Panoche Energy Center
Legacy Contract Background

I. The Issue

- Panoche Energy Center (PEC) in Firebaugh, CA is a 400 MW natural gas peaking electric power plant that has historically been determined by the California Air Resources Board (CARB) to be a "Legacy Contract Generator" under the current Cap-and-Trade Regulation. This status recognizes that the PEC facility is unable to pass along GHG costs associated with the program under its contract with PG&E to the ultimate consumer of the electricity. These "stranded costs" are very significant and growing.
- CARB is currently amending the Cap-and-Trade Regulation to make modifications which take effect next year and also extend the program post 2020. In the immediate time preceding the amendment package release, staff presented at a public workshop a proposed solution for the issue facing PEC—to treat the facility the same way as other non-power plant Legacy Contract holders[1]. But the subsequently published amendments reversed course (without opportunity for public input) and now propose to completely eliminate "Legacy Contract" status and regulatory relief for PEC[2]. The current draft amendments would leave the PEC facility, along with its bondholders, which include public pensions, completely exposed to the price of compliance. This is an inequitable situation not encountered by any other power plant inside or outside of California.
- The CARB Board is meeting on September 22 to hear the entire amendment package. Without an <u>acknowledgement from the Board for staff to continue to address this issue CARB's current proposed amendments</u> will strand PEC with the entire cost of the regulation--a total stranded liability exposure for 2016 will exceed $5,000,000. Over the next 12 years PEC's stranded liability is set to be no less than approximately $108,000,000, and likely will be much more.
- Under PEC's exclusive contract with PG&E signed in 2006 (before AB 32 was finalized, hence the term "legacy contract"), PEC operates the facility exclusively for PG&E. PG&E has full control over when the facility runs, and therefore also has control over the quantity of GHG and criteria (smog forming) emissions the facility emits.
- Critically, the fundamental "carbon price signal" associated with AB 32 is missing from the cost to PG&E's (and its ratepayers) for electricity from the facility. Without a price of carbon built into the dispatch orders, the facility has been operating far more than normal/design thus increasing: 1) costs for PG&E ratepayers, 2) increasing local air pollution, 3) increasing the use of scare water resources, and 4) dramatically increasing the costs of operation, and 5) completely defeating the regulatory "price signal" intended to be sent to consumers.
- For the past three years, despite repeated attempts, PEC has not been able to negotiate a workable contract amendment with PG&E. The prior regulatory relief (set to be eliminated) and the current proposed amendments (failing to address PEC's issue), create zero burden or incentive for PG&E to address this situation, but their ratepayers, the citizens of the San Joaquin Valley, the facility bondholders, and the environment are all losers in this equation. There are no winners under the current proposal.
- If CARB were to revert to the earlier staff proposal, market forces would bring the operation of the facility into line with its design efficiency, it would release less local air pollution, it would use less water, it would cost less to operate and thus saving PG&E ratepayers on operational costs, and there would be a consistent policy price signal under AB 32.

---

[1] June 24, 2016 Workshop https://www.arb.ca.gov/cc/capandtrade/meetings/062416/arb_and_caiso_staff_presentations_updated.pdf (slide 35)
[2] July 12, 2016 Released https://www.arb.ca.gov/regact/2016/capandtrade16/appa.pdf