

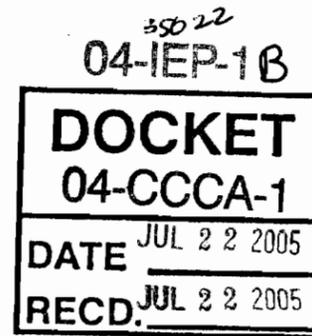
BEFORE THE CALIFORNIA ENERGY COMMISSION
OF THE STATE OF CALIFORNIA

In the Matter of:

The Preparation of the 2005 Integrated
Energy Policy Report (Energy Report)

Docket No. 04-CCCA-1
Docket No. 04-IEP-1B

COMMENTS OF THE COGENERATION ASSOCIATION OF CALIFORNIA AND
THE ENERGY PRODUCERS AND USERS COALITION



Michael Alcantar
Don Brookhyser
Alcantar & Kahl LLP
1300 SW Fifth Avenue
Suite 1750
Portland, OR 97201
503.402.9900 office
503.402.8882 fax
mpa@a-klaw.com
deb@a-klaw.com

Counsel to the Cogeneration
Association of California

Evelyn Kahl
Rod Aoki
Alcantar & Kahl LLP
120 Montgomery Street
Suite 2200
San Francisco, CA 94104
415.421.4143 office
415.989.1263 fax
ek@a-klaw.com
rsa@a-klaw.com

Counsel to the Energy Producers and
Users Coalition

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The Cogeneration Association of California¹ (CAC) and the Energy Producers and Users Coalition² (EPUC) (jointly, CAC/EPUC) submit these comments to the California Energy Commission (Energy Commission). The Comments are submitted pursuant to the Energy Commission's June 15, 2005 Notice of Climate Change Advisory Committee Quarterly Meeting And Integrated Energy Policy Report Committee Workshop (Notice).

As stated in the Notice, a fundamental purpose of the Advisory Committee is to "provide input on a wide range of specific strategies, analyses, and proposed recommendations on ways to reduce greenhouse gas emissions in the state...." As stated by CAC/EPUC during comments at the July 12, 2005

¹ CAC represents the power generation, power marketing and cogeneration operation interests of the following entities: Coalinga Cogeneration Company, Mid-Set Cogeneration Company, Kern River Cogeneration Company, Sycamore Cogeneration Company, Sargent Canyon Cogeneration Company, Salinas River Cogeneration Company, Midway Sunset Cogeneration Company and Watson Cogeneration Company.

² EPUC is an ad hoc group representing the electric end use and customer generation interests of the following companies: Aera Energy LLC, BP America Inc. (including Atlantic Richfield Company), Chevron U.S.A. Inc., ConocoPhillips Company, ExxonMobil Power and Gas Services Inc., Shell Oil Products US, THUMS Long Beach Company, Occidental Elk Hills, Inc., and Valero Refining Company - California.

Workshop, a significant means of reducing greenhouse gas emissions in California is through the preservation of existing, and encouragement of new, combined heat and power (CHP) projects in the State. As the Energy Commission is aware, CHP is the sequential production of both thermal energy (such as heat or steam) used for industrial, commercial, heating or cooling purposes, and electric energy, from a single source of fuel. This unique dual use of a single fuel results in a reduction in the overall consumption of that fuel thereby providing both energy efficiency and environmental benefits.

Throughout the IEPR process, the Energy Commission has recognized the environmental benefits of CHP (cogeneration)

In the 2003 IEPR, the Energy Commission stated in pertinent part:

Distributed generation, including cogeneration and self-generation, has tremendous potential to help meet California's growing energy needs as an additional generation source and an essential element of customer choice. Its use offers potential benefits that extend to customers, utilities, and the system as a whole and can be used strategically to meet the policy objectives of the RPS and reduce greenhouse gases. (2003 IEPR at 15) (emphasis added)

Cogeneration offers another low-cost, low-emission option for the efficient use of natural gas. By creating both electric and thermal energy, cogeneration plants can achieve heat rates that "match or exceed the heat rates of new gas-fired combined-cycle power plants." Cogeneration is a major element in the state's energy system, contributing more than 6,300 MW. (2003 IEPR at 24) (emphasis added).

More recently, the June 2005 Energy Commission Staff Paper on Global Climate Change stated that "the use of combined heat and power ... from a single combustion source promises to be an effective strategy to reduce GHG

emissions.” (June 2005 Staff Paper at 24) Additionally, in the April 2005 Assessment of the California CHP Market, CHP is described as “the most energy efficient and cost-effective form of distributed generation” (April 2005 Report at 1-1); and as having, among other benefits, “environmental benefits both in the reduction of criteria pollutants and emissions of carbon dioxide that contribute to global warming.” (Id. at 2-1) These environmental benefits were quantified by a 2000 Energy Commission Report where it was estimated that existing cogeneration reduces in-state NOx emissions by over 7,600 tons annually vis-à-vis central generation plants and gas-fired boilers. (Market Assessment of Combined Heat and Power in the State of California (2000)) The 2000 Report also estimated that existing cogeneration reduced CO₂ emissions by about 26 million tons per year on a regional basis.

