under this test, the law will be invalidated only if the burdens on interstate commerce are excessive when compared to the local benefits. Defining this test in *Pike v. Bruce Church*, the US Supreme Court explained that once □a legitimate local purpose is found, then the question becomes one of degree□and that the weight given to the burden depends □on the nature of the local interest□.[12] Effects on interstate commerce are part of this equation but tend to be subordinate to the analysis of local benefits. Economic benefits are disfavored while environmental and consumer protections tend to be seen as legitimate.

[8] *Wyoming v. Oklahoma, 502 U.S. 437, 454 (1992)*(striking down a statute requiring all in-state power plants burn a mixture of at least ten percent in-state coal).
[9] *Hughes v. Oklahoma, 441 U.S. 322, 337 (1979).*
[10] For a far more thorough review of the application of the dormant commerce clause to state RPS eligibility rules, see The Dormant Commerce Clause Threat to Market-Based Environmental Regulation: The Case of Electricity Deregulation, Kirsten H. Engel, 26 Ecology L.Q. 243, 1999.
[11] *Minnesota v. Clover Leaf Creamery, 449 U.S. 456, 471 (1981)*(upholding state requirement prohibiting the sale of milk in non-recyclable plastic containers).
[12] *Pike v. Bruce Church, 397 U.S. 137, 142 (1970).*

Courts have upheld non-discriminatory state policies that directly burden out-of-state companies engaged in commerce within a national market. In *Exxon v. Maryland*, the Supreme Court upheld a Maryland statute that barred producers of petroleum products from selling gasoline at the retail level.[13] Despite the fact that all the burdened producers were out-of-state businesses, the court concluded that a disparate impact on outside businesses is an insufficient basis for invalidating the law.[14]

In *Proctor & Gamble v. Chicago*, the Seventh Circuit Court of Appeals upheld a local law banning the use of phosphates in detergent as a strategy for controlling "nuisance algae" in Lake Michigan.[15] Even though the amount of phosphates from detergents entering the lake constituted three percent of the annual total, the court refused to conclude that the benefits were insubstantial. Rather, the court found that "the city council was justified in believing that eventually its phosphate ban, in conjunction with other actions, would result in eliminating and preventing nuisance algae in the Illinois Waterway."[16] Not only was the goal of local environmental protection deemed valid, but the court also acknowledged that the effort to protect other communities, and to set an example for other jurisdictions, was presumptively legitimate.[17]

Cowlitz argues that a state law disadvantaging any out-of-state interest is presumptively invalid, citing *New Energy Co. v. Limbach*, 486 U.S. 269, 273 (1988) for the proposition that "a regulatory scheme that is otherwise discriminatory will not

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[13] *Exxon v. Maryland, 437 U.S. 117 (1978).*

[14] *Exxon* at 126. ("The fact that the burden of a state regulation falls on some interstate companies does not, by itself, establish a claim of discrimination against interstate com merce.")

[15] *Proctor & Gamble Co. v. City of Chicago, 509 F.2d 69 (7th Cir. 1975).*

[16] *Proctor & Gamble* at 74, 79.

[17] *Proctor & Gamble* at 81. ("we find that Chicago has a legitimate interest in banning phosphate detergents as an example for other communities presently releasing their sewage into Lake Michigan. Chicago is attempting to convince these communities to control their phosphate discharge into the lake. Chicago could reasonably decide that it would be aided in this endeavor if it could show these other jurisdictions that Chicago is willing to endure whatever hardships may be associated with the loss of phosphate detergents.")

survive strict scrutiny under the Commerce Clause, however, merely because it may benefit some out-of-state producers.[18] In that case, the Court struck down an Ohio tax credit provided to in-state producers of ethanol and producers of ethanol in states that had reciprocal agreements to offer similar tax treatment to Ohio ethanol producers. The Court specifically found that this "reciprocity agreement" still resulted in facial discrimination and was therefore subject to strict scrutiny.

