

May 28, 2010

Ms. Mary Nichols, Chairman
Mr. James Goldstene, Executive Officer
Mr. Dave Mehl
Mr. Gary Collord
California Air Resources Board
1001 I Street
Sacramento, CA 95814

Re: 3Degrees Comments on ARB's Renewable Electricity Standard Preliminary Draft Regulation

Dear Ms. Nichols, Mr. Goldstene, Mr. Mehl, and Mr. Collord,

3Degrees appreciates the opportunity to provide comments on the Renewable Electricity Standard (RES) Preliminary Draft Regulation (PDR), released on May 14, 2010. We commend the Air Resources Board (ARB) for its recognition that a 33% RES is crucial to achieving the greenhouse gas (GHG) reduction goals under AB 32. Specifically, we support ARB's decision to (a) impose no limits on the use of unbundled renewable energy credits (RECs), (b) allow REC trading by non-regulated parties, and (c) prevent double counting of RECs sold into the voluntary market. These are all components of sensible regulation that achieves GHG reductions in the most cost-effective manner while ensuring the environmental integrity of the RES.

One aspect of the RES that still is a point of concern for 3Degrees, however, is a portion of the proposed REC definition in Section 97002(a)(15). The language stating that "[a] REC does not constitute property or a property right," does not accurately reflect the nature of RECs, the present status of various markets for RECs, or their current treatment by other State and Federal agencies. Additionally, Section 97002(a)(15) would incur unintended consequences upon existing REC markets and REC market participants and likely does not accomplish the goal of shielding ARB from regulatory takings claims under the 5th Amendment to the United States Constitution.¹

An effective way to mitigate these risks would be to amend the language to read "*The RES compliance value of a REC does not constitute property or a property right.*" This would focus the definition only on rights created under AB 32, address regulatory takings concerns, align RES REC treatment with other State and Federal Agencies, and prevent market and contractual uncertainty that would stem from not recognizing existing property rights in RECs.

¹ USCA CONST. Amend. V. (West 2010), see also, Pennsylvania Coal Co. v. Mahon, 260 U.S. 393, (1922).

Property Rights in RECs Already Exist Under California Law

California Civil Code section 654 defines property in terms of ownership: “[t]he ownership of a thing is the right of one or more persons to possess and use it to the exclusion of others. In this Code, the thing of which there may be ownership is called property.”² The ability of individuals and businesses to own and use RECs to the exclusion of others, in voluntary markets in California and voluntary and compliance markets in other States, brings RECs squarely within the understanding of what constitutes property in California. These property rights in RECs exist in addition to the ability of parties to use RECs for compliance with California regulatory requirements.

Furthermore, the California Public Utility Commission (CPUC) has determined that distributed generation (DG) RECs are owned by the generator, acknowledging property rights under California law in DG RECs through the recognition of their exclusive ownership by the party creating them.³ This ruling by the CPUC acknowledges that the underlying property rights of RECs exist and can be created, owned, and traded outside of government programs.

Declaring that RECs Do Not Constitute Property or Property Rights Would Incur Unintended Consequences Upon Existing REC Markets and REC Market Participants.

As drafted, Section 97002(a)(15) would create serious market and regulatory uncertainty because the ability of parties to enforce existing and future contractual obligations and pursue remedies would be unclear. Denying the property nature of RECs would also put in jeopardy the ability of investors and lenders to obtain security interests in RECs, and investment in renewable energy could be hurt as a result.

Presently, commentators in California agree that RECs constitute property, although the specific type of property which RECs constitute has not yet been formally determined by the courts.⁴ ARB’s proposed language would cause creditors to parties owning RECs to reconsider whether they will be able to perfect a security interest in a product which a California regulatory agency has determined is not property. It is possible that creditors would not accept the risk that they may be unable to perfect their security interests, or that creditors would not grant credit on terms as favorable to the debtor. The resulting change in present business practices would make it much more difficult for parties seeking to secure credit to pledge their RECs as collateral.

