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Reply to Truckee Office

February 2, 2007

Commissioner Byron
Commissioner Geesman
California Energy Commission
Docket Unit
Attn: Docket No. 06-OIR-1
1516 Ninth Street, MS-4
Sacramento, California 95814-5512
Email: docket@energy.state.ca.us

DOCKET
06-OIR-1

DATE FEB 02 2007

RECD. FEB 02 2007

Re: Docket No. 06-OIR-1
Comments of M-S-R Public Power Agency

Dear Commissioners Byron and Geesman:

I serve as General Counsel to the M-S-R Public Power Agency. Enclosed herewith are the comments of the M-S-R Public Power Agency submitted in response to the Proposed Regulations Establishing a Greenhouse Gases Emission Performance Standard and Implementing Regulations pursuant to Senate Bill 1368. These comments were also submitted electronically at docket@energy.state.ca.us on February 2, 2007.

Please feel free to contact me or Martin Hopper, Director, M-S-R Public Power Agency at (408) 615-6677 to discuss M-S-R's comments. Thank you.

Very truly yours,

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SCG/ks
cc: M-S-R Public Power Agency

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In the Matter of:)
)
Proposed Adoption of Regulations)
Establishing a Greenhouse Gases)
Emissions Performance Standard)
For Baseload Generation of Local)
Publicly Owned Electric Utilities)

Docket No. 06-OIR-1

**Comments of the
M-S-R Public Power Agency
On the Implementation of SB 1368 Emission Performance Standard
And Implementing Regulations**

The M-S-R Public Power Agency respectfully submits its comments on the implementation of SB 1368 Emission Performance Standard.

Introduction

The M-S-R Public Power Agency (“M-S-R”) is a public entity, without taxing power, created pursuant to Sections 6500, et seq., of the Government Code of the State of California and a Joint Exercise of Powers Agreement, dated April 29, 1980 (as amended and restated on November 17, 1982) among the Modesto Irrigation District, City of Santa Clara (dba Silicon Valley Power) and the City of Redding (herein “Member” or “Members”). M-S-R is authorized, inter alia, to acquire, construct, maintain and operate facilities for the generation and transmission of electric power and to enter into contractual agreements for the benefit of any of its Members.

The San Juan Project

In 1983 M-S-R bought an undivided 28.8% interest in Unit No. 4 of the San Juan Generating Station ("SJGS") located near Farmington, New Mexico. The San Juan Generation Station is a four unit 1640 MW coal-fired powerplant. These four units entered service between 1973 (Unit No. 2) and 1982 (Unit No. 4). M-S-R financed its purchase of its interest through the issuance of tax-exempt revenue bond debt. The final maturity of the bonds runs through July 2023 and about \$400 million principle remains outstanding on the bonds at this time.

Environmental Improvement and Emission Reduction Project

In 2005 the nine owners of the SJGS entered into a settlement agreement and Federal Consent Decree regarding claims made pursuant to the Clean Air Act wherein SJGS committed to achieve certain environmental control improvement projects by specified dates certain at a cost currently estimated to exceed \$268 million. M-S-R's share of these costs is about \$24 million and pertains to work effecting SJGS Unit No.4 and facilities common to other SJGS units. The work to be performed on SJGS Unit No. 4 includes the installation of low NO_x burners, replacement of the electrostatic precipitators with a baghouse to reduce emissions of particulate matter and SO_x, and the installation of an activated carbon injection system to reduce mercury emissions. As an ancillary benefit of this project, the net capacity of SJGS Unit No. 4 will increase from about 507 MW to about 512 MW. Pursuant to the consent decree, this work is underway and scheduled for completion and testing this fall to meet the SJGS Unit No. 4 December 31, 2007, deadline. As this work was contracted prior to December 31, 2006, the requirements of CEC Staff's draft sections 2901 and 2902 would not apply. However, if this settlement occurred today, M-S-R would be appear to be prohibited from entering into it because these actions could be construed either to extend the life of SJGS by more than five years (by allowing it to operate beyond December 31, 2007) or to increase the capacity (by increasing the efficiency of the generating unit and reducing losses) of the unit (it should be noted that the fuel through-put as governed by the capacity of the boiler

would be unchanged but the electric output would be increased.) However, as publicly stated by Assemblyman Levine on January 25, 2007, to the Northern California Power Agency, it was not the intent of the legislature to prohibit improvements in efficiency or environmental controls of existing non-CCGT generating facilities. Therefore, we respectfully request CEC Staff to modify their proposal consistent with both the language of the statute and the intent of the legislature as illustrated here.

Efficiency Improvement Project

As part of the routine operation and maintenance of the SJGS, boiler components are regularly replaced as are elements of the steam turbine and the electric generators. Under the joint ownership and operation agreements for SJGS each owner is obligated to pay their share of the costs of such replacements as may be approved by the project owners as a whole. M-S-R, as a minority owner of the station, does not have the sole right to veto any expenditures approved by the majority of the owners. If such an expenditure was found to be in conflict with CEC Staff's proposed regulations, M-S-R could be placed in the untenable position of choosing between regulatory compliance or defaulting on its obligations under the SJGS operating and ownership agreements. This concern is not theoretical.

Evaluated as part of the environmental project described above was the need to replace steam turbine sections to restore performance lost to eroded components and to address age and stress-related cracking. The original turbine vendor recommended replacement of turbine blades and further recommended the use of modern "dense-pack" technology. For SJGS Unit No. 4 this replacement would result in about a 4% increase in efficiency which would reduce CO₂ production by about 90 lbs per MWh and increase net capacity by about 27 MW at a cost of about \$10 million. This work was originally intended to be performed in the 2007 major outage in conjunction with the installation of the environmental upgrades mandated by the consent decree. However, due to delays in reaching determinations with the US EPA that this turbine upgrade would not trigger "New Source Review," there was insufficient lead-time to complete this project in 2007.

We believe it is now the intent of the SJGS owners to install this upgrade during the 2009 Unit No. 4 maintenance outage. If the remaining SJGS owners elect to proceed with this project, M-S-R, if unable to veto the project, would be placed in an untenable position. We could be forced to choose between violating regulation, defaulting under the SJGS operating and ownership agreements, or divesting our interest. Although divestiture is theoretically possible, it is not clear M-S-R could exercise this option without retiring all the bonds issued to finance this project. As the current market for coal-fired generation facilities would appear to value a sale of our interest at about \$100 million, this option would create great economic hard-ship to M-S-R and its ratepayers. Therefore, M-S-R needs relief from the provisions of the CEC staff's draft which would preclude investment in this efficiency improvement project consistent with the intent expressed by Assemblyman Levine.

Conclusion

M-S-R respectfully requests that the provisions of the proposed regulations provide a specific exemption for projects that reduce the emissions of non-CCGT generation or improve the efficiency of non-CCGT generation even if a corollary effect of the emission reduction or efficiency improvement includes an incidental increase in project capacity. In the alternate we respectfully request a savings clause that provides that local publicly owned electric utilities such as M-S-R should not be required to take any action that would contradict the terms of its contracts in existence prior to January 1, 2007 (the effective date of SB 1368).

Respectfully Submitted,

A handwritten signature in black ink, appearing to read "Steven C. Gross".

Steven C. Gross
General Counsel
M-S-R Public Power Agency