In contrast to the facts presented in *New Energy*, the product categories established by SBx2 do not facially discriminate against out-of-state interests and do not grant special privileges to certain out-of-state producers based on reciprocity agreements. The law and the Decision allow unlimited amounts of procurement from both in-state and out-of-state facilities to count towards the first product category. There are no facial quotas, no bright lines at the border and no restrictions on participation based solely on location. The requirement is narrowly tailored to apply only to the delivery of renewable energy into California.

The product categories are designed to prioritize the value provided to California customers from each of the different types of transactions. The legislation identifies the following key benefits expected from the enactment of the RPS program, none of which are tied to economic protectionism, and each of which "independently justifies the program":[19]

> (1) Displacing fossil fuel consumption within the state.
>
> (2) Adding new electrical generating facilities in the transmission network within the Western Electricity Coordinating Council service area.
>
> (3) Reducing air pollution in the state.
>
> (4) Meeting the state's climate change goals by reducing emissions of greenhouse gases associated with electrical generation.

[18] Cowlitz application, page 11.
[19] Cal. Pub. Util. Code "399.11(b)

(5) Promoting stable retail rates for electric service.

(6) Meeting the state's need for a diversified and balanced energy generation portfolio.

(7) Assistance with meeting the state's resource adequacy requirements.

(8) Contributing to the safe and reliable operation of the electrical grid, including providing predictable electrical supply, voltage support, lower line losses, and congestion relief.

(9) Implementing the state's transmission and land use planning activities related to development of eligible renewable energy resources.

In order to realize these benefits, SBx2 establishes three product categories and adopts limits on the amount of post-June 1, 2010 procurement that can be used from each product category to meet the overall targets. The first product category includes procurement of bundled renewable energy[20] from facilities with a first point of interconnection with a California Balancing Authority (CBA), facilities that are located outside a CBA but can provide energy via dynamic transfer, or facilities located anywhere in the WECC that can directly schedule energy from the generator into a CBA □without substituting electricity from another source□.[21]

The first product category relies on non-discriminatory criteria designed to ensure that California customers receive direct incremental deliveries of renewable energy without the use of matching, tagging or substitute brown energy provided at a later time. These criteria are intended to maximize the displacement of in-state fossil generation and avoid reliance on the use of fossil fuels to facilitate the import. Any renewable facility within the WECC system may qualify for this treatment regardless of location.

[20] Bundled renewable energy refers to a transaction including the energy from the underlying generation facility and the associated Renewable Energy Credits (RECs).
[21] Cal. Pub. Util. Code □399.16(b)(1).

Cowlitz argues that few out-of-state generators can qualify for first product category transactions due to both the requirements of the RPS program and the considerable uncertainty regarding how transactions must be structured in order to satisfy these criteria.[22] Cowlitz is mistaken on both counts. First, extending eligibility to any facility directly connected to a CBA allows broad participation by generation throughout the WECC. Both the California ISO and LADWP systems (each of which qualifies as a CBA) have regional footprints with delivery points physically located far outside of California. The ISO balancing authority area contains many delivery points in Arizona and Nevada, and the LADWP system includes interfaces in Nevada, Arizona northern Oregon and Utah.[23] Moreover, some delivery points located physically within California can accommodate direct interconnection from renewable generation located in Oregon, Nevada, Arizona and Mexico.[24] Indeed, any facility with a first point of interconnection to the Pacific Northwest intertie (cited by Cowlitz) would be considered within the first product category since this line is part of the LADWP Balancing Authority.[25]

For resources not directly connected to a CBA, any first product category transaction must be provided either by dynamic transfer or a transaction not relying on substitute energy to schedule the power into a CBA. The Decision includes an extended discussion of the requirements for demonstrating a dynamic transfer and for a transaction that does not rely on substitute energy to schedule energy from the renewable generator into a CBA.[26]

[22] Cowlitz application, page 12.