The proposed language of Section 97002(a)(15) is also inconsistent with the treatment of RECs by the CPUC, the Western Regional Energy Generation Information System (WREGIS), and the United States Environmental Protection Agency (EPA). The EPA website states that a REC “represents the property rights to the environmental, social, and other nonpower qualities of renewable electricity generation.”⁵ Both the definition of a WREGIS Certificate⁶ and the CPUC’s

² [Cal. Civ. Code § 654](#), see also, [Bady v. Detwiler](#), 127 Cal. App. 2d 321, (2d. Dist. 1954).

³ CPUC [Decision 07-01-018](#) (conclusions of law no. 3).

⁴ See [RECs In Secured Transactions Under Calif. Law](#), available at http://www.lw.com/upload/pubContent/_pdf/pub2572_1.pdf.

⁵ See <http://www.epa.gov/grnpower/gpmarket/rec.htm>

⁶ WREGIS, [Modified WREGIS Certificate Definition](#)

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definition of Green Attributes⁷ recognize that RECs may be used for purposes other than compliance. The proposed language in Section 97002(a)(15) would add regulatory uncertainty surrounding RECs, which could discourage investment in RECs and renewable energy.

Declaring that RECs Do Not Constitute Property or a Property Right Does Not Shield ARB from Regulatory Taking Claims

3Degrees recognizes the concern that acknowledging the property aspects of RECs could expose ARB to claims of a government taking under the 5th Amendment to the United States Constitution. However, Section 97002(a)(15) as drafted would not provide the desired protection and might in-fact increase the ARB's risk to claims of uncompensated takings by negatively affecting existing property rights in RECs.

Some emission allowance programs have provided by statute, that allowances do not constitute property rights.⁸ These provisions ensure that subsequent reductions in allowance allocations will not subject government entities to 5th Amendment takings claims by negatively affected compliance entities. Emission allowances are entirely created by government programs, and only exist within those confines. RECs are fundamentally unlike emission allowances. RECs are not an allowance or authorization to pollute, instead, RECs are created by the generator of renewable energy, and exist and have value outside of government programs.

As has been established above, property rights in RECs already exist under California Law. Section 97002(a)(15) could be interpreted as eliminating these existing property rights. This elimination of property rights may be a regulatory taking under the 5th Amendment.

ARB Can Mitigate its Regulatory Taking Risk and Mitigate any Unintended Consequences on Existing REC Markets and REC Market Participants by Slightly Amending Section 97002(a)(15)

In order to avoid regulatory and market uncertainty, RES regulations should only focus on rights created under AB 32. The ability to use RECs to meet the requirements of a compliance program is the only aspect of a REC that is a government created right. As long as AB 32 regulations only address government created rights, the risk of regulatory takings claims and other unintended consequences will be minimized.

3Degrees recommends amending Section 97002(a)(15) to read “ *The RES compliance value of a REC does not constitute property or a property right.*” This change would cause the term to only focus on rights potentially created under AB 32, address concerns regarding regulatory takings, and bring RES treatment of RECs in line with other State and Federal Agencies. Finally, this language would prevent the resulting market and contractual uncertainty that would arise from a refusal to recognize existing property rights in RECs.

⁷ CPUC [Decision 08-08-028](#), Appendix B, page 1.

⁸ The Clean Air Act, 42 U.S.C 7651(f)

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Conclusion

3Degrees applauds the hard work and thought that ARB staff has put into the 33% RES draft regulation and overall AB 32 program. However, the proposed language of Section 97002(a)(15) would create regulatory and market uncertainty surrounding RECs, possibly hurting investment in renewable energy and the goal of reducing GHG emissions. As shown, valuable property rights in RECs already exist, and the elimination of these rights could be seen as contradicting existing California law and a regulatory taking. By amending this language, ARB can protect itself from takings claims and recognize the existing property rights in RECs, ensuring that investment and demand in renewable energy markets continues to grow.

Thank you for this opportunity to contribute comments.

Sincerely,



Gabe Petlin
Director of Regulatory Affairs
3Degrees