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October 16, 2013

Dr. Steven Cliff  
Climate Change Program Evaluation Branch  
California Air Resource Board  
1001 I Street  
Sacramento, California 95812 Via Email: scliff@arb.ca.gov

**Subject: Comments of CSU on 2013 Proposed Regulation Amendments to Cap & Trade Regulations for Legacy Contracts**

Dear Dr. Cliff:

The Chancellors Office of the California State University (CSU) provides the following comments on amendments to the Cap & Trade Regulations (“C&T” or the “Regulations”) released on September 4, 2013. CSU’s comments focus on proposed Section 95894, “Allocation to Legacy Contract Generators for Transition Assistance”, the associated definitions of “Legacy Contract” and “Legacy Contract Emissions” and on credits for universities.

As to the latter point, we have reviewed the proposed amendments for the University allowances and find the changes to be acceptable.

As to the other points, CSUCI requests that the ARB make the following changes:

- Clarify that the transition assistance afforded to Legacy contracts will apply to non-standard QFs which do not have GHG cost recovery in their Power Purchase Agreement (PPA).
- Clarify that facilities with Non-Standard QF Contracts, which were not addressed in CPUC Decision D.10-12-035, should be treated differently from those with Standard QF Contracts.
- Provide that the transitional assistance formula in Section 95894 should be revised to account for actual emissions for the balance of the original term of the PPA. In the case of CSUCI, that would be April 2018.

Our specific requests and the reasons therefor are discussed below.

## **Background**

**Project History.** CSU campuses operate several cogeneration projects across the state in both public and investor owned utility (IOU) service territories. The largest is CSU Channel Islands (CSUCI). CSUCI is the site of the former Camarillo State Hospital (CSH), which was closed in the mid-nineties and was transferred to the CSU system. CSUCI is only facility owned by CSU that sells substantial electricity to an IOU under long term power purchase agreement (PPA). The PPA provides for the sale and delivery of 26.5 MW of firm capacity and energy to Southern California Edison (SCE). The original term of the PPA terminates in April 2018.

The project at CSH was part of the so-called “big ten” cogeneration projects solicited circa 1982 under the leadership of Governor Brown. In order to encourage a diverse mix of projects, the Department of General Services (DGS) selected some projects that served only the energy needs of the particular site and some projects that were large enough to sell significant electricity to the IOU's. The five large projects that sell electricity to the IOU's all entered thirty (30) year power purchase agreements (PPA's) with the IOU. The project at Agnews was converted from a cogeneration plant in 2012 when the state announced its intentions to close the Agnews Developmental Center in 2012. The remaining four large projects have PPA's with original termination dates in 2017 and 2018.

**QF Settlement for Standard Offer Contracts.** The CPUC and legislature authorized QF contracts beginning in 1982. For the better part of two decades, the IOU's argued that the short-run avoided cost (SRAC) prices under Standard Offer #4 contracts were too high. This ongoing dispute ultimately led to the QF Settlement Program.

As part of the CHP Program Settlement, CHP facilities with *standard offer type* QF contracts were offered an amendment (the Legacy Amendment). The Legacy Amendment included various pricing options for QFs paid under standard SRAC pricing, which under the legacy contacts are adjusted from time to time by the CPUC. Integrated into each standard SRAC pricing option were differing levels of recovery of C&T compliance costs.

**CSUCI and Non-Standard Contracts.** As the ARB has learned, there is a small set of qualifying CHP facilities with Non-Standard QF Contracts that need a means to allow recovery of C&T compliance costs. These non-standard CHP facilities were financed and are operated based upon the non-standard pricing terms.<sup>1</sup> The existence of these non-standard contract provisions would impose unreasonable burdens on those owners were they to accept the standard legacy amendment under the CHP Program Settlement.

The PPA for the CSUCI project began as a Standard Offer #4 contract. Circa 2002, SCE and the previous owner of the project changed to what is now known as a Non-Standard QF Contract. The changes reduced the maximum price that could be paid under the CPUC's SRAC. This reduction was negotiated by SCE to benefit SCE's ratepayers by lowering the maximum prices paid under the PPA. The revised PPA also established a floor price which provided some downside protection to the owner of the project in the event SRAC prices dropped. These changes took place long before AB 32 was adopted.

Requiring CSUCI and other holders of Non-Standard QF Contracts that have undertaken contract amendments prior to the QF Settlement Program to enter yet another negotiation with the respective IOU would result in such owners taking a second SRAC pricing amendment, which would not be equitable to those owners. Projects like CSUCI would be forced to enter a second negotiation regarding SRAC pricing (having completed the one in 2002) whereas those projects subject to the QF Settlement required only one pricing restructure to obtain relief for their C&T burden.

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<sup>1</sup> The three that CSU is aware of are the projects at CSUCI, CIM and Metropolitan Hospital.

**Financing and Contract Integrity.** Among the factors that have led CSUCI to request assistance for the balance of the term is a concern regarding regulatory and contract integrity. Contract integrity is a major concern in project financing. In order for lenders/investors to finance projects of this nature, they need to be reasonably certain the contracts upon which the financings are based can be relied upon for at least their original term. Absent reasonable assurance of this contract integrity, it is difficult to attract project financing.

The State very publicly announced that it could provide reasonable contract certainty for the full 30 year terms that were contemplated for the “big ten” projects. The development of the CSUCI plant when it was Camarillo State Hospital was one of the plants specifically authorized by Government Code §14671.6.<sup>2</sup> That legislation and the IOU’s standard offers were necessary to facilitate development and financing of the project. Now CSUCI and the owners of the other projects with Legacy contracts<sup>3</sup> are facing the situation where, in the last five years of their contracts, they will incur costs that were not contemplated when the projects were planned. AB 32 raises the costs without a corresponding increase in revenues.

CSU submits that should the ARB adopt our recommended revisions, the regulatory integrity of the original ‘standard offer’ program will be maintained. We also submit that this will be done without compromising the overarching goals set forth in AB 32.

### **CSU’s Recommendations**

We request that the ARB clarify the language for ‘transitional assistance’ and the applicability to Non-Standard QF contracts. To that end, we are concerned with language in the definition of “Legacy Contract” that states “legacy contracts exclude contracts that *give rise to* a Legacy PPA Amendment”. We do not feel that ARB intended to exclude CSUCI’s plant and the other Non-Standard Contracts from the transitional assistance. Our first recommendation would be for the ARB to recognize that the Legacy PPA Amendments from the QF settlement were not appropriate for Non-Standard Legacy Contracts.

Furthermore, we recommend clarification in the definition of “Legacy Contract Emissions” with regard to the sentence “Legacy contract emissions do not include emissions that are *included in the calculations of cost* under the CPUC’s Qualifying Facilities and Combined Heat and Power Program Settlement” Again, we believe this is not clear because we are not aware of any such data in the CHP settlement.

We would propose that the ARB add definitions of both non-standard QF contract and Legacy PPA Amendment and eliminate the reference to the emissions because we are not aware that any such data exists.

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<sup>2</sup> 14671.6 Notwithstanding Section 14670, the Director of General Services, with the consent of the state agency concerned, or the Trustees of the California State University with Department of Finance and Department of General Services approval, may let for up to 35 years any real or personal state property for energy conservation purposes or to permit the construction and operation of energy distribution systems, cogeneration facilities, and alternative energy supply source facilities.

Projects which may be undertaken ...pursuant to this section include, but are not limited to, cogeneration and energy conservation projects at the following facilities: Metropolitan, Atascadero, Agnews, and Camarillo State Hospitals; California Institution for Men at Chino, Correctional Training Facility at Soledad; and California State Universities at San Jose, Northridge, Pomona, and San Luis Obispo.

<sup>3</sup> Other known Legacy contracts includes three of those mentioned above including Metropolitan State Hospital and Chino State Prison.

We have discussed language revisions with other non-standard QF contract holders and agree with their proposed language herein.

**“Non-Standard QF Contract” means a contract that does not include standard pricing based on short-run avoided costs, as set and adjusted from time to time by the California Public Utilities Commission (CPUC).**

**“Legacy PPA Amendment” means the pro forma standard amendment that was offered, under the Combined Heat and Power Program Settlement adopted by the California Public Utilities Commission (CPUC) by Decision number D-10-12-035, to combined heat and power qualifying facility (QF) generators that had existing QF contracts.**

“Legacy Contract” means a written contract or tolling agreement, originally executed prior to September 1, 2006, governing the sale of electricity and/or Legacy Contract Qualified Thermal Output at a price, determined by either a fixed price or price formula, that does not allow for recovery of the costs associated with compliance with this regulation; the originally executed contract or agreement must have remained in effect and must not have been amended since September 1, 2006 to change or affect the terms governing the California greenhouse gas emissions responsibility, price or amount of electricity or Legacy Qualified Thermal Output sold, or the expiration date. For purposes of this regulation, legacy contracts exclude contracts that give rise to a Legacy PPA Amendment, ~~as defined in the Combined Heat and Power Program Settlement pursuant to CPUC Decision number D-10-12-035, with a privately owned utility as defined in the Public Utilities Code section 216 (referred to as an Investor Owned Utility or IOU),~~ **but does not exclude generators with Non-Standard QF Contracts that did not execute a Legacy PPA Amendment.** A legacy contract does not apply to opt-in covered entities.

“Legacy Contract Emissions” means the emissions calculated, based on a positive or qualified positive emissions data verification statement issued pursuant to MRR, by the Legacy Contract Generator, that are a result of either electricity and/or Qualified Thermal Output sold to a Legacy Contract Counterparty, and calculated pursuant to section 95894 of this regulation. ~~Legacy contract emissions do not include emissions that are included in the calculation of cost under the CPUC’s Qualifying Facilities and Combined Heat and Power Program Settlement pursuant to CPUC Decision number D-10-12-035.~~

Given the situation, we recommend that the ARB revise Section 95894(d) (2) to allocate allowances not just through the first compliance period but through the balance of the original term of the Non-Standard Contracts. As the board staff is aware, this change will only affect a very small number of projects. It will eliminate the inequity they face by not having any other options and we submit will have virtually no impact on the overall C&T program.

We intend on making a request for an opportunity to speak to the Board in this matter. We thank you for your consideration of our concerns and proposed solutions.

Sincerely,



Len Pettis  
Chief of Plant, Energy and Utilities  
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LGP:

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