[23] An incomplete list of delivery points outside California follow:

Oregon Malin (CAISO), Captain Jack (CAISO), Celilo (LADWP)
Nevada Mead (CAISO/LADWP), El Dorado (CAISO), Merchant (CAISO), Marketplace (CAISO/LADWP), Crystal (LADWP), Mohave (CAISO/LADWP), Gonder (LADWP)
Arizona Palo Verde (CAISO), North Gila (CAISO), Navajo Generating Station (LADWP)
Utah Intermountain (LADWP)

[24] For example, some renewable generation located in Mexico may connect directly to the Imperial Valley substation (CAISO).

[25] D.11-12-052, Finding of Fact #1.

[26] D.11-12-052, Pages 22-27, 37-42; Ordering Paragraphs 1, 4, 5, 6, 9, 12

Cowlitz is also incorrect in claiming that in-state renewable generation "will easily qualify for Category 1."[27] The Decision adopts the requirement that any transaction involving unbundled RECs will be classified as a third category product pursuant to §399.16(b)(3).[28] This requirement places in-state and out-of-state generation on the same footing -- both must provide bundled renewable energy products to a CBA without substitution. In the event that either an in-state or out-of-state renewable generator sells its energy and RECs to different buyers, the transaction may only count towards the §399.16(b)(3) product limits. As a result, the policy regulates evenhandedly and places the same requirements on all similarly situated entities regardless of their geographical location.[29]

Cowlitz argues that the eligibility rules are unclear based solely on speculation contained in comments filed by several parties and asserts that the range of views expressed by these stakeholders demonstrates ongoing uncertainty about how the first product category requirements can be satisfied by a generator located outside of a CBA.[30] These comments, all of which were filed before the Commission issued a Proposed Decision in this proceeding, fail to shed any light on the actual Decision and adopted requirements. For example, Cowlitz cites an objectionable proposal made by Sempra Generation that was not adopted in the Decision.[31]

Cowlitz further argues that dynamic transfers are insufficiently defined because the FERC-approved CAISO tariffs that enable such arrangements may evolve over time in response to more experience and stakeholder input.[32] This critique is misplaced because the CAISO currently offers dynamic transfers. The fact that such tariffs may change in the future is not relevant. Moreover, Commission does not have jurisdiction over the extent to which the CAISO allows dynamic transfers with other

[27] Cowlitz application, page 10.
[28] D.11-12-052, Conclusion of Law #18, Ordering Paragraph #3.
[29] *Minnesota v. Clover Leaf Creamery, 449 U.S. 456, 471 (1981).*
[30] Cowlitz application, pages 12-13.
[31] Cowlitz application, page 13.
[32] Cowlitz application, pages 14-15.

Balancing Authorities.[33]

Cowlitz cannot identify any particular material "uncertainty" that lingers.[34] A facility located outside a CBA may fully participate in the RPS program and sell bundled products that meet the first product category criteria under a variety of possible arrangements. The Decision provides clear guidance for an up-front showing by IOUs and an *ex-post* compliance showing by all retail sellers to demonstrate that the product category requirements have been satisfied in practice.[35] The *ex-post* showing is critical because compliance is based on delivered energy rather than forecasts of expected future production. There is no evidence presented by Cowlitz that these requirements are either too uncertain to implement or too restrictive to allow robust participation by out-of-state generation.

Cowlitz finally argues that the Commission should suspend all consideration of new renewable power commitments by the IOUs in order to maximize the amount of the remaining market that can be served by out-of-state generation.[36] In essence, Cowlitz suggests that the Commission should mandate greater quantities of procurement from out-of-state generation in order to avoid the charge of impermissible discrimination. This suggestion ignores the fact that IOUs and other retail sellers have made recent purchases based on the market value of renewable resources being offered in competitive solicitations. The Commission should not be forced to prove the absence of discrimination by requiring IOUs to explicitly favor out-of-state resources. Such an outcome makes no sense and is not required by the dormant Commerce Clause. The RPS program does not guarantee any generator, whether in-state or out-of-state, an absolute right to a profitable contract with a California IOU or retail seller.

