

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Case 03-M-0188 - Proceeding on Motion of the
Commission Regarding a Retail Renewable
Portfolio Standard

INITIAL COMMENTS OF
CONSTELLATION NEWENERGY
REGARDING IMPLEMENTATION OF A RETAIL
RENEWABLE PORTFOLIO STANDARD

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DISCUSSION

I. INTRODUCTION AND SUMMARY

We submit the following comments on behalf of Constellation NewEnergy in response to ALJ Stein's Rulings regarding comments in this docket.¹ Constellation NewEnergy supports the establishment of a renewable energy portfolio standard ("RPS") in New York State. Before the Public Service Commission ("Commission") implements an RPS, we urge consideration of several important issues, as discussed herein, bearing upon the competitive energy market in New York State.

Of prime concern is the implementation of the overall RPS Structure (Section V below). Constellation NewEnergy recommends an individual compliance mechanism because it will accomplish the RPS goal and minimize negative effects to the competitive energy market in New

¹ Case 03-E-0188 - Proceeding on Motion of the Commission Regarding a Retail Renewable Portfolio Standard, Letter to All Parties (July 21, 2003); Ruling Establishing Comment Procedures (June 19, 2003); Ruling on Motion to Amend Comment Schedule and Convene Reliability Impacts Meeting (June 13, 2003); Further Ruling Concerning Schedule and Procedure (September 19, 2003).

York. The centralized procurement approach is inferior because it will reduce liquidity and discourage market efficiencies. Compatibility with the interstate market is also a critical element to a successful RPS. Renewable Energy Credits (“REC”) can and should be traded between regional states to maximize renewable energy available to the state, mitigate potential cost impacts and encourage the development of renewable resources.

The following comments are generally organized in accordance with ALJ Stein’s “Summary of Working Group Discussions.”

II. COMMENT ON THE REVISED WORKING OBJECTIVES

Constellation NewEnergy supports the “Working Target” of obtaining at least 25 percent of the electricity retailed in New York from renewable resources. Achieving the objective can reasonably be expected to promote benefits to the environment, improve the state’s diversity of generation and stimulate economic activity in the renewable energy sector. Depending on how the RPS requirement is ultimately implemented, market forces can produce the incremental renewable resources in an economically efficient manner. In order to ensure efficient procurement of renewable resources, however, consideration of modifications and qualifications to Objectives 4, 5 and 6 are necessary.

Objective 4, “Equity and Economic Efficiency,” calls for minimizing adverse impacts on energy costs and allocating costs equitably among ratepayers. These are two important issues. First, energy costs can be controlled with a cap on the cost of RECs by implementing an Alternative Compliance mechanism.² Second, Objective 4 limits the consideration of equitable cost to “ratepayers,” a term that is not always assumed to include ESCO customers. The term “ratepayer” must be deemed to include not only utility ratepayers, but also consumers of electricity purchased from ESCOs.

² See discussion, *infra*, (Section V, p. 8).

Objective 5, titled “Competitive Neutrality,” must be a cornerstone of the RPS requirement. The Objective does not specifically indicate that the RPS should be implemented in a competitively neutral way. It only states that the RPS should be compatible with competition in energy markets in New York State. Objective 5 should explicitly incorporate the goal of implementing the RPS equitably and in a competitively neutral manner. It is essential that the RPS system does not result in advantages to some participants and disadvantages to others.

An essential element of any efficient and liquid market is transparency. These two important factors are recognized by Objective 6, “Administrative Fairness and Efficiency.” In order for the RPS to work efficiently to obtain renewable sources of electricity at the lowest cost, it is critical that market participants can obtain clear and verifiable RPS data. We recommend the adoption of a generation information system (“GIS”) like that used in the Northeast Independent System Operator (“NEISO”). Adopting a GIS-compatible system will yield several significant benefits. First, it would allow for a regionally integrated system and prevent double counting of renewable generation attributes. Second, the RPS target will be most easily and efficiently obtained if the regional market beyond New York State is available (as we recommend below). A compatible system will promote the availability of out-of-state resources. Third, it is already known to provide the market transparency that is necessary. Fourth and finally, the existing GIS platform has been used successfully and many market participants are already familiar with it; its use will reduce transition time and costs and will promote liquidity of the market.

