

entities in a consistent, non-discriminatory manner. Staff's Response suggested other issues should be considered in this case to include: (1) whether renewable energy consumed on-site by QFs is energy "contracted for delivery;" (2) whether the Legislature has authorized the Commission to approve costs based on incentives to benefit existing and potential developers and owners of customer-owned renewable energy systems; and, (3) policy constraints the Commission should consider in approving any unbundling of RECs.

On December 5, 2005, El Paso Electric Company ("EPE") moved the Commission for an order finding that there was no case or controversy requiring a declaratory order because the issues raised are question of fact properly before the Commission in PNM's 2006 Procurement Plan case. The New Mexico Attorney General filed a Partial Response to Petition for Declaratory Order on December 7, 2005. In her Partial Response, the Attorney General indicated: (1) her general support for the Response filed by Staff to include the proposal that other issues be considered in this case; and, (2) that the public interest would be served by a comprehensive review of the matters raised in PNM's Petition for Declaratory Order that would apply to all affected entities in a consistent, non-discriminatory manner.

The Commission entered its Order Docketing Case on December 13, 2005. In its Order, the Commission found that it should: (1) exercise its discretion to entertain PNM's Petition in whole; (2) deny EPE's Motion to Dismiss; and, (3) not decide Staff's request to broaden the scope of the case. The Commission's Order designated Lee Huffman as Hearing Examiner to preside over the case and to consider whether to broaden the scope of the case.

The Notice attached to the March 3, 2006 Procedural Order issued by the Hearing Examiner states that he would consider the following six issues in this docket:

1. Whether a public utility has discretion to acquire, or not to acquire, RECs from a QF from which it purchases energy under NMPRC Rule 17.9.570 NMAC.
2. Whether it is reasonable and prudent for a public utility to pay value for RECs, whether or not acquired with the associated energy.
3. Whether renewable energy consumed on-site by a QF is energy “contracted for delivery” and thus usable to meet a utility’s renewable portfolio standard.
4. Whether the Legislature has authorized the Commission to approve incentives to benefit existing owners of customer-owned renewable energy systems.
5. Whether there are any policy constraints the Commission should consider in approving any unbundling of RECs.
6. Whether energy and RECs must be obtained by a utility in order for an energy purchase to be considered a purchase from a renewable QF and, if so, what is the avoided cost which utilities should pay for bundled energy and RECs.

Argument

Upon review of the oral and pre-filed testimonies in this case, it is apparent that the parties agree more than disagree on the six issues listed above. The major area of disagreement is whether renewable energy consumed on-site by a QF is energy contracted for delivery.

Issue 1

All parties, with the exception of PNM, agree that a public utility has discretion to acquire, or not to acquire, RECs from a QF from which it purchases energy under NMPRC Rule 17.9.570 NMAC (“Rule 570”). Tr.: Southwestern Public Service Company (“SPS”) Ex. 1, pp. 6-7; El Paso Electric Company (“EPE”) Ex. 1, p. 9; Coalition for Clean Affordable Energy (“CCAЕ”) Ex. 1, p. 3; Staff Ex. 2, p. 2. There is

agreement among these parties that §62-16-5(B)(1) of the Renewable Energy Act (REA”) gives utilities this discretion.

PNM is the only party that that may question whether a utility has discretion to acquire, or not to acquire, RECs from a QF from which it purchases energy under Rule 570. Tr., Public Service Company of New Mexico (“PNM”) Ex. 1, p. 6. As stated by PNM, Rule 570 does not address RECs since the rule was promulgated prior to the passage of the REA. Tr., PNM Ex. 1, p. 7. And, as indicated by the company, §62-16-5(B)(1)(a) 2) provides that when a utility buys renewable energy from a QF, it automatically owns the RECs unless they are retained by the generator through specific agreement with the utility. Tr., PNM Ex. 1, pp. 8-9.