[33] D.11-12-052, page 27.
[34] Cowlitz application, page 14.
[35] D.11-12-052, pages 40-41.
[36] Cowlitz application, page 15.

Based on the absence of any demonstration of facial discrimination, the Commission should reject the federal claims raised by Cowlitz and decline to grant rehearing. The Decision will allow full and fair competition by renewable generation located outside of California. Although the Applicant may prefer a more lax set of legislative and regulatory standards, this policy preference does not equate to a fatal Constitutional infirmity.

III. THE DECISION NEED NOT ADOPT THE APPLICANT'S PREFERRED DEFINITION OF "FIRMED AND SHAPED" PRODUCTS

Cowlitz asserts that the Decision's requirements for Second Category products exceed the applicable statutory authority, represent an abuse of discretion by the Commission and facially discriminate against out-of-state generators.[37] Instead of the definitions adopted by the Decision, Cowlitz urges the Commission to adopt the far more permissive definition of "firming and shaping" contained in previous RPS eligibility guidebooks issued by the California Energy Commission.

The arguments raised by Cowlitz are not valid legal critiques but rather represent unfulfilled policy preferences. Cowlitz ignores the fact that, in enacting SBx2, the Legislature explicitly required the Commission to adopt new requirements related to "firmed and shaped" products. The Legislature did not define the terms "firmed", "shaped" or "incremental electricity" in §399.16(b)(2). The Commission is therefore responsible for defining each of these concepts and issuing rules to ensure that the definitions are enforced.

The Decision notes that the terms "firmed and shaped" do not have "a generally accepted definition within the industry."[38] The Decision also properly concludes that the new statutory requirements are "more precise" and "more prescriptive" than those in prior law and should therefore be understood to "narrow the range of

[37] Cowlitz application, page 17.
[38] D.11-12-052, page 44.

transactions that would meet the criteria of 399.16(b)(2).[39]

Cowlitz fails to offer any evidence that the Commission failed to consider its preferred interpretation or provide any basis for concluding that the Commission abused its discretion. The Decision contains a discussion of proposals to rely on previous CEC eligibility guidelines and concludes that the CEC definition was not, and could not have been, intended to describe a portfolio content category of new 399.16.[40] As TURN has explained in previous comments, the previously applicable CEC guidelines led to rampant gaming by retail sellers. In comments, TURN offered the following critique:[41]

> TURN strongly urges the Commission to reject the *laissez faire* approach advocated by parties arguing to allow the existing CEC rules to stand. As the Commission is painfully aware, the IOUs have executed a wide range of transactions for products described as firmed and shaped. Many of these deals functionally replicate unbundled REC transactions through stripping mechanisms, wash trades of energy and delivery using legacy import contracts for resources such as the Palo Verde nuclear plant and SDG&E s El Dorado CCGT plant. Allowing these types of transactions to count as firmed and shaped is tantamount to a decision to eliminate any meaningful distinction between the second and third product categories.

The Commission is fully within its discretion to adopt a definition of firmed and shaped that ensures such products offer incremental electricity to California from resources that are not already committed to selling their output to another buyer. The purpose of these restrictions is to guarantee that power is not double counted and that the consequence of such a transaction is not merely the incremental generation of electricity by fossil fuels. Adopting the CEC guidelines endorsed by Cowlitz would defeat this intent.

The Decision properly responded to the enactment of SBx2 and the comments of all

[39] D.11-12-052, page 45.
[40] D.11-12-052, page 45.
[41] Reply comments of TURN, R.11-05-005, August 19, 2011, page 4.

parties in concluding that the eligibility rules should create bright lines between products described in §399.16(b)(2) and §399.16(b)(3). While Cowlitz may prefer a different set of policy outcomes, there is no basis for concluding that the Commission abused its discretion in adopting a set of specific "firming and shaping" requirements.

IV. CONCLUSION

Since the Applicant has failed to demonstrate valid legal errors in the Decision, the request for rehearing should be denied.

Respectfully submitted,

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