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BEFORE THE CALIFORNIA ENERGY COMMISSION

Application for Certification for the
VALERO COGENERATION PROJECT

Docket No. 01-AFC-5

Sitting Committee:
Honorable Arthur Rosenfeld

**VALERO'S PETITION
FOR EXTENSION OF
ON-LINE DATE FOR
PHASE II OF THE
VALERO COGENERATION
PROJECT**

1. Pursuant to Section 1769(a) of the regulations promulgated by the California Energy Commission ("Commission"),¹ Valero Refining Company- California ("Valero") hereby requests that the "Project Operation Requirement" on page 239 of the Commission's Decision and Certificate for the Valero Cogeneration Project be extended and modified as follows:

Project Operation Requirement

Phase I (51 MW) of the Valero Project shall be on line by no later than December 31, 2002. Phase II (51 MW) of the Valero Project is planned to be ~~shall be~~ on line by no later than November 1, 2007. If either phase of the project is not fully operational by its respective on line date, the Energy Commission will conduct a hearing to determine the cause of the delay (unless the project owner waives the right to such a hearing, in which case the certification for the phase or phases not fully operational shall be forfeited) and consider what actions, if any, are appropriate. If the Energy Commission finds that the project owner, without good cause, failed to have a phase of the project in operation by its respective on line date, the Energy Commission may deem that the project owner has forfeited its certification as to the portions of the project not in operation by its respective on line date.

¹ Cal. Code Regs., tit. 20, § 1769.

2. The requested extension is necessary because Phase II will not be completed by November 1, 2005. As you will recall, during the siting process Valero noted that any commitment to completing Phase II would be contingent on Valero's funding decisions, electricity market conditions and resolution of any legislative and/or regulatory uncertainties. For example, the Project Operation Requirement condition (at page 239 of the Commission's Certificate) provides that Phase I "shall be online" by December 31, 2002 but further provided that Phase II is only "planned to be online" by December 31, 2002. This condition confirms that Phase II was only in the planning stage during the siting process, and that Valero had not made a final commitment to Phase II.

3. Valero did, however, commit to constructing Phase I. Phase I is currently online and operational and is in compliance with the existing Project Operation Requirement condition. Phase I has added approximately 51 Megawatts of new dedicated in-state generation for the State of California.

4. The requested extension will simply allow Valero more time to consider the viability of Phase II, which if constructed, could add an additional 50 Megawatts of new dedicated in-state generation for California.

5. In the event Staff determines that the requested extension should be processed as an Amendment under the Certificate conditions and Section 1769(a)(3), then Valero requests Commission approval of the requested extension for the following reasons:

6. First, as the record in this Docket reflects, Valero proposed to build Phase I and Phase II of its Cogeneration Project in direct response to Governor Davis' declared state of emergency and the Governor's repeated calls for California businesses to construct additional in-state generating capacity. In answering the Governor's call, Valero committed to pursuing Phase I of the Cogeneration Project and proposed to consider pursuing a second phase that could add even more in-state generating capacity. Valero understands that well after it commenced construction of Phase I, the California Public Utilities Commission ("CPUC") began considering

whether facilities that construct cogeneration units to serve their own on-site electric and thermal needs, such as Valero, should be subject to potentially enormous “exit fees” for a variety of costs incurred, and contracts procured, by the California Department of Water Resources (“CDWR”) during 2001. Indeed, both the Commission and Valero (through its membership in the Energy Producers and Users Coalition – “EPUC”) have been active participants in the CPUC’s proceeding (R.02-01-011) on these issues. Additionally, the CPUC has been considering the methodology to determine avoided costs for qualifying facilities for pricing purposes and qualifying facility long-term contract policy for utility procurement purposes (R.04-04-003 and R.04-04-025). These proceeding could have significant financial impacts and Valero and EPUC have been active participants in these proceedings. Valero understands that the schedule for the qualifying facility phase of R.04-04-003/R.04-04-025 has been subject to many delays thus far. While the CPUC intended to have a decision on qualifying facilities issues by the end of 2005, it now appears that that will be unlikely. Valero understands that CPUC decisions in these proceedings that could affect the economic viability of Phase II might not reasonably occur until some point in 2006. Prior to these final decisions in these proceedings, Valero cannot reasonably assess the financial viability of Phase II. (Moreover, Valero anticipates that it would take a minimum of approximately nine months to complete Phase II after Valero’s assessment of the viability of Phase II.)

