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COMMISSION TRIES TO BALANCE NEEDS OF POWER USERS, UTILITIES

Focus Column
Environmental Law

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When the government tries to decide how it should recover $20 billion for past overpayments of electricity costs, it gets everyone's attention. The state Public Utilities Commission is engaged in a high-stakes zero-sum game that pits users of electricity, who range from homeowners and apartment dwellers to commercial buildings and industrial manufacturers, against utilities to determine who will pay their "fair share" of the bill.

The commission's decisions in this arena will shake up the state energy markets again. What remains to be determined is whether these new actions also will open an economic path for companies and municipalities trying to control their energy costs with clean on-site electricity generation.

A recent commission decision, proposed Sept. 24 and subject to comment, establishes a variety of fees (called exit fees) to be imposed on "direct access" customers as a partial payback of debts from the energy crises. See "Order Instituting Rulemaking Regarding the Implementation of the Suspension of Direct Access Pursuant to Assembly Bill 1X and Decision 01-09-060," Cal. Pub. Utilities Comm'n Rulemaking 02-01-011 (Jan. 9, 2002).

Direct-access customers obtain electricity from independent electric service providers, not the electric utility, a business practice sanctioned by early rounds of energy deregulation. The proposed decision sets exit fees for direct-access customers at up to 2.7 cents per kilowatt-hour - or higher under alternative decisions proposed by other commissioners - a significant hit for many customers who negotiated long-term contracts in the 5- to 7-cent-per-kilowatt-hour range. Direct access represents 12 percent of the electricity capacity in the state.

This decision is especially significant for large energy users because it forces them to make some critical decisions on how they buy electricity and how much they pay for it. In some cases, the imposition of exit fees will make direct access uneconomical.

It is unclear what effect the decision will have on the enforceability of existing long-term direct-access contracts. What is clear is that the stakes are high and that significant motivation exists to find ways out of

uneconomic contractual relationships. By making this decision on direct access, the commission has decided that a significant part of the $20 billion bill should be borne by direct-access customers.

The commission now turns its attention to the bundled customers (those receiving service from the grid, including individual and commercial accounts) and customers who opted or will opt to install on-site power or "distributed generation."

The commission proceedings affecting distributed generation were merged with the direct-access proceedings under the moniker DA/DL, standing for direct access/departing load.

Distributed-generation customers (those who generate their power on-site, either in parallel mode with the electric utility or on a stand-alone basis) have a separate set of fees in store for them, termed "departing load" fees.

Hearings to set departing load fees for customers who opted for on-site generation are under way at the commission, and interested parties expect a proposed decision sometime before the end of the year. Many stakeholders have proposed a settlement that would resolve the direct access/departing load issues. The expectation is that departing-load fees may come in slightly higher than those for direct-access customers. Some parties, such as the Center for Energy Efficiency and Renewable Technologies, are pushing for reduced fees for "ultra clean" distributed generation, such as solar, wind and fuel cells.

A customer's decision to opt for "clean" or "dirty" distributed generation most often reflects primarily economic considerations. The strong perception in the marketplace is that clean energy is more expensive energy. For the most part, without government support, that perception is an accurate view of reality. Clean technologies are often new technologies that face substantial cost hurdles that more established (usually dirtier) technologies do not encounter.

The dirtier distributed-generation technologies are represented by fossil fuel-burning engines that emit significant amounts of nitrous oxide and other carbon pollutants into the environment. When the heat generated by these less-clean technologies is used, however, projects often offer rapid paybacks for facility owners, assuming that all other things, like departing-load fees, are equal.

Many clean-energy interests argue, on the other hand, that if the less-clean technologies were forced to take into account the damage to the environment and the costs of future remediation and cleanup occasioned by polluting technologies, the cost analysis would shift to the side of the clean energy.

Legislation has begun to address this imbalance by providing economic subsidies for selected clean-energy technologies. Most notably in the distributed-generation arena, the commission, acting per legislative mandate, issued Decision D. 01-03-073 (March 27, 2001) (as modified by D. 02-04-044 (April 4, 2002)), to provide a tiered system of financial incentives to encourage customer self-generation.

The decision gave the following subsidies: the lesser of 50 percent of total project costs or $4,500 per kilowatt to solar and wind technologies, as well as fuel cells operating on renewable fuels; the lesser of 40 percent of total project costs or $2,500 per kilowatt to fuel cells operating on nonrenewable fuel and utilities; and 30 percent of total project costs or $1,000 per kilowatt for gas turbines, microturbines and certain internal combustion engines using sufficient heat recovery and meeting reliability criteria.

In an acrimonious prologue to the commission's decision, the bellwether and highly influential South Coast Air Quality Management District successfully petitioned to modify the rule to allow for other agency funding of projects receiving commission self-generation funds.

Attention is now focused on how the commission will implement SB1038, signed by the governor on Sept.

12 as part of an omnibus renewable-energy legislative package. SB1038 has added a new section to the Public Utilities Code that permits the commission to consider energy efficiency and emission performance when establishing rates and fees for distributed generation.

The rationale for this new code section is encouragement of early compliance with air quality standards established by the state Air Resources Board. Technologies that meet high emission-performance standards, termed "ultra-clean," and other low-emission distributed-generation technologies can expect a lessened impact from proposed departing-load fees, perhaps in the 1-cent-per-kilowatt-hour range.

Ultra-clean distributed generation is defined as those technologies that meet or exceed the standards set by the state Air Resources Board for 2007, including solar, wind, fuel cell and certain combustion technologies employing catalysts to reduce emissions.

Sound public-policy reasons dictate treating ultraclean distributed generation differently. As noted, dirtier, cheaper technologies may not be taking into account the future costs of deteriorating air quality. Restricting the ability of clean and efficient distributed-generation technologies to compete in the marketplace could force the state Air Resources Board to roll back its emission standards for distributed generation, which in turn would set back the timetable on the state's clean-air initiatives.

The growing market for trading emissions credits may alleviate some of the economic imbalance, but legislatively mandated subsidies and other economic incentives remain potent weapons in the environmentalists' arsenal.

Is clean distributed generation for real? The jury is out. Now is the time for interested parties to weigh in on the matter. The commission is under extreme pressure to find ways to pay for upcoming bond issues necessary to pay for above-market power costs and, in some instances, historical procurement charges. Commissioners may need to be persuaded that the state's energy bills can be paid without sacrificing its air quality.

Will departing-load fees be imposed? Most likely, although the extent of those fees may be tempered by recent legislative action that clearly encourages clean distributed-generation technologies. Depending on how the final commission decisions come down, even some direct-access customers may be looking to distributed generation to supplement their electricity load - and on an unexpected basis: cost.

As of Nov. 7, the Public Utilities Commission issued a final ruling adopting the 2.7-cents-per-kilowatt-hour direct-access cap, leaving assessment of the departing-load surcharge to be determined.

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