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BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.	Rulemaking 06-04-009 (Filed April 13, 2006)

ENERGY RESOURCES CONSERVATION
AND DEVELOPMENT COMMISSION
OF THE STATE OF CALIFORNIA

In the Matter of: AB 32 Implementation	CEC Docket 07-OIIP-01

COMMENTS OF THE CALIFORNIA CLEAN DG COALITION REGARDING COMBINED HEAT AND POWER POLICIES

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In accordance with the May 1, 2008 Administrative Law Judges' (ALJs') Ruling Requesting Comments on Combined Heat and Power Policies and the May 20, 2008 ALJs' Ruling Modifying Schedule and Correcting Suggested Outline for Comments and Reply Comments, the California Clean DG Coalition (CCDC) files these Comments Regarding Combined Heat and Power Policies.

CCDC is an ad hoc group interested in promoting the ability of distributed generation (DG) system manufacturers, distributors, marketers and investors, and electric customers, to deploy DG. Its members represent a variety of DG technologies including CHP, renewables, gas turbines, microturbines, reciprocating engines, and storage.[1] CCDC is committed to electricity markets that enable the best solutions for consumers, the environment, and the investor owned utilities (IOUs). CCDC's members operate in all 50 states.

[1] CCDC is currently comprised of Capstone Turbine Corporation, Caterpillar, Inc., Cummins Inc., DE Solutions, Hawthorne Power Systems, Holt of California, Johnson Matthey, Johnson Power Systems, Peterson Power Systems, Quinn Power Systems, RealEnergy, LLC, Solar Turbines Incorporated, Stowell Distributed Power Corp., Tecogen, Inc., and VRB Power Systems, Inc.

As stated in the Joint California Public Utilities Commission (CPUC) and California Energy Commission (CEC) Staff Paper on GHG Regulation for CHP (Joint Staff Paper), "CHP has the potential to lead to a significant net decrease in GHG emissions."[2] Through implementation of AB 32, the state has a tremendous opportunity to maximize the value of CHP resources and their recognized ability to contribute to reductions in CHP emissions. CCDC urges California to implement a greenhouse gas (GHG) policy and regulatory framework for CHP DG that sets the stage for the rest of the nation.

Following are CCDC's comments regarding certain questions posed in the May 1, 2008 ALJs' Ruling Requesting Comments on CHP Policies. CCDC's comments follow the outline established in the ALJs' May 13 and May 20, 2008 Rulings.

V. Treatment of CHP.

A. Detailed Proposal.

Question 1: Taking into account and synthesizing your answers to other questions in this paper, explain in detail your proposal for how GHG emissions from CHP facilities should be regulated under AB 32.

CHP designed and operated primarily for on-site power and thermal energy use, which meets an overall efficiency or GHG threshold as determined pursuant to AB 1613 (Qualifying Customer CHP), should be recognized as a GHG reduction measure. Such Qualifying Customer CHP should not be subject to GHG regulation, other than as may be appropriate to allow customer owners to realize the benefits of GHG emission reductions associated with Qualifying Customer CHP. For example, Qualifying Customer CHP owners should be allowed to elect to participate in any cap and trade program that may be established.

A standard methodology for calculating CHP GHG emissions should be adopted. CCDC recommends that the GHG emissions from a CHP unit, less the avoided boiler GHG emissions, be compared to the published marginal GHG emission rate of the local electric utility, adjusted for transmission and distribution losses. The difference is the GHG emissions reductions attributable to the CHP unit.

Qualifying Customer CHP should be included in an appropriate end-use sector. Because CHP reduces overall natural gas use and, therefore, reduces electricity purchases and associated

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[2] Joint Staff Paper, p. 9.

transmission and distribution losses, it is and should be treated within the sector as an energy efficiency measure. If it is determined that an end-use sector is not appropriate, CHP should be included in a separate CHP sector. Within any separate CHP sector, it may be necessary to further distinguish between Qualifying Customer CHP and CHP that exports power to the grid.

California has long recognized the benefits of CHP, including its potential to contribute to GHG emission reductions. The CPUC and CEC, and the Legislature, should continue their efforts to remove legal and regulatory barriers to CHP implementation in California. To achieve this goal, transmission and distribution congestion relief and capacity payments should be made, incentives for natural gas-fired DG should be reinstated, DG tariffs permanently eliminating standby charges should be adopted, nonbypassable charges should be eliminated, CHP DG should be allowed to serve microgrids, and the CHP recommendations set forth in the 2007 Integrated Energy Policy Report should be implemented.