7. In addition, during recent legislative terms, significant legislative attention was focused on issues related to electric generation and the electric markets in California. Further, Valero understands that the Utility Reform Network (TURN) ballot initiative to “re-regulate” the electric industry has qualified for the next statewide ballot, which could be November 8, 2005. Valero understands that the TURN ballot initiative would prohibit any new Direct Access transactions and encumber existing “grandfathered” Direct Access transactions, and could impact significantly the electric market structure in California. Given the significant level of legislative interest in electricity issues, there is a high degree of uncertainty concerning the rules that will

govern a generating facility like Phase II. Moreover, given the TURN ballot initiative, the future structure of the electric market in California remains unclear.

8. Accordingly, the regulatory and financial uncertainties created by the issues being considered in R.02-01-011, R.04-04-003, and R.04-04-025, as well as in the legislature and by the TURN ballot initiative, have made it impossible for Valero to make a reasoned determination as to the viability of Phase II.² Therefore, for the reasons set forth above, it is currently impossible for Valero to undertake a meaningful analysis of whether Phase II is viable, and there is good cause for granting the requested extension.³ It should also be noted that had Valero known it would be subject to an enormous exit fee when it promptly responded to the Governor's call for additional in-state generating capacity in 2001, Valero would not have committed to build Phase I, let alone consider Phase II; indeed, had Valero known it would be subject to these significant exit fees, Valero could not have been able to economically commit to Phase I or consider Phase II.⁴

9. Second, the proposed extension of the on-line date for Phase II will not have an adverse impact on the environment, and accordingly, no mitigation measures are required. The Commission's Decision already evaluated all of the potential environmental impacts related to the project, and found that none were significant. Moreover, the requested extension will allow the "Project Operation Requirement" in Valero's Certificate to more closely coincide with the timeframes contained in the permits issued to Valero by the Bay Area Air Quality Management District ("BAAQMD"). The BAAQMD permit currently extends through November 1, 2005, and can be administratively renewed through November 1, 2007. Upon obtaining the approval of Valero's requested extension, Valero intends to request the aforementioned administrative extension from the BAAQMD, which Valero further anticipates will be granted. (Valero notes its willingness to request from BAAQMD an updated Best Available Control Technology

² Cal. Code Regs., tit. 20, § 1769(a)(1)(B, D).

³ Cal. Code Regs., tit. 20, § 1769(a)(1)(B, D).

determination if necessary to extend the BAAQMD permit.) Therefore, because the requested extension does not change any other aspect of the Energy Commission's approval, does not create any new environmental impacts and is consistent with the BAAQMD's permit and approvals, the requested extension will have no impact on the environment.⁵

10. Third, as indicated above, the requested extension does not change any other aspect of the Commission's approval or the basis for the Commission's finding that the project fully complies with applicable laws, ordinances, regulations and standards. Accordingly, the proposed extension will have no impact on Valero's ability to comply with applicable laws, ordinances, regulations, and standards if Phase II is constructed in the future.⁶

11. Fourth, the requested extension would have no adverse effect on adjacent property owners, the public or other parties to this proceeding. (To Valero's knowledge, the list of property owners potentially affected by the project and this amendment is that same as provided in Valero's Application for Certification, and that list is incorporated herein). As discussed above, the requested extension simply allows additional time for the CPUC to come to final decisions in the proceedings noted above. Such final decisions are a clear prerequisite for Valero's determination of whether Phase II will be viable. The requested extension does not change the substance of the Commission's Decision. The Commission has already determined that the project would have less-than-significant effects on adjacent property owners and the public. Indeed, because the majority of the construction work required for the project was completed as part of Phase I, most of the "less-than-significant" effects have already been completed. Therefore, adjacent property owners, the public and other parties to this proceeding will not be adversely affected by the requested extension.⁷ However, because Phase II cannot be completed by November 1, 2005, if the requested extension is not granted it will be extremely

⁴ See, Cal. Code Regs., tit. 20, § 1769(a)(1)(C).

⁵ Cal. Code Regs., tit. 20, § 1769(a)(1)(E).

⁶ Cal. Code Regs., tit. 20, § 1769(a)(1)(F).

⁷ Cal. Code Regs., tit. 20, § 1769(a)(1)(G, H, I).

difficult for Valero to continue to consider whether Phase II could be viable. The requested extension would permit Valero to reasonably assess the impact of CPUC final decisions on the viability of Phase II. Without the requested extension, this impact would be unknown, rendering the continued consideration of Phase II's viability difficult. This could essentially eliminate the possibility of Valero's continued assessment of Phase II. The potential provided by Phase II for adding approximately 50 Megawatts of new dedicated in-state generating capacity at Valero's Benicia Refinery, which would have a public benefit for the State of California, could be lost.

12. Therefore, Valero is requesting that Commission grant the requested extension for Phase II.

Respectfully submitted,

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California



Nora Sheriff

July 22, 2005

Date