The Energy Commission’s recognition of these important benefits is consistent with both findings of the California Public Utilities Commission as well as State law. In its Decision 04-01-050, the CPUC confirmed the significant benefits which QF power provides to California as discussed in its earlier Decision No. 02-08-071:

As a general proposition, we find that QF power provides significant benefits to the state, in the form of more efficient industrial processes, as well as electric power. QFs have continued to provide power to the state during difficult circumstances during the past several years. A consequence of not making provisions for continuing QF contracts would be more QF power going off-line, creating additional net short that the utilities would need to procure during the interim period. (D.04-01-050 at 134)

Additionally, the CPUC found:

QF power provides numerous benefits to California, including environmental attributes, local power production, and economic development (D.04-01-050, FOF 71) (emphasis added)

Accordingly, the CPUC found:

In compliance with PURPA and recent FERC decisions, the Commission should provide an opportunity for existing QFs to continue to provide power to the utilities in a manner that encourages facility maintenance and upgrade. (D.04-01-050, FOF 74)

Because the State has long recognized the benefits of cogeneration, it has made the encouragement of private investment in cogeneration a State policy. The following are examples of California's efforts to encourage cogeneration development and support existing cogeneration operations:

In 1978, California's Warren-Alquist Act explicitly committed the State to the promotion and development of cogeneration:

§ 25004.2. The Legislature further finds that cogeneration technology is a potential energy resource and should be an important element of the state's energy supply mix. The Legislature further finds that cogeneration technology can assist meeting the state's energy needs while reducing the long-term use of conventional fuels, is readily available for immediate application, and reduces negative environmental impacts. The Legislature further finds that cogeneration technology is important with respect to the providing of a reliable and clean source of energy within the state and that cogeneration technology should receive immediate support and commitment from state government.

(emphasis added)

Consistent with this commitment, California Public Utilities Code Section 372 (a) states in pertinent part that:

*[i]t is the policy of the state to encourage and support the development of cogeneration as an efficient, environmentally beneficial, competitive energy resource that will enhance the reliability of local generation supply, and promote local business growth. *** (emphasis added)*

Through the 2004 IEPR Update, the Energy Commission stated:

Over the next several years, California faces significant challenges in ensuring adequate electricity supplies to keep California's lights on during critical peak demand periods. This challenge is especially evident in Southern California, which also faces regional and local reliability challenges. To address these, California must step up its efforts to achieve the goals already established for demand response programs, make better use of its existing fleet of power plants and move aggressively to bring new resources on-line. (2004 Update, Executive Summary ¶ 1)

At a time when the State is concerned both about having enough reliable and deliverable generation to meet its current and projected load, and reducing GHG emissions, CHP resources in California are at risk. As the Energy Commission is well aware, cogeneration resources represent approximately 16% and 18% respectively, of the total generation of PG&E and Edison. The contracts through which these resources provide power to the utilities expire at a significant rate over the next few years.³ Without adequate assurances that they will be able to continue to provide power to the utilities upon terms and conditions that are consistent with the unique operating characteristics of cogeneration, many of these resources remain at risk. Moreover, absent the availability of meaningful options to provide power to the utilities, sponsors contemplating

³ ... QF power contracts are actually set to expire at a significant rate over the next five to seven years. By 2008, expired QF contract capacity is expected to exceed 1,000 MW and approach 1,800 MW by 2010. SCE is projected to lose the most QF capacity during this time period. D.04-01-050 at 135-136

development of new cogeneration operations may be discouraged from investing in and commencing operations.

For a typical existing cogeneration operation that produces more electrical energy than is consumed on site, the option to employ cogeneration is linked to the ability to harmonize the operation of the cogeneration facility with the production requirements of the thermal host and the electrical needs of the utility. The commercial or industrial customer, which utilizes cogeneration to manage thermal energy requirements, must have a repository for the electrical energy that is generated from the cogeneration process. These types of companies which rely on the thermal energy output of a cogeneration facility for their core operations will only continue to operate under a cogeneration configuration for as long as such a configuration continues to be economic, provides a reasonable certainty of stable, long-term operation, and does not jeopardize their ability to reliably produce their core business product. This means that cogeneration must be preserved through a dedicated position in the utilities "baseload" resource portfolio.

In the absence of a long-term commitment with the utility, there is no guarantee that the industrial customer will have an outlet for the electrical energy that is produced in the cogeneration process. Because the production of thermal energy is directly tied to the ability to deliver electrical energy, the lack of a long-term commitment with the utility to deliver the electrical energy is a threat to the industrial customer's ability to conduct its core business. Moreover, the lack of a known contract term, and known terms and conditions for the delivery of

electrical power to the utility, present the industrial customer with a significant amount of uncertainty as to whether it is prudent to continue to rely on cogeneration operations. Such uncertainty encourages the industrial customer to evaluate the installation of boilers to insure the long-term production of the thermal energy required for its core business operations. Correspondingly, the continued operation of existing cogeneration is discouraged and the electrical energy supplied to the grid is jeopardized.

Therefore, the net result of a failure to adequately address the retention of cogeneration resources is that existing cogeneration benefits, which California has relied upon for the last two decades, may be lost as industrial facilities move to insure the operational certainty that they require. It is imperative that the policies adopted in this proceeding adequately provide for the retention of generation from existing CHP resources as well as the development of new resources. Assuring that existing cogeneration continues to be in the utilities' generation portfolio will provide the State with an energy efficient and environmentally beneficial generation resource, while enhancing the California business community's ability to continue to manage its energy requirements (both thermal and electric) in a time proven manner.

The Energy Commission can facilitate the retention of these resources by expressly making the preservation of existing cogeneration resources and encouragement of new cogeneration resources a goal of the 2005 IEPR and identifying cogeneration as a preferred resource in the State. The Energy Commission can also work with the CPUC to provide the appropriate directives

and incentives for the utilities to provide meaningful contract commitments to both existing and new cogeneration projects.

CONCLUSION

The Energy Commission may facilitate the retention of cogeneration resources and corresponding environmental benefits by expressly making the preservation of existing cogeneration resources and encouragement of new resources a goal of the 2005 IEPR. This would include identifying cogeneration as a preferred resource in the State.

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Respectfully submitted,



Michael Alcantar
Don Brookhyser

Counsel to the Cogeneration
Association of California



Evelyn Kahl
Rod Aoki

Counsel to the Energy Producers
and Users Coalition