B. Regulation of CHP GHG Emissions.

Question 2: Should GHG emissions from CHP systems be regulated in one sector? If so, which one? How?

CHP results in GHG emission reductions because a CHP unit creates two useful outputs – electricity and thermal energy – using a single fuel source. Even though CHP generates two types of energy, CCDC does not support splitting CHP emissions into two or more sectors (*e.g.*, the electric sector, the natural gas sector and/or the industrial or other end-use sector). Such an approach could easily result in overly complex, costly, and disparate regulatory treatment of similar units.

CCDC recommends that Qualifying Customer CHP be included in an appropriate end-use sector. Because CHP reduces overall natural gas use and, therefore, reduces electricity purchases and associated transmission and distribution losses, it is and should be treated within the sector as an energy efficiency measure. This means that measurement of Qualifying Customer CHP GHG emissions must properly account for avoided central power plant emissions and transmission and distribution losses. If it is determined that an end-use sector is not appropriate, CHP should be included in a separate CHP sector. Within any separate CHP sector, it may be necessary to further distinguish between Qualifying Customer CHP and CHP that exports power to the grid.

Question 9: Should CHP be part of a cap-and-trade program or not? If so, should the entire unit or certain CHP outputs be part of the cap and trade program?

CHP designed and operated primarily for on-site power and thermal energy use, which meets an overall efficiency or GHG threshold as determined pursuant to AB 1613 (Qualifying Customer CHP) should be recognized as a GHG reduction measure.[3] Such Qualifying Customer CHP should not be subject to GHG regulation, other than as may be appropriate to allow customer owners to realize the benefits of GHG emission reductions associated with Qualifying Customer CHP. For example, Qualifying Customer CHP owners should be allowed to elect to participate in any cap and trade program that may be established.

Question 16: Should CHP be considered an emission reduction measure under AB 32? Why or why not?

As stated above, CCDC recommends that CHP be considered an emission reduction measure under AB 32 because CHP results in less GHG emissions than does the purchase of electricity generated by a combined cycle generation turbine and use of thermal energy produced by a boiler.

For an apples-to-apples comparison of Qualifying Customer CHP and utility GHG emissions, the fuel chargeable to power for a Qualifying Customer CHP system can be calculated by subtracting the amount of fuel that would be required for thermal production in the absence of the Qualifying Customer CHP system from the amount of fuel that is consumed by the Qualifying Customer CHP system. The fuel chargeable to power can then be used to calculate the GHG emissions chargeable to power.

The figure below illustrates the net GHG (CO_2) emissions chargeable to power for several natural gas-fired on-site Qualifying Customer CHP technologies, assuming utilization of 100% of the usable heat and an offsetting boiler efficiency of 80%.[4] The figure compares the GHG emissions from various Qualifying Customer CHP technologies to (1) the GHG emissions from a natural gas plant operating at the maximum allowable GHG emissions as determined

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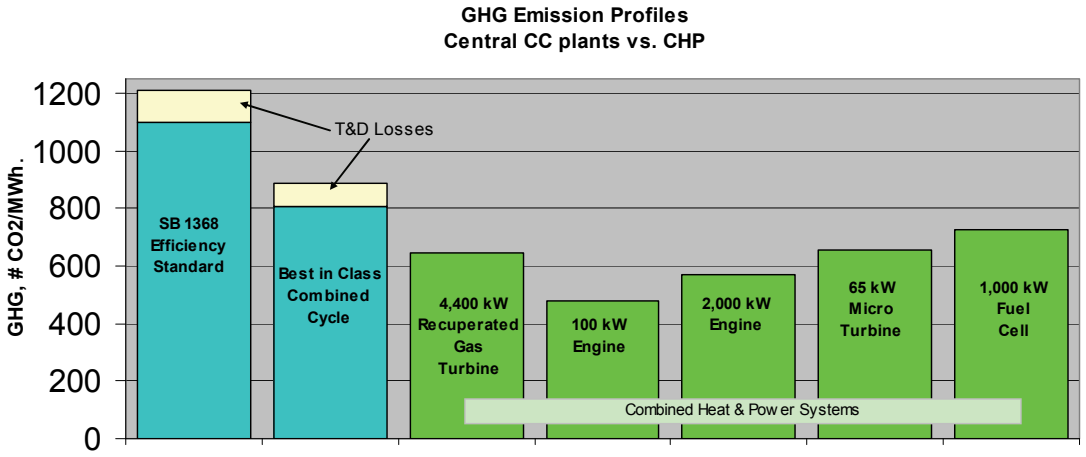
[3] AB 1613 (added by Stats. 2007, c. 713) enacted the Waste Heat and Carbon Emissions Reduction Act. (Pub. Util. Code §§ 2840-2845.) Public Utilities Code section 2843 sets a minimum efficiency standard of 60% for CHP, and directs the CEC to adopt guidelines for CHP subject to the Waste Heat and Carbon Emissions Reduction Act.

[4] A default boiler efficiency value of 80% should be used, unless a customer demonstrates a different value should be used at a particular site.

pursuant to SB 1368, and (2) a modern high efficiency combined cycle natural gas plant, both adjusted for transmission and distribution losses.[5] As shown, the net Qualifying Customer CHP GHG emission rates are 40 – 50% less than the SB 1368 benchmark. The difference between the net Qualifying Customer CHP emissions and whatever baseline emission is selected (*i.e.*, SB 1368 or marginal GHG rate), is the offset amount that should be credited to the Qualifying Customer CHP unit or system owner.

Although all the technologies illustrated below are "topping cycles", the same approach and methodology can be applied to "bottoming cycles" – subtract the fuel requirements without CHP from the fuel requirements with CHP and calculate GHG emissions.



As with electric efficiency measures, credit for the "indirect" central power plant emissions offset by the use of CHP must be provided to the Qualifying Customer CHP unit or system owner in order to motivate investment in CHP and the related GHG benefits. Any concept that a CHP system owner might have to purchase new power generation offsets for increased on-site GHG emissions associated with deployment of a Qualifying Customer CHP unit, without regard to off-site or indirect GHG emission savings would seriously stymie CHP implementation.[6]

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[5] SB 1368 (added by States 2006, c. 598) enacted Public Utilities Code sections 8340 and 8341. Section 8341 provides certain parameters for calculating GHG emissions from various types of energy generation facilities.

[6] *See* Comments of the Energy Producers and Users Coalition and the Cogeneration Association of California Regarding Interim Opinion on Greenhouse Gas Regulatory Strategies, pp. 10-13 (February 28, 2008).

Question 23: Should the Commissions pursue policy or programmatic measures to overcome some of the barriers to CHP deployment?

Yes. The benefits of CHP have long been recognized by the state. Those benefits include the potential for reductions of GHG emissions. The CPUC has characterized climate change as the "preeminent" environmental challenge of our time.[7] In order to ensure the benefits of CHP are realized, and to maximize the potential of the state's response to the climate change challenge, CCDC urges the Commissions to consider the following policy and programmatic measures to overcome some of the barriers to CHP deployment:

(1) Provide a one-time payment to Qualifying Customer CHP owners for transmission and distribution congestion relief.

(2) Provide incentive to the local electric utility to educate, assist, and promote the development of Qualifying Customer CHP. The Commissions should determine an appropriate incentive payment that declines over time.

(3) Adopt a CHP portfolio standard. The Commissions should determine annual amounts of power to be supplied by Qualifying Customer CHP.

(4) Provide annual avoided capacity payments to Qualifying Customer CHP. The current value of avoided capacity is in the vicinity of $100 per kW per year.

(5) Provide the option to Qualifying Customer CHP owners to procure natural gas at the IOUs' portfolio cost, to mitigate natural gas price volatility.

Other measures are discussed below in the context of existing legal and regulatory barriers, in response to Question 22.

D. Legal Issues.

Question 22: Are there other legal and regulatory barriers to CHP implementation in California that should be considered with respect to GHG regulation? If so, please explain in full with citations to specific relevant legal authorities. Also explain if and, if so, how the barriers could be avoided?

CCDC has long appreciated the CPUC's pronouncements indicating the "state's commitment to DG development."[8] Unfortunately, state policy favoring DG has not translated

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7 D.08-04-039, as modified by D.08-04-054, p. 2.

8 *See, e.g.*, Order Instituting Rulemaking Regarding Policies, Procedures and Rules for the California Solar Initiative, the Self-Generation Incentive Program (SGIP) and Other Distributed Generation Issues (OIR) issued March 17, 2008 (R. 08-03-008), p. 2.

to a viable market for DG, particularly CHP DG. The IOUs' testimony in the 2006 Long-Term Procurement Plan proceeding (R.06-02-013) shows that installations of small clean CHP DG occur at a snail's pace, and do not come close to achieving the potential that has been identified by the CEC.[9]

There are several legal and regulatory barriers to CHP implementation in California. Those barriers, and proposed solutions, are described below.

(1) *Barrier*: AB 2778, adopted in 2006, amended Public Utilities Code section 379.6 relating to the Self-Generation Incentive Program (SGIP). Among other things, AB 2778 limited the technologies eligible for SGIP incentives to qualifying wind and fuel cell DG projects, with the result that CHP DG is not currently eligible for such incentives.

Solution: CCDC recommends that the Commissions work with the Legislature to reinstate CHP as a technology eligible for SGIP incentives.

(2) *Barrier*: Uncertainty regarding the long-term status of the current interim exemption from standby reservation charges inhibits deployment of CHP DG. Public Utilities Code section 353.13(a) directs the CPUC to require that the IOUs establish new tariffs and rates for customers using DG that take into account the actual costs and benefits of DG. That same section also states the Legislature's clear preference that the required new DG tariffs continue on a long-term basis the existing "interim" standby charge exemptions. The required tariffs are to provide that "customers with similar load profiles within a customer class will, to the extent practicable, be subject to the same utility rates, regardless of their use of distributed energy resources . . . ." [10] Similarly, the 2007 Integrated Energy Policy Report (IEPR) recommends the elimination of standby reservation charges for CHP.[11]

Solution: The CPUC should perform the cost-benefit analysis required by Public Utilities Code sections 353.9, 353.13(a) and 2827(n) and develop the DG tariffs called for in section 353.13(a). Such tariffs should effectuate the Legislature's intent and the 2007 IEPR's recommendation to eliminate on a long-term basis standby reservation charges for DG.

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9 *See e.g.*, R.06-02-013, Exh. 10, Vol. 1, pp. IV-24 – IV-25 and Table Vol. 1, IVC-5 (PG&E); Exh. 21, p. 17 (SCE); and Exh. 43, Exhibits IV-3 and IV-4 and Assessment of California Combined Heat and Power Market and Policy Options for Increased Penetration, CEC and PIER Collaborative Report, prepared by the Electric Power Research Institute (November 2005) CEC-500-2005-173 (http://www.energy.ca.gov/2005publications/CEC-500-2005-173/CEC-500-2005-173.PDF), Table 2-2.

10 Pub. Util. Code § 353.13(a).

11 2007 IEPR, p. 212.

(3) *Barrier*: Existing and potential nonbypassable charges inhibit deployment of CHP DG. CPUC Decision 03-04-030 provides that certain nonbypassable charges apply to CHP DG. Additionally, in Rulemaking 06-02-013, the IOUs propose that additional new procurement-related nonbypassable charges should apply to DG, including CHP DG.[12]

Solution: Eliminate nonbypassable charges for CHP DG. This is not only good policy, but also consistent with the recommendation in the 2007 IEPR that the CPUC and CEC "work cooperatively to eliminate all nonbypassable charges for DG and CHP, regardless of size or interconnection voltage, and standby reservation charges for DG."[13]

(4) *Barrier*: Microgrids are not presently allowed under California law. Under Public Utilities Code section 218(b), the owner of a CHP unit may only sell electrical output from that unit to two adjacent consumers without becoming subject to regulation by the CPUC as a public utility. This restriction precludes installation of CHP DG at locations otherwise ideally suited to facilitate implementation of the benefits of DG. Such locations are referred to as microgrids, and include health care institutions, industrial and business parks, and technology and research campuses.

Solution: The CPUC and CEC should work with the Legislature to authorize the use of CHP DG to serve microgrids.

(5) CCDC also encourages the CPUC and CEC to consider and implement each of the recommendations in the 2007 IEPR intended to allow California to realize the significant system and efficiency benefits CHP applications provide to the distribution system.[14]

VIII. Conclusion.

CCDC appreciates the opportunity to provide these comments and respectfully urges the Commission to adopt the recommendations set forth herein.

DATED: June 2, 2008 DAY CARTER & MURPHY LLP

By: /s/ Ann L. Trowbridge
Ann L. Trowbridge

12 A proposed decision addressing these proposals has not yet been issued.

13 2007 IEPR, p. 212.

14 2007 IEPR, p. 212.

CERTIFICATE OF SERVICE

I, Paula S. Hefley, hereby certify that I served a copy of the **COMMENTS OF THE CALIFORNIA CLEAN DG COALITION REGARDING COMBINED HEAT AND POWER POLICIES** on June 2, 2008, on all known parties to Service Lists for R.06-04-009 via electronic mail to those whose addresses are available and via U.S. mail to those who do not have an electronic address as follows:

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Copies were also served by email to the California Energy Commission docket office at docket@energy.state.ca.us and to project manager Karen Griffin at kgriffin@energy.state.ca.us.

I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Executed on this 2nd day of June, 2008, at Sacramento, California.

/s/ Paula S. Hefley
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