INDEPENDENT
ENERGY
PRODUCERS

November 11, 2009

Chairman Larry Goulder and Committee Members
Economic and Allocation Advisory Committee
California Air Resources Board
1001 I Street
Sacramento, CA 95814

RE: Transitional treatment of independent power producers (IPPs) operating under existing contracts that currently provide no reasonable means for GHG cost recovery

Dear Chair Goulder and Committee Members,

As a follow-up to the Economic and Allocation Advisory Committee (EAAC) meeting on November 4, 2009, the Independent Energy Producers Association ("IEP") appreciates the opportunity to comment on an important issued raised in the meeting: namely, the appropriate transitional treatment of independent power producers (IPPs) operating under existing contracts that currently provide no reasonable means for GHG cost recovery.

In response to the comments of Professor Knittel regarding generally Energy Intensive Exposed Industries, the issue was raised as to the proper *transitional* treatment of IPPs operating under existing contracts which they have no reasonable (nor in some cases lawful) means of cost recovery for GHG allowances they might incur under the First Deliverer approach. IEP wanted to support Professor Knittel's concern regarding this issue and emphasize its transitional nature.

Limited Scope/Scale. Regarding IPP contracts currently in existence for which no reasonable means of GHG cost-recovery exists, the scope and scale as a practical matter is limited primarily to federally sanctioned, PURPA-based contracts. Originally, these contracts were for renewable and non-conventional generation (e.g. fossil-fueled CHP). Owners/operators of these facilities receive energy and/or capacity payments based, by law, on the utilities' avoided cost, i.e. a payment for energy and/or capacity that the utility would pay "but for the presence of the QF" (i.e. a so-called 'Qualifying Facility' under PURPA). In California, the Public Utilities Commission (PUC) over the years has developed various avoided cost payment methodologies for payments to QFs that reflect this federal standard and existing state law (e.g. Section 390 of the PUC Code). Today, many of these facilities are operating under fixed price arrangements or, alternatively, are paid based on a formula composed in part by an administratively determined (i.e. CPUC) heat rate. Currently, there are approximately 10,000 MWs of QFs operating in California; however, approximately 6,000 MWs are renewables, while the remaining are CHP or operate based on FERC-sanctioned non-conventional fuels.

In addition to QFs, IEP anticipates that there exists today a limited subset of non-PURPA facilities operating under existing contracts which similarly provide no reasonable means for the operator to recover the costs of GHG compliance borne by First Deliverers. While IEP is unaware of the scope/scale of this subset, we believe the total amount of IPPs operating under these contract structures is severely limited.

Transitional Issue. The vast bulk of the existing contracts, particularly PURPA contracts, expire in a relatively short timeframe. IEP's understanding, based on recent conversations with utilities, is that 50-60% of the existing QF contracts expire by 2015 and the vast bulk of QF contracts (90% or more) expire by 2020. Currently, the CPUC is addressing successor agreements for Qualifying Facilities (QFs) eligible for PURPA-based contracts. It is highly likely that any and all successor agreements will address the treatment of GHG cost-risk faced by QFs.

Clearly, this is a near-term, transitional problem. The problem falls primarily on preferred resources such as renewables, CHP, and other non-conventionally fueled generation fostered under PURPA. IEP reiterates its concern regarding the treatment of IPPs holding existing contracts that currently provide no reasonable means of cost recovery. During a relatively short, transitional time-frame, we recommend freely administering sufficient GHG allowances to those IPPs that can provide evidence of contractual and/or operational constraints that limit their ability to recovery of the GHG costs they would otherwise incur.

Respectfully,

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