COMMITTEE HEARING

BEFORE THE

CALIFORNIA ENERGY RESOURCES CONSERVATION

AND DEVELOPMENT COMMISSION

In the Matter of:	) Docket No.
	) 02-REN-1038
Implementation of Renewables	)
Investment Plan Legislation	) Continuation of
(Public Utilities Code Sections	) Renewable Energy
381, 383.5, and 445, [SB-1038])	) Program
________________________________	)

CALIFORNIA ENERGY COMMISSION

1516 NINTH STREET

HEARING ROOM A

SACRAMENTO, CALIFORNIA

FRIDAY, DECEMBER 13, 2002

10:15 A.M.

Reported by:
Peter Petty
Contract No. 150-01-005

COMMISSIONERS PRESENT

John L. Geesman, Presiding Member

James Boyd, Associate Member

STAFF PRESENT

Marwan Masri

Tim Tutt

Ann Peterson

Tony Goncalves

Jim Hoffsis

ALSO PRESENT

Bob Ellery
Sierra Pacific Industries

Steven Kelly, Independent Energy Producers Association

Bill Carlson
Wheelabrator Environmental Systems, Inc.
representing California Biomass Energy Alliance

Greg Lawyer
Colmac Energy, Inc.

Peter Weiner
Paul Hastings

Nancy Rader
California Wind Energy Association

Jack Pigott
Geothermal Energy Association

Mark Rentz
California Forestry Association

Brian Dahle, Supervisor
Lassen County
Regional Council of Rural Counties

ALSO PRESENT

Bob Marino
Fairhaven Power Company

John Prevost
Pacific Lumber Company

Kelly Lloyd
EnXco

Richard Steed
Eel River Sawmills

Milton Schultz
Burney Forest Power

Gregg Morris
Green Power Institute

Steve Ponder
FPL Energy

Ralph Sanders
HL Power

Paul Wood
Coventa Energy

Eric Wills
Sunray Energy, Inc.

Michael Theroux
Theroux Energy
U.S. Heat and Power Association

Tandy McMannes
Kramer Junction Power

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P R O C E E D I N G S

10:15 a.m.

PRESIDING MEMBER GEESMAN: Okay, let's go ahead and get started. I apologize for the delay; we needed to do a sound check. I know at most professional concerts that can cause riots in the crowd, but I think 15 minutes will have to be acceptable.

I'm John Geesman, the Presiding Commissioner of the Commission's Renewables Committee. I think joining me later will be Commissioner Boyd, the other member of the Commission's Renewables Committee.

This is a good news/bad news type of task. I think everybody's here because of the state's greater emphasis on promoting renewable sources of energy. That's the good news.

The bad news is I think everyone is here because you realize that we have a finite pool of resources with which to subsidize the development of renewable resources.

We can argue --I don't there are many arguments in this room as to whether that subsidy is sufficient or well calibrated to the task ahead. I take as a couple of the guiding lights on this subject to be comments made by representatives of the state's two large investor-owned utilities earlier this fall.

John Fielding from the Southern California Edison Company, at the Independent Energy Producers Conference in September, said that he didn't think that the public goods charge was sufficient to accomplish the state's renewable portfolio standard goals, and that that public goods charge would need to be increased in order to do so.

I don't know the extent to which that represents his company's position. But I'd just say that as one Commission I embrace that.

The other comment from Dan Richard, Pacific Gas and Electric, made at the CFEE Conference in October; he would hope that his company would make all of its purchases of new electricity supplies come from renewables.

Again, I don't know the extent to which that represents the policy of his company. But as one Commissioner I embrace that, as well.

The Governor and Legislature have set very aggressive goals for the state in increasing its reliance on renewable sources of electricity.

I don't believe that they have given us an adequate volume of funds with which to get there. But we will do our best.

As a consequence, I don't expect anybody to be happy with the outcome of this process. But please recognize what the Commission will try to do is use each of its subsidy dollars as well as possible in terms of promoting the achievement of the renewable portfolio standard goals in as professional and businesslike a fashion. And focusing on what moves us forward.

With that, let me turn to the staff. I believe you've got a brief presentation to summarize the subject of today's hearing.

MR. TUTT: Thank you, Commissioner Geesman. We actually have two subjects in today's hearing, and with your blessing, Commissioner Geesman, we will take consumer education first.

COMMISSIONER GEESMAN: Okay.

MR. TUTT: We don't have a PowerPoint presentation for that. But I'm going to turn it over to Ann Peterson, our account lead with the consumer education account.

Before I do that, everyone knows, or if you don't know, Marwan Masri, our Deputy Director, is also here at the table with me. And my name is Tim Tutt; I'm the Technical Director of the Renewable Energy Program.

So we'll get going with consumer education first.

MS. PETERSON: We have copies of handouts for both the consumer education account and the existing account on the back table.

Really, we made very few changes with the consumer education account guidebook. Basically we've tried to clarify it and simplify the guidebook, but there really are no substantial changes.

Two minor changes that were made, we've asked that folks who receive funding from the consumer education account convey that the Energy Commission has provided support for the project.

And the other change that we've made is we have limited applicants to receive only one funding award per solicitation.

So those were the significant changes to the consumer education account.

COMMISSIONER GEESMAN: Are there comments or questions about the consumer education account? Sir, would you come forward and identify yourself.

MR. ELLERY: My name's Bob Ellery with Sierra Pacific Industries. I guess my only comment is -- two comments -- one, direct access is closed, therefore consumers can't buy any more renewables.

Two, given the insufficient funds to really get to a portfolio I ask whether this is a good use of money.

Thank you.

COMMISSIONER GEESMAN: Those questions have been asked internally, as well.

Shall we go then to the other subjects in front of us today, Mr. Tutt?

MR. TUTT: I think that would be -- unless there's anyone else who wishes to speak on consumer education?

COMMISSIONER GEESMAN: Okay, existing account.

MR. TUTT: Joining us at the table is Tony Goncalves, our existing account lead. And, again, there's handouts in the back on existing account. Jim Hoffsis, the Office Manager for our office, is also here. And Tony will go through the presentation on changes in the existing account, and then open it up to public comment.

MR. GONCALVES: Thank you. I'll keep this fairly brief and primarily to sort of the major comments and issues that we've heard over the last couple of weeks.

Essentially the program structure and procedures have not changed from that which was in place over the first four years of this program. The major changes, of course, are in the eligibility for funding from the program.

The legislation established that only biomass, solar thermal and wind would be eligible. And in our guidelines, the draft ones that are out, we have proposed that facilities with high fixed-price contracts be ineligible for funding. And that is defined as a contract that has an annual average at or above the applicable target.

We have become aware that the language in there was not sufficiently clear, especially in addressing the 5.37 cent contract. Those facilities that signed those amendments, the intent was that all facilities that signed those would be ineligible for funding whether they had some type of a blended contract or a discounted contract. It wasn't very clear and we wanted to make sure that everybody, before we got started, was aware of the intent of what was there.

The other changes are some proposals that we had in our guidelines. One of those is to make no payments for 2002 generation. We are proposing not to inflate the targets and caps on an annual basis. We have increased the values. The previous target values were 3.5 cents for tier 2. We are proposing 3.8 cents. The previous target for tier 1 was 5 cents, and we have increased that to a proposal of 5.37.

And the final issue is the time differentiation. And we are proposing to do it sort of as we did in the past on a monthly basis, relative to monthly averages, as opposed to going to an hourly or a time of use type of system.

And that concludes the presentation.

COMMISSIONER GEESMAN: Okay. What I'm going to do is proceed with the people that have filled out blue cards. If anyone wishes to address the Committee you should get a blue card from the Public Adviser; fill it out; and she will bring it up to me. And I'll call you when the time is right for your comment.

I want to introduce Commissioner Boyd,

who has joined us. He's the Second Member of the Renewables Committee.

Let me say, based on yesterday's experience, this probably works best if we keep it as informal as possible. The staff can respond to factual questions that any of you may have.

I'd like to encourage people to keep the remarks to about five minutes. And I would tell you that the human ear, and I have two of them, tends to shut down after about five minutes of hearing the same voice. Commissioner Boyd may have a little more powers of concentration than I do, but I would encourage you to be brief and succinct.

If you have written comments, we very much would appreciate that. We will close the docket at the close of business on Monday. So you do have some additional time to file written comment if you've not brought them with you. If you do have written materials, please summarize them in your verbal remarks. I can assure you we read and carefully review each written submittal.

And I do want to reserve the ability to interrupt you with questions, should they occur to me during your presentation.

Why don't we have --

COMMISSIONER BOYD: Commissioner Geesman, if I might, I'd like to apologize to the audience for being late. I was really here, intending to come down here, but about ten minutes of ten, as the Commissioner knows, the Commissioners have all kinds of duties. Another one of mine happens to be the State's Liaison with the Nuclear Regulatory Commission, and we had a little legal flap crop up that needed to be taken care of right away. So, I'm sorry I missed the first items. I'm glad I'm here now, and thank you for the introduction.

COMMISSIONER GEESMAN: We'll proceed. I don't know how long we'll go today, but everyone that wants to speak will have an opportunity. We may or may not break for lunch, depending on how the hearing goes.

Why don't we have first up Steven Kelly.

MR. KELLY: Thank you, Commissioner. Steven Kelly with Independent Energy Producers. And if I may ask your indulgence, I'd like to request five minutes of each ear so that I can get ten total, maybe, to give a proper overview of this.

And I'd like to frame this issue regarding the existing account in two contexts. One is to address the issue about 2002 production. And then to follow that up and deal with the issue about the going for what I call the pricing matrix.

And in doing that for each of those components I'd like to give a brief background which will provide some context for my comments; talk about the implications of the proposed revised guidebooks; and then make some recommendations, if I may.

Regarding the 2002 productions issue, and it's critical to put this in context, and I want to spend some time doing that.

The background on the issue from the renewable sector is one of -- actually begins, I think, in the energy crisis of 2001 where these energy developers and producers were not paid for production for a number of months under the presumption, though, that they were going to get paid at a proper time in the future.

And as a result of that, they continued operating, kept the lights on in a number of cases. And ultimately did get paid for the production they made. And that was a very welcome, though it was a difficult period of time.

The Energy Commission's investment plan, the June 2001 plan that was adopted by this Commission spoke, in my mind, fairly clearly to that context and for the need to pay for 2002 production.

Throughout that document there is a number of references to the fact that 2002 production was to be paid, and the target number in that investment plan that was approved by this Commission was 5.5 cents.

And that was in place from the beginning, even though it had not been endorsed by the Legislature, the Commission's endorsement of that