

April 8, 2010

Mr. Gary Collord
California Air Resources Board
1001 I Street
Sacramento, CA 95812

RE: Comments on Draft Renewable Electricity Standard (RES)

Dear Mr. Collord:

The Royal Bank of Scotland plc (“RBS”) appreciates the opportunity to comment on the Preliminary Draft Renewable Electricity Standard (“RES”) being developed by the California Air Resources Board (CARB) as directed by Executive Order S-21-09¹. The RES builds upon California’s existing Renewable Portfolio Standard (“RPS”) and raises the procurement target from 20 to 33 percent.

RBS is a public limited company registered in Scotland, is a financial holding company under the U.S. Bank Holding Company Act of 1956, as amended, and is engaged in a full range of banking, capital markets, and asset management activities. RBS has a fifty one (51%) percent ownership interest in Sempra Energy Trading LLC (“SET”). SET is a full-service energy trading company that markets and trades physical and financial energy and metals products, including electric power, natural gas, crude oil, base metals, and associated commodities. SET is authorized to sell energy, capacity, and ancillary services at market based rates and transacts within all the Regional Transmission Organizations, including the California Independent System Operator (“CAISO”).

Our comments today are with regard to the use of Renewable Energy Credits (“RECs”) in meeting RES targets. In general, RBS supports approaches that would allow the maximum flexibility for regulated entities to meet RES targets by allowing access to the widest set of eligible resources. According to Executive Order S-21-09, eligible resources may be located anywhere within the Western Interconnection. The different types of approaches that can be used to meet RES/RPS targets from renewable resources outside of California have been classified as:

1. Bundled energy and REC transactions that are dynamically scheduled into California,
2. Energy and REC transactions with firm transmission that are not dynamically scheduled,
3. “Firming and shaping” transactions that re-bundle RECs with firm power, and
4. REC-only or Tradable REC (“TREC”) transactions.

The first category of bundled dynamically scheduled transactions is currently not widely available due to technical limitations at the CAISO. This type of transaction would require firm transmission into the CAISO and would rely on the CAISO for firming services. The second set of transactions also represents bundled energy and REC transactions except they are not dynamically scheduled. These transactions require firm transmission from the eligible facility to the CAISO but rely on the source Balancing Authority rather than the CAISO to firm up the schedule across the hour. The third category of “firming and shaping” transactions involves re-bundling of eligible RECs with firm power delivered at the California border as defined in delivery rules established by the California Energy Commission (“CEC”) ². These transactions do not require any transmission reservation and do not rely on the CAISO for firming services. The volumes of such transactions within a calendar year are limited by the actual RPS eligible MWhs that are generated within the Western Interconnection in that calendar year. The fourth category is the only category representing unbundled REC transactions and was not authorized until recently.

While the objective of the March 11 CPUC Decision authorizing TRECs is to allow added flexibility for compliance, we believe its practical impact in the near term will be just the opposite. This results from two aspects in the decision. The first is an interim cap of 25 percent on REC-only or TREC transactions and the second a potential mischaracterization of “firming and shaping” transactions and non-dynamically scheduled imports as TRECs.

¹ Executive Order S-21-09 <http://gov.ca.gov/index.php?executive-order/13269/>.

² Renewables Portfolio Standard (RPS) Eligibility Guidebook, Dec 19, 2007 <http://www.energy.ca.gov/2007publications/CEC-300-2007-006/CEC-300-2007-006-ED3-CMF.PDF>.

The classification of “firming and shaping” transactions as TRECs overlooks important differences between the two types of transactions. While a TREC or REC-only transaction fixes the price of the REC, a “firming and shaping” transaction also fixes the price of the associated power just as a bundled energy and REC transaction would. Additionally, while TRECs may be perceived as a new market instrument requiring the use of a cap, “firming and shaping” transactions have been used for some time. The classification of “firming and shaping” transactions as TRECs and the consequent application of a 25 percent interim cap will stymie further contracting with renewable resources outside California. This could adversely impact renewable development at a time when federal stimulus funds are still available for new projects that commence construction in 2010.

The CPUC Decision makes the delivery from dynamically scheduled facilities the only uncapped option for meeting RPS targets. The rationale for this approach is unclear as it does not seem to provide any useful societal purpose. A MWh of energy from an RPS eligible facility generated anywhere in the Western Interconnection that displaces a MWh of energy from a Green House Gas (“GHG”) emitting resource should produce a GHG reduction regardless of where the displacement occurs. In some instances, if the output from a coal facility is displaced outside of California, the GHG reduction may be even higher.

Similarly, given the interconnected nature of the electrical grid, it is physically impossible to separate renewable energy from fossil energy and therefore the focus should be on verification that the RPS eligible facility has actually generated renewable energy and displaced fossil MWhs rather than a proposal to track which MWhs ultimately reach California consumers. This would expand the pool of eligible resources and ultimately result in the lowest REC prices for consumers. It is also important to recognize that just as the grid is interconnected so are the market clearing prices of electricity in that interconnected grid. California consumers benefit when more supply is on the grid even if that supply is in another state or province.

It is well known in the industry that intermittent energy resources require some type of firming arrangement to make the underlying energy useful. “Firming and shaping” transactions, as well as TRECs, allow for firming of intermittent energy resources to be done where it is most effective and economical to do so. For example, if hydro flexibility in the Northwest allows for easier and less expensive ways of addressing the intermittency of variable energy resources, then it would make sense to allow that option rather than force that responsibility onto the CAISO through a dynamically scheduled import. From a GHG minimizing perspective, the balancing by hydro resources instead of by fossil resources within California may offer additional benefits.

While quantifying the precise costs and GHG reductions associated with different types of firming arrangements is not easy, administratively precluding some arrangements in favour of others without such analysis will not lead to the lowest cost for consumers. Least cost solutions arise from finding the best fit of resource basin, compatible land use, access to transmission and balancing resources. Maximizing use of the existing grid and existing resources should be encouraged, not discouraged. Indeed, more alternatives for firming arrangements and more sources of supply will lead to more efficient use of land and transmission resources.

Finally, we realize there are real operational challenges and costs that entities in the Northwest must deal with in integrating renewable resources used to back exports to California. For example, the Bonneville Power Administration’s Wind Integration Tariff charges a fixed fee for wind generators that interconnect within its system to provide energy imbalance, regulation and load following services. If such services were to be available for a lower cost within California, that would be reflected in contracting and development decisions.

We thank you for the opportunity to provide comments on the Draft Renewable Energy Standard.

Sincerely,

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