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Feed-In Tariffs: A Valuable Tool

Law360, New York (November 13, 2008) -- California's Renewables Portfolio Standard ("RPS") requires California's investor owned electric utilities ("IOUs") and other retail electric sellers to procure 20 percent of their retail electric sales from eligible renewable resources by no later than 2010.

In addition, Governor Schwarzenegger directed that the 2007 Integrated Energy Policy Report prepared by the California Energy Commission ("CEC") review the feasibility of extending RPS goals to 33 percent renewable energy by 2020.

Since then, the CEC and the California Public Utilities Commission ("CPUC") have been working together to evaluate the potential for adopting a more aggressive RPS and making 33 percent of the power delivered in California from renewable sources by 2020.

Forces are already moving the State in that direction. Chief among these is the recent Climate Change Proposed Scoping Plan ("Proposed Scoping Plan") released by the California Air Resources Board ("ARB").^[1]

Under Assembly Bill ("AB") 32, the ARB must develop a scoping plan that sets forth a comprehensive set of actions to reduce California's greenhouse gas ("GHG") emissions to 1990 levels by 2020.

One of the Proposed Scoping Plan's primary recommendations on how the State can achieve its GHG emissions goal is: "Achieve 33 percent renewable energy mix statewide."

The ARB's Proposed Scoping Plan is aggressive given today only about 12 percent of California's retail electric load is served by renewable resources. In fact, this percentage has actually decreased in recent years from approximately 14 percent.

Furthermore, the percentage of renewable generation in each IOU's electric generation

portfolio differs significantly. The CPUC's most recent Renewables Portfolio Standard Quarterly Report[2] shows that while in 2007 renewable energy made up 15.7 percent of Southern California Edison Company's ("SCE") bundled sales, it comprised 11.4 percent of Pacific Gas and Electric Company's ("PG&E") and only 5.2 percent of San Diego Gas & Electric Company's. The Quarterly Report concludes:

"IOUs are now projected not to meet the 20 percent by the 2010 target, even if all of the 2010 generation that is now rated medium or high risk or under negotiation, were to come online by that year."

California's IOUs may hit 20 percent in the 2012-2013 timeframe, if the state successfully removes barriers to project development. It is worth noting that reaching the 20 percent goal in 2013 would leave the IOUs only 7 years to achieve the 60 percent increase in RPS generation needed to reach a 33 percent target in 2020.

New Approaches, Such As The Use Of Feed-in Tariffs, Must Be Considered If California Is To Reach A 33 Percent RPS By 2020

Given the progress to date and the ARB's proposed recommendation of a 33 percent RPS by 2020, it is necessary that California consider new approaches to promote the development of renewable resources. One approach that has proven successful is the use of "feed-in tariffs."

What Is A Feed-In Tariff?

A recent report prepared by KEMA Inc.[3] for the CEC defines a feed-in tariff as follows:

At its simplest, a feed-in tariff is an offering of a fixed-price contract over a specified term with specified operating conditions to eligible renewable energy generators. Feed-in tariffs can be either an all-inclusive rate or a fixed premium payment on top of the prevailing spot market price for power.

The price paid represents estimates of either the cost or value of renewable generation. The tariff is generally offered by the interconnecting utility and sets a standing price for each category of eligible renewable generator; the price is available to all eligible generators.

Tariffs are often differentiated based on technology type, resource quality, or project size and may decline on a set schedule over time.

Feed-In Tariffs Have Been Successfully Used In Other Jurisdictions

The most common policy to promote renewables is the feed-in tariff.[4] The success of feed-in tariffs in promoting the use of renewable resources is evidenced by the progress that countries such as Germany and Spain have achieved. Germany has employed feed-in tariffs since 1991.

Today, it has 22,622 megawatts (MW) of wind and 3,800 MW of solar photovoltaic ("PV") installed capacity. By contrast, California with 2,484 MW of installed wind power and 281 MW of solar PV has only about ten percent of Germany's installed wind power and seven percent of its solar PV.

Spain also has experienced significant progress in developing renewable generation by using feed-in tariffs. At the end of 2007, Spain had a total of 15,145 MW of wind capacity and 500 MW of PV capacity. In 2007 alone, Spain added 3,522 MW of wind and its PV market grew by 300 percent.