Commission Rule 570 can’t be read in a way that would contradict the language of the Renewable Energy Act. Stated another way, Rule 570 must be read in a way that would conform to the provisions of the REA. Because of this, Staff is not sure why PNM would question its ability to acquire, or not acquire, RECs when it purchases energy from a QF under Rule 570. Perhaps the Rule 570 uncertainty that PNM wants the Commissions to remove is: when it would be appropriate for a utility not to acquire RECs? Tr., PNM Ex. 1, p. 11. If this is the case, when the expert witness for EPE, SPS and Staff addressed this issue, none of them could come up with a reason for a utility not to keep the RECs. Tr., pp. 91-92, 108-109, 145, 162, 174-177.

Issue 2

All parties agree that it could be reasonable and prudent for a public utility to pay value for RECs, whether or not, acquired with the associated energy. However, the basis for the parties’ position on this issue differ. PNM agrees because it believes that RECs

have commercial value apart from any energy purchased by a utility from a QF and that in the interest of fairness, utilities out to compensate QFs separately for RECs. Tr., PNM Ex. 1, pp. 6, 13-14. SPS agrees because it believes that it could be reasonable and prudent for a utility to acquire RECs independent of Energy and that the forum for making this determination is in a public utility's annual renewable energy procurement plan proceeding. Tr., SPS Ex. 1, pp. 4. EPE takes the position that the issue of whether it would be reasonable and prudent for a public utility to pay value for RECs independent of energy depends on the facts and circumstance of each purchase. Tr., EPE Ex. 1, pp. 9-10. CCAE maintains that RECs intrinsically involve the unbundling of environmental attributes from energy and that the issue of whether it would be reasonable and prudent for a public utility to pay value for RECs independent of energy depends on Commission approval of such a purchase in a public utility's annual renewable energy procurement plan proceeding. Tr., CCAE Ex. 1, pp. 4-5.

Staff also agrees that it could be reasonable and prudent for a public utility to pay value for RECs, whether or not acquired with the associated energy, if: (1) the purchase was a reasonable cost option; and, (2) the associated energy must have been sold at retail by a utility to New Mexico electric consumers. Tr., Staff Ex. 2, pp. 3-4. Staff takes this position for several reasons. First, this position comports with the provisions of: (1) §62-16-5(A), which provides for renewable energy certificates that can be used by a public utility to establish compliance with the renewable portfolio standard ("RPS"); (2) §62-16-3(E), which defines RPS to mean percentage of retail sales by a public utility to electric consumers in New Mexico; and, (3) §62-16-5(B)(1)(b), which allows a transaction such as EPE's purchase of RECs from PNM. Second, the reasonable cost option comports

with the concept that a utility must provide its electric service at fair, just and reasonable rates.

Staff believes that the testimony of the expert witnesses for PNM and EPE support Staff's position that the renewable energy represented by RECs purchased without energy must be sold at retail by a utility to New Mexico electric consumers. The witnesses for EPE, Mr. Thomas Newsom, declared that when EPE purchased RECs from PNM, it was EPE's intent to take credit for renewable energy generated and contracted for delivery in New Mexico that the RECs represent. Mr. Newsom also stated that "there is a presumption that it [renewable energy] is going down all the way to the retail customer level." Tr., pp. 103-104. The statements of PNM witness, Mr. Patrick Scharff, are in basic agreement with Mr. Newsom's testimony. The main difference between the two testimonies is that Mr. Scharff maintains that the energy represented by the RECs could be "delivered to a specific customer or for a load that would otherwise be served." Tr., pp. 45-46.

Issue 3

The issue of whether renewable energy consumed on-site by a QF is energy "contracted for delivery" and thus usable to meet a utility's renewable portfolio standard is a key and contentious issue in this case. PNM, SPS and CCAE contend that energy consumed on site results in RECs that can meet the renewable energy standard set out in the Renewable Energy Act. Staff and EPE do not agree with the stated positions of PNM, SPS and CCAE.

PNM bases its contention regarding energy consumed on site on the "language in Rule 571," and on "considerations of public policy that favor the development of

renewable resources.” Tr., PNM Ex. 1, p. 15. Notably, PNM bases its contention concerning the meaning of the words that are found in the REA on a rule that was issued by the Commission years before enactment of the REA. Also, the Direct Testimony of Mr. Scharff fails to mention any sections of the REA that would support his stated position. In his response to Staff’s position that energy consumed on site is not contracted for delivery, Mr. Scharff indicates in his Rebuttal Testimony that the REA does not make any reference to a sale being required for a REC to be created. Tr., PNM Ex. 2, p. 6. As will be discussed below, Staff maintains that this statement is incorrect when all provisions of the REA are considered.

In his Direct Testimony pre-filed on behalf of SPS, Mr. Butler states that “the Commission should broadly interpret Rule 572 as it concerns QF on-site renewable energy generation and consumption to best promote renewable energy development.” Tr., SPS Ex. 1, p. 10. Mr. Butler does not address on-site energy consumption in his Rebuttal Testimony. The stated purpose of Rule 572 is to implement the REA and to bring significant economic development and environment benefits to New Mexico. 17.9.572.6 NMAC. If the provisions of Rule 572 were contrary to the requirement of the REA, which they are not, Rule 572 would be illegal. Support for SPS’s contention regarding energy consumed on site must be found, if at all, in the REA - not in Rule 572.

Mr. Luce states in his Direct Testimony pre-filed on behalf of CCAE that energy consumed on-site by a QF is energy contracted for delivery “as long as there is some kind of contract governing the delivery of the energy ...” He also states that interconnection and energy delivery of all grid-connect systems ... is always governed by a contract between the QF and the public utility.” Tr., CCAE Ex. 1, p. 5. While it is true that

interconnection agreements govern energy delivery to the grid, Staff has a problem with the concept that energy can be contracted for delivery even if there is no energy to deliver. This approach would seem to be more in the realm of imagination than contract reality.

Mr. Luce addresses the definition of renewable portfolio standard that is found in the REA in his pre-filed Rebuttal Testimony. Mr. Luce acknowledges RPS language that requires a percentage of retail sales to be supplied by renewable energy. However, he argues that the RPS language does not address how a utility is to achieve the required percentage of retail sales. Tr., CCAE Ex. 2, p. 4. It is true that the RPS definition does not address how a utility is to achieve the required percentage of retail sales. But, this does not explain how renewable energy that does not exist can be acquired by a utility to be used as part of a utility's retail sales to New Mexico customers.

EPE, like Staff, take the position that renewable energy consumed on-site by a QF is not energy "contracted for delivery" and not usable to meet a utility's RPS. EPE's expert witness, Tom Newsom, argues that under the REA, a REC requires that the associated energy be purchased by a utility or otherwise contracted for delivery into New Mexico. Tr., EPE Ex. 1, p. 11. Mr. Newsom also argues that because energy consumed by a customer is not metered and contracted for delivery, those kWh are not usable to meet a utility's RPS. **Id.** Staff agrees with Mr. Newsom's arguments.

Staff arrived at its conclusion that renewable energy consumed on-site by a QF is not energy "contracted for delivery" and not usable to meet a utility's RPS after considering the following statutory language:

1. The RPS is defined in the REA as the percentage of retail sales by a public utility to electric consumers in New Mexico that is required by the REA to be supplied by renewable energy. §62-16-3(E)¹.
2. The Legislature found in §62-16-2(A)(3) that public utilities should be required to include prescribed amounts of renewable energy in their electric energy supply portfolios for sales to retail customers in New Mexico.
3. The Legislature declares in §62-16-2(B)(1) that one of the purposes of the REA is to prescribe the amounts of renewable energy resources that public utilities shall include in their electric energy supply portfolios for sales to retail customers in New Mexico.
4. The RCT is defined in §62-16-3(C) as the cost established by the Commission above which a public utility shall not be required to add renewable energy to its electric energy supply portfolio pursuant to the RPS.
5. Section 62-16-4(C) sets a date for the Commission to establish the RCT above which level a public utility shall not be required to add renewable energy to its electric energy supply plan.
6. Sections 62-16-4(C)(1) through (5) all refer to factors related to renewable energy that the Commission must take into account when it establishes and modifies the RCT.
7. Section 62-16-4(D) sets the date for a public utility to file a report to the Commission on its purchases of renewable energy during the prior calendar year.
8. Section 62-16-5(A) provides that the Commission is to establish a system of renewable energy certificates that can be used by a public utility to establish compliance with the RCT.

RECs establish compliance with the RCT. The RCT requires that a percentage of the retail sales made by a public utility to electric consumers in New Mexico be supplied by renewable energy. Renewable energy consumed by a generator is not available for a public utility to either acquire for sale to retail consumers or to contract to deliver.

¹ The RPS definition is not is not ambiguous and therefore not subject to construction.

Accordingly, Staff does not believe that RECs can't exist in the absence of renewable energy for a public utility to contract to deliver or for a utility to acquire for retail sale.

Issue 4

The parties have taken a variety of positions concerning whether the Legislature has authorized the Commission to approve incentives to benefit existing owners of customer-owned renewable energy systems. PNM maintains that although the REA does not specifically address incentives, the Commission should allow compensation for RECs to existing as well as to new owners of renewable energy system. The basis for this position is that the REA “finds that the generation of electricity through the use of renewable energy presents opportunities to promote energy self-sufficiency, preserve the state’s natural resources and pursue an improved environment.” Tr., PNM Ex. 1, pp. 6, 18.

While agreeing with PNM’s position, Staff questions PNM’s statement that it is inaccurate to characterize payments made for RECs as incentives. Tr., PNM Ex 2, p. 9. Payments made for RECs increase the amount of compensation received by renewable energy generators. This would appear to be an incentive. This is especially true for those types of renewable generation with higher RCTs.

SPS answer to the fourth issue is that the Legislature has not authorized the Commission to approve incentive to benefit owners of renewable energy systems installed prior to July 1, 2004. Tr., SPS Ex. 1, pp. 5, 11. EPE takes the same position as SPS. Tr.: EPE Ex. 1, p. 11; EPE Ex. 2, p. 13. CCAE does not directly address Issue 4. Rather, it states that the REA “does not deal with incentives, per se” and that “the question of incentives, per se, is simply irrelevant.” Tr., CCAE Ex. 1, p. 6.

Staff notes, as do other parties, that there is no explicit authorization in the REA to approve incentives to existing customer-owned renewable energy systems. Tr., Staff Ex. 2, p. 7. However, as pointed out in Staff's testimony, the REA does not address the age of the resources generating renewable energy. Tr., Staff Ex. 2, p. 8. If payments made above avoided cost for renewable energy with RECs are considered to be an "incentive," then by definition, an incentive is paid when a utility pays more than avoided cost for renewable energy and RECs - even if it is to existing owners of customer-owned renewable energy systems.

Issue 5

The fifth issue to be considered in this docket is whether there are any policy constraints the Commission should consider in approving unbundling of RECs. There is a wide range of responses to this issue. PNM states that it has not identified any. Tr.: PNM Ex 1, pp. 6, 19. CCAE finds the question confusing because in its view "RECs intrinsically involve an unbundling of RECs from energy." CCAE Ex. 1, p. 7. Staff agrees with the comments of SPS and EPE which are to the effect that unbundling must be in accordance with applicable law. Tr.: SPS Ex. 1, pp. 5, 12; EPE Ex. 1. p. 12.

While no one could argue that REC unbundling does not have to follow applicable law, this answer may be what the Hearing Examiner had in mind when he posed the question. Staff recommends that the Commission direct utilities to: (1) procure RECs principally for meeting their RPS requirements, not for trading activity; and, (2) adopt strategies to minimize cost impact on ratepayers. Staff's recommendation that utilities procure RECs principally for meeting their RPS requirements is criticized.

PNM's response to Staff's first recommendation is that "RECs represent important property interests that ought, to the extent not restricted by specific state laws or regulations, to be freely transferable between willing buyers and sellers, like any other property interest." Tr., PNM Ex. 2, p. 10. Staff does not believe that its recommendation restricts the transfer of property interests by generators. Rather, Staff's recommendation applies to public utilities in order to insure that utilities do not engage in diversified activities and subject their customers to market place risk. The business of New Mexico electric public utilities is to provide electric service to their customers, not to engage in the buying and selling of RECs.

EPE disagrees with Staff's recommendation concerning utility acquisition of RECS. One of the reasons given for this disagreement is that EPE believes that the recommendation is contrary to the provisions of the REA. One of the reasons advanced by EPE in support of this belief is that the Commission does not have the jurisdiction to dictate whether a utility can negotiate with a QF for the QF to retain RECs. Tr., EPE Ex. 2, p. 5. Staff does not, however, understand the relevance of this argument. If a QF retains RECs associated with renewable energy sold to a utility, this would not lead to the utility acquiring excess RECs.

EPE also disagrees with Staff's recommendation concerning utility acquisition of RECs because it believes that this would restrict a utility's ability to account for mismatches in any given year. Tr., EPE Ex. 2, pp. 5-6. Staff's recommendation, however, does not prohibit a utility from acquiring extra RECs in order to insure compliance with the REA. EPE also indicates that the REA allows acquisition of excess RECs for arbitrage purposes. Tr., EPE Ex. 2, p. 6. Staff believes this

proposition is highly questionable in the absence of Commission approval due to the risk that utility ratepayers would be exposed to. Last, EPE indicates that the REA contemplates that RECs can be traded and sold. **ID.** While this may be true, this doesn't mean that the Commission must allow electric utilities to buy and sell RECs in the market place.

The reason that Staff uses the word “principally” in its recommendation that utilities procure RECs in order to meet their RPS requirements, is to allow utility acquisition of RECs when the associated energy is less expensive than avoided cost. Utilities with fuel clauses, will reduce ratepayer cost when sale proceeds of RECs that accompany low cost energy are credited against their balancing accounts. When an electric utility without a fuel clause, such as PNM, sells RECs a problem arises concerning how to credit the proceeds of the sale to the utility's customers.

Issue 6

While the responses of the parties to Issue 6 differ, the parties appear to generally agree, consistent with their answers to Issue 1, that pursuant to the provision of the REA, RECs accompany a purchase of renewable energy from a QF, unless otherwise agreed to by the utility and generator. The parties also generally agree that Commission rule 570 and 571 govern the avoided cost which utilities pay for bundled renewable energy and RECs.

Conclusion

For the reasons stated above, Staff recommends that the Commission find: (1) that a utility has the discretion to acquire, or not to acquire, RECs from a QF from which it purchases energy under NMPRC Rule 17.9.570 NMAC; (2) it is reasonable and

prudent for a public utility to pay value for RECs purchased to satisfy its RPS if, it is a least cost option and the associated energy meets the requirement of the REA; (3) renewable energy consumed on-site by a QF is energy “contracted for delivery” and thus usable to meet a utility’s renewable portfolio standard if it is the subject of a buy sell agreement; (4) the Legislature has authorized the Commission to approve incentives (RECs) that benefit existing owners of customer-owned renewable energy systems; (5) the Commission should direct utilities to procure RECs principally to meet their RPS and to adopt strategies to minimize cost impact on ratepayers; and, (6) RECs are obtained by a utility under the provision of the REA at the avoided cost calculated under the provisions of Rules 570 and 571.

Respectfully submitted,

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