III. THE RETEC STRAW PROPOSAL

RETEC has introduced several straw proposals for an RPS structure: one for centralized procurement, one for individual compliance and one hybrid model that contains features of both the individual and central models. The RETEC proposals contain a description of several

possible RPS structures and are useful illustrations, but each proposal has significant flaws and unnecessary complications. Each of the proposals contains elements that directly detract from the Working Target and six Revised Working Objectives. For instance, RETEC recommends the Commission impose unspecified penalties and surcharges above and beyond any capped and predictable Alternative Compliance mechanism created to implement the RPS requirements.³ This conflicts with the need for transparency and unnecessarily hinders the efficient working of the marketplace. In another example, RETEC proposes an additional incentive for emerging technologies.⁴ The incentive is a potential subsidy for otherwise uneconomic technologies and conflicts with the goal of obtaining RPS requirements in the most efficient manner. Promoting alternative technologies is already undertaken by NYSERDA with funds already collected and earmarked for that purpose. Although promoting new technologies may be laudable, there is no need to duplicate NYSERDA's, particularly when it would interfere with the operation of a competitive market. Moreover, the implementation of a market-based RPS will naturally promote investment in promising and economic technologies. The subsidy proposed by RETEC is unnecessary and oversteps the bounds of this proceeding, detracting from its central goals.

We discuss in Section V (below) why an individual compliance mechanism is far superior to the central procurement model. For that reason, a complete critique of the RETEC proposal is not necessary. Instead, we support those elements of the RETEC proposal that are consistent with the model described in Section V (such as equal application of RPS requirements to both regulated utilities and ESCOs⁵ and an opt-out for meeting RPS requirements for a central procurement approach)⁶ and we specifically reject all elements of the RETEC proposals that are inconsistent with our discussion below.

³ See RETEC Discussion Proposal, p. 7 (7/23/03).

⁴ See RETEC Discussion Proposal, p. 4 (6/24/03).

⁵ See RETEC Discussion Proposal, p. 2 (6/24/03).

⁶ See RETEC Discussion Proposal, p. 6 (7/23/03).

IV. ELIGIBILITY

Constellation NewEnergy notes that parties agree that the measurement of renewables should be based upon energy purchased, not capacity. The RPS should not be based upon energy capacity, which does not measure the energy retailed in the state.

The Department of Public Service Staff (“Staff”) has proposed a compromise “baseline” for existing renewable resources that does not specifically reference which categories or technologies are included in that baseline. Although specific categories are not referenced in the baseline, it is clear from the working group discussions that not all types of existing renewable technologies are included. We support the principle articulated by the Clean Technologies Coalition (“CTC”) that “any and all technologies, and applications thereof, that further the RPS goals and objectives should be included within the RPS: protection of the environment (with respect to greenhouse gases and other environmental benefits), reduction in fossil fuel use, energy security and reliability, economic development, cost efficiency, and energy efficiency.”⁷ This principle would recognize that a slightly larger renewable baseline exists and would resolve the competing positions of several parties regarding eligibility. The Commission should consider making and adjusting Staff’s baseline assumption.

According to the principle that all sources of renewable energy that advance the goals of this proceeding should be recognized, we encourage the Commission to adopt broad eligibility criteria for the incremental RPS as well as the baseline. The Commission should include as many energy sources as possible so as not to discourage development of new types of sources. The RPS should recognize the value and environmental benefits of energy sources that some parties have advocated be excluded, such as waste-to-energy, either by simply including additional eligible resources, or by adopting a tiered structure. The tiered approach may be

⁷ Transmittal letter to CTC Eligibility Proposal, dated June 9, 2003.

somewhat more complicated than simply adopting broad eligibility standards, but a tiered approach is a better alternative than excluding certain resources.

Modifications that expand either the baseline or incremental eligibility of resources are consistent with the goals of this proceeding and will provide important economic benefits. Increased eligibility of resources will create a more liquid REC base, reducing the overall cost and reducing the risk of unnecessarily high and inefficient prices.