By adopting a solar thermal feed-in tariff, Spain also helped to spur the development of solar thermal power. It now has approximately 270 MW of solar thermal power under development.

California's Current Use Of Feed-In Tariffs

California has experimented with feed-in tariffs as a means of promoting renewable sources of electric generation, albeit with limited success.

In 2006, the legislature enacted AB 1969 adding Public Utilities Code Section 399.20, authorizing tariffs and standard offer contracts for the purchase of eligible renewable generation from public water and wastewater facilities.

Last year the CPUC adopted Decision ("D.") 07-07-027 which ordered each regulated electric utility to submit tariff provisions implementing that legislation.

Under the Commission's decision each IOU must offer a standard contract or tariff to an eligible public water facility or eligible public waste water facility that owns an eligible renewable energy resource that is not greater than 1.5 MW. The price paid is the adopted market price referent ("MPR") for the year in which the facility actually commences commercial operation.

In addition to adopting a feed-in tariff for eligible public water and wastewater facilities, the CPUC also expanded the program for non-water and wastewater facilities to include an additional 228.447 MW of eligible renewable generating capacity located in the SCE and PG&E service territories.

Like the feed-in tariff for public water and waste water facilities, a standardized contract is provided and the eligible renewable generating resource cannot exceed 1.5 MW of effective generation capacity. The seller is paid the MPR for the year in which the facility commences commercial operation.

There are other discrete programs that use feed-in tariffs in California. SCE, for example, offers standard contracts for biomass generators that are less than 20 MW. The program, which became effective in May 2007, expires at the end of 2008 or 250 MW, whichever comes first.

The energy price paid is the MPR for the year in which the facility comes on line. As of June 2008, only 11 MWs were under contract.[5]

If Feed-In Tariffs Are To Help Meet California's RPS, They Should Not Be Limited To The MPR

While California has experimented with feed-in tariffs, it has not enjoyed the same success as programs in Germany or Spain. One of the primary reasons for this is the price paid under the feed-in tariffs that are currently authorized or in use by California IOUs are all set at the MPR.

Yet, as the CPUC specifically pointed out in D.04-06-015, the MPR "does not represent the cost, capacity or output profile of a specific type of renewable generation technology ... [T]he MPR is to represent the presumptive cost of electricity from a non-renewable energy source, which this Commission ... held to be a natural gas-fired baseload or peaker plant." [6]

Thus, the MPR paid under the feed-in tariffs currently in use in California bears no relationship to the cost of the renewable resource generating facility, nor does it reflect the value of such a facility.[7]

Using the MPR as the contract price that is paid to renewable energy projects has the effect of limiting the effectiveness of the feed-in tariff. First, as noted, the MPR bears no relationship to the cost of the renewable resource generating project.

This is especially true since many of the projects that are eligible for feed-in tariff tend to be smaller - in the 1.5 MW to 20 MW range. Thus, they do not have the economies of scale that one might find in a natural gas combined cycle facility.

Second, the MPR bears no relationship to the value of the renewable resource generating facility. While the CPUC has recently included a calculation of the cost of the proxy plant's compliance with regulatory programs limiting GHG emissions in the MPR methodology, this simply accounts for one of the additional cost of fossil generation, but does not recognize the positive societal and environmental values of renewable generation.

Because of the inherent flexibility of feed-in tariffs and because they can be designed to encourage the development of specific forms of generation or generation at specific locations where it would be most valuable to the utility, the "one-size fits all" approach of the MPR calculation underestimates the value of the new renewable resource proposed to be brought on-line through a feed-in tariff.

For example, because of transmission constraints, the State may find it desirable to encourage through a feed-in tariff renewable projects that are connected to the grid in areas that are not transmission constrained.

This would result in cost savings to ratepayers that should be reflected in the price that is paid to the generator under the feed-in tariff. Using the MPR approach to establish the price fails to recognize this value.

Another example is the State may wish to encourage a certain type of renewable resource, such as biomass generation as compared to an intermittent renewable resource. A feed-in tariff can be used to do this, recognizing the additional value of the particular resource. The one-size fits all MPR approach, which is based on a gas fired proxy plant, fails to take this additional value into account.

Finally, under current feed-in tariffs, renewable generators are not eligible for public purpose funds if the cost of generation exceeds the MPR. This is true, no matter how desirable the generation may be or how much the cost of generation exceeds the MPR.

To be eligible under current rules, the generator must participate in the IOU's competitive bid process and obtain CPUC approval. For small renewable generators, this drawn-out procedure may represent an unacceptable economic hurdle.

If Feed-in Tariffs Are To Be Used To Help Achieve California's RPS And GHG Goals, Public Utilities Code Section 399.15 Must be Modified

As discussed above, to be effective feed-in tariffs may have to provide for payments that are in excess of the MPR when justified. Consequently, it may be necessary to make modifications to Public Utilities Code §399.15 to allow for such payments.

Section 399.15 sets forth the utilities' basic RPS obligation and limits the amount of above MPR costs that an IOU incurs in trying to achieve its RPS. Under §399.15 an IOU need not enter into contracts that exceed the MPR if it would have to pay funds that are greater than the amount of renewable energy public goods charges that it receives.

More important to the development and use of feed-in tariffs, the statute provides that contracts with prices that exceed the MPR may be counted toward this cost limitation only if it has been approved by the CPUC and was selected through a competitive solicitation.

Requiring a competitive solicitation for a contract to be eligible is contrary to the very nature of a feed-in tariff, which by definition is available to all eligible generators. Furthermore, there is no reason for such a requirement when feed-in tariffs are used.

Since the feed-in tariff is part of the IOU's tariff structure, it must be approved in advance by the CPUC. Thus, the type of renewable generation that will be eligible, the terms and conditions of the tariff, as well as the prices that will be paid all will be examined and approved by the CPUC in advance of the effective date of the feed-in tariff.

Furthermore, the tariff can be designed so that the utilities continue to receive the same protection limiting their payment exposure to the amount of the renewable energy public goods charges they receive.

Conclusion

Given the progress to date by the California's electric utilities, additional actions are required if California is to attain the more aggressive RPS that the ARB has stated that it intends to rely on to achieve California's GHG emissions goals.

The most common and effective policy used by other countries to reach similar goals is the feed-in tariff. Feed-in tariffs have proven that they can be an effective tool in fostering the development of renewable electric generation.

California should provide its IOUs with this important tool. To make it truly effective, however, the State should provide for feed-in tariffs which allow a price to be paid that exceeds the MPR when warranted.

Public purpose goods funds can be beneficially used to cover these additional costs. In addition, the Commission must remove other impediments, such as the requirement of competitive solicitation for contracts with payments in excess of the MPR.

The alternative to failing to reduce GHG emissions because an effective RPS was not instituted is potentially catastrophic. California electric utilities should not be denied the tools that have proven most effective in developing renewable electric facilities.

California should implement an aggressive feed-in tariff policy to assist in attaining its RPS and reducing GHG emissions.

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[1] Climate Change Proposed Scoping Plan, a framework for change, October 2008, the California Air Resources Board for the State of California.

[2] Renewables Portfolio Standard Quarterly Report, July 2008, California Public Utilities Commission.

[3] California Feed-in Tariff Design and Policy Options, prepared for the California Energy Commission by KEMA Inc., dated September 2008, CEC -300-2008-009D.

[4] Renewables 2007 Global Status Report, (Paris: REN 21 Secretariat and Washington, DC: Worldwatch Institute, at 7.

[5] Exploring Feed-in Tariffs for California, Feed-in Tariff Design and Policy Options, Draft Consultant Report, prepared for the California Energy Commission by KEMA, Inc., dated June 2008, CEC -300-2008-009D, at 4.

[6] D.04-06-015, at 6. The Commission further refined the MPR model in D.05-12-042. The MPR represents the cost of a long-term contract with a combined cycle gas turbine facility, levelized into a cent-per kWh value.

[7] The MPR performs a number of functions, the most important of which is to act as a

dividing line for bids submitted to the IOU for an RPS contract. Bid prices at or below the MPR may be accepted as per se reasonable by the CPUC. Bids priced at above the MPR may face a stronger burden of proof in justifying the reasonableness of their contract price. Contracts that are above the MPR and are approved by the CPUC are eligible to receive Public Goods Charge funds which are available to each IOU on a pro rata basis.

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