

Ferguson: Energy Matters

March 28, 2008

Obsolete Referent

The Market Price Referent, universally known to insiders as the MPR, is an arcane holdover from the heady days of deregulation over a decade ago. The MPR has never been useful and today is a liability. It's time to abandon the obsolete MPR.

In 1996, as readers know, California started experimenting with a deregulated electricity market operated by the California Power Exchange. For every hour of every day, an electricity price was established in the CalPX market. As you also know, the price didn't turn out to be cheap, but that's another story.

We advocates worried about the ability of renewable-powered electricity, like wind and solar, to compete in the marketplace against relatively "cheap" gas-fired power power plants. As a result, AB 1890—the 1996 deregulation legislation—included establishment of a "public goods charge." Some of the funds from this line on your electric bills is allocated to defray the expected "above market price" for renewable energy.

The chaos that deregulation created deterred building new power plants. Funds for building renewable generation were never used.

After the deregulated wholesale market collapsed, the state began another dubious experiment with renewable energy known as the renewables portfolio standard. According to the renewables law, all California utilities are supposed to obtain 20 percent of their electric energy from alternative energy by 2010.

Utilities, however, were given an escape hatch—if renewable energy cost too much, the utilities didn't have to meet the target.

But how much is economically "too much"? Enter the misnamed "market price referent." Since there was no longer any electricity market, the regulators were instructed to guess what the market price would be if there were a well-functioning market. That guess is the MPR, the average market price of electricity—as predicted by the bureaucrats—for the next 20 years.

The accumulating public goods funds were to be used to defray the cost of renewables purchased by utilities if the cost exceeded the MPR by making supplemental energy payments. If these supplemental funds were ever depleted, the renewables portfolio standard requirement would be lifted.

Recently the SEP account was moved from the Energy Commission and allocated to the utilities for administration. A workshop was held March 27 to discuss the latest market price referent calculations.

To the best of my knowledge the arcane market price referent scheme—even with the supplemental funds—has not led to the construction of a single new renewable energy generating facility, even though the state is nowhere close to meeting the renewables portfolio standard target. The whole idea of the market price referent has been a dismal failure.

The biggest flaw in the market price referent scheme is the guesswork involved in setting a pseudo-market price for 20 years into the future. The assumption is that the marginal cost of electricity for the next 20 years will be determined by the cost of gas-fired power. So the market price referent gurus must guess what the price of gas will be for the next 20 years. Good luck.

Earlier market price referent guesstimates completely missed the dramatic increase in gas prices in recent years. The market price referent methodology continues to predict that natural gas will be cheaper 20 years hence than it is today.

Does anybody really believe this? I think not.

Moreover, there is something perverse about using the cost of fossil power to cap the price for renewables. There has never been a cap placed on the price utilities can pay for natural gas. When gas prices go up, the cost is passed directly through to ratepayers at no risk to the utilities.

Why does brown power with volatile prices get a free ride from the regulators, whose gas price forecasts have been terribly wrong, while green power with known and reasonable long-term prices is confined to the market price referent ghetto?

There is a growing consensus among advocates, utilities, regulators and even the governor's office, that the market price referent is worse than useless and should be abandoned. It's time to pull the plug on the market price referent.

The alternative under discussion is to make utility renewable contracts subject to reasonableness review as are other contracts. But what, then, is a "reasonable" price to pay for renewable energy?

One answer has recently been provided by Arizona. Arizona Public Service has signed a 30-year contract for substantial amounts of solar power with Abengoa Solar, a well-known Spanish developer. The 280 MW facility reflects sunlight with curved mirrors to heat oil which drives a conventional steam turbine. California built a series of such plants in the 1980s, but nothing since. Moreover, the new facility includes thermal storage for several hours of operation, making the plant "dispatchable" for the grid to meet varying demand.

The price of the APS solar contract over 30 years is 14 cents/kWh as reported by the *Wall Street Journal*. When you stop to think about where natural gas prices are apt to be even 10 years from now, you'll agree that 14 cent/kWh solar energy is a real bargain.

Is California, land of talk about global warming, going to play second solar fiddle to Arizona?

California should go its neighbor one better and offer to buy **all** the solar power anyone wants to sell for 14 cents. An executive order to that effect would be something the governor could justifiably brag about.

If California is serious about global warming, it will no longer base its energy procurement policies on the estimated price of fossil electricity much less on predictions that the price of gas will not increase in the next 20 years.

Go with what works! Get rid of the market price referent and offer a reasonable price for solar and other renewable generation! What a concept.

—Dr. Rich Ferguson, Research Director, CEERT, rich@ceert.org.
Opinions expressed by DrF are not necessarily those of any organization with which he is affiliated.