The Commission should view the proposed interim targets as just that: targets, achievement of which should be strived for, but are which not hard and fast numbers to be met. Although the interim targets are useful for planning purposes, the progress toward the goal of 25 percent by 2013 may unfold in an unpredictable pattern. For that reason, we recommend that the proposed interim targets be soft targets; the primary benefit of adopting them will be to monitor progress and to guide the PSC in setting annual requirements. The Commission can thus accommodate variations that are certain to occur in the development of new renewable resources.

We also agree with other parties that an adjustment mechanism is necessary to correct for actual load growth when it varies significantly from the forecast.

V. OVERALL RPS STRUCTURE

A. THE COMMISSION SHOULD ADOPT THE INDIVIDUAL COMPLIANCE MODEL

Constellation NewEnergy recommends that the Commission adopt the individual compliance mechanism as described herein. An individual compliance mechanism, if implemented properly and with certain safeguards, is the most efficient, least cost path to widespread renewable energy sources.

The Staff Strawman for an Individual Compliance approach contains six elements on which all parties to Working Group 2 agreed. Most important is the Strawman's determination of participating entities because it includes delivery utilities and ESCOs.⁸ One option that was rejected by the group is to have the ESCO share of renewables acquired by the delivery utility. ESCOs should be entitled to acquire RECs on their own and should not have their renewables portfolio managed by the utility delivery company. Such an arrangement is inconsistent with the Commission's vision for a competitive marketplace. It was rightfully rejected by the group and it should be rejected by the Commission.

The consensus for Individual Compliance is that the targets should be a fixed percentage of actual loads by LSE. The targets, still to be determined,⁹ would increase annually. The parties agreed that an important component is a trading and banking mechanism. This permits flexibility to obtain RECs and is fundamentally necessary to meeting the requirement because the RECs will have to be matched to actual load, after the fact, when the amount of load served is determined.

The Staff Strawman proposal for Individual Compliance is an innovative approach to meeting the RPS that Constellation NewEnergy supports because it is flexible and also because it protects market participants and consumers from a situation where the price of RECs increases dramatically. The protection derives from implementing an Alternative Compliance mechanism.

⁸ Participation is subject to the right of LIPA and NYPA to elect not to participate, in which case their respective loads would be removed from the calculation of the obligations of all LSEs. The participating LSEs should not be required to obtain renewables to cover the significant loads of these two state authorities.

⁹ See discussion, *supra*, regarding "soft" targets (Section IV, p. 8).

Under the Alternative Compliance approach, an LSE can purchase or trade RECs in the open market, or pay an amount based upon its load.

The amount paid for Alternative Compliance would be capped. The Strawman proposes to cap the amount at the lower of \$50/MWh or 150% of REC market value. While we agree there should be a cap, we disagree with the Strawman's target cap. In fact, we believe that the cap should not be established in advance, because it will most likely skew price signals causing them to be falsely high. If the alternative to the market is known, that price will, as a practical matter, set the market price. The influence of the cap will significantly harm the REC market and increase the cost to consumers. On top of that, the Alternative Compliance amount could be 150% of an artificially high market price. This is a real danger that must be avoided.

Instead of establishing a set cap, the amount to be paid for Alternative Compliance should be set at the end of a given RPS period and adjusted yearly based upon the average market price.

As was discussed in Working Group 2, we agree that the funds collected from an Alternative Compliance mechanism could be deposited in fund to be used for obtaining renewable energy. In the event an insufficient supply of RECs exists, funds would be collected and used to increase supply in future years. Another benefit of the Alternative Compliance mechanism is to make RPS enforcement unnecessary, eliminating the associated administrative cost and burden.

The Individual Compliance approach is a straightforward approach that protects consumers from unreasonably high prices (if the amount for Alternative Compliance is set at the

end of the RPS reporting period), accomplishes the goal of increasing the use of renewable energy in the state and works with competitive market forces to do so efficiently.

**B. THE COMMISSION SHOULD REJECT THE
CENTRALIZED PROCUREMENT MODEL**

Constellation NewEnergy does not support the adoption of a Centralized Procurement structure for the RPS. If one entity is obtaining most or all of the RECs for the entire state, there will be no accurate price signals to determine the appropriate cost of RECs. The REC market will be inefficient at best – essentially, there will be no market. Unlike Individual Compliance, the Centralized Procurement method is inconsistent with the Commission’s policy of promoting a competitive electricity market.

Another disadvantage of the Centralized Procurement approach is that consumers will ultimately pay more to meet the RPS requirements. First, as explained above, there will not be clear price signals to determine the correct price. Second, under the “contract for differences approach,” whereby the procuring entity (whether the entity is the ISO or a state agency) pays the difference between a fixed price and the market price for energy, consumers are likely to pay more. The “contract for differences” virtually ensures that all consumers will pay a premium over the market price for RECs. This forces the ratepayer to pay for a hedge in the REC market, when the RPS could be more efficiently satisfied by the LSE in a competitive market.

In the event that a Centralized Procurement mechanism is selected over the superior Individual Compliance proposal, a load serving entity should have the option to either meet its RPS requirements through the state program or to acquire RECs on its own. In one iteration of a Centralized Procurement model, this was called an “opt-out.” The opt-out (for some or all of an

LSE's requirements) would create a minimal amount of flexibility in acquiring needed RECs. Practically speaking, however, the price of RECs will be set by the Centralized Procurement entity. Because of the various disadvantages of the Centralized Procurement approach and the many benefits of the Individual Compliance structure, we urge the Commission to adopt the Individual Compliance approach as outlined herein.

VI. CREDIT TRADING

A. THE COMMISSION SHOULD ADOPT THE NEW ENGLAND GIS MODEL FOR TRACKING RECS

Constellation NewEnergy urges Staff and the Commission to adopt the New England model for REC trading. It will not be efficient to reinvent the wheel; the New England system is already successful and comprehensive (it tracks financial transactions and more emissions than the other models). Adoption of this multi-jurisdictional model will also avoid the potential of double-counting of RECs used in more than one state. RECs are created when the renewable electricity is generated and electricity is often procured from out-of-state. A system that is compatible with other jurisdictions is thus essential. Many LSEs are already familiar with the GIS system and it could be implemented quickly and effectively.

One of the most important aspects of the model is that it is designed for multi-jurisdictional use. The Commission should permit the interstate trading of RECs. Accepting interstate RECs is only natural given that New York obtains electricity from neighboring states and Canada. Allowing the use of out-of-state RECs, even from states beyond neighboring jurisdictions, should be encouraged.

The New York model, which is based upon the Commission's environmental disclosure program, should not be adopted. The model was designed for a different purpose and would

unnecessarily restrict the options for implementing the RPS. For instance, the banking of credits is an element of consensus among the parties. However, because of the limited reporting period associated with conversion transactions for environmental disclosure, the New York model prevents any reasonable banking period. The environmental disclosure program also only tracks three emissions categories (sulfur, oxides of nitrogen and carbon dioxide), whereas the New England GIS tracks five more (mercury, volatile organic compounds, particulates, particulate matter greater than 10 microns in diameter, and carbon monoxide). It makes inherent sense to adopt the more comprehensive and regionally compatible New England GIS system.

VII. CONTRACTING STANDARDS

Constellation NewEnergy has no specific comments on the contracting standards for agreements between LSEs and generators selling RECs, except that long-term contracts should not be required and the terms and conditions of any LSE contract should be negotiated between the parties thereto, without unnecessary requirements imposed upon them. Imposing terms and conditions unnecessarily interferes with the working of a competitive market.

CONCLUSION

Constellation NewEnergy urges the Commission to implement an RPS that promotes competition in the renewable energy market, protects consumers from the potential imposition of unjust prices and is compatible with the interstate energy market. We believe that the best way to accomplish the goals of an RPS is by implementing an individual compliance mechanism as described herein and to adopt our other proposals for promoting an efficient and liquid market for renewable energy.

Respectfully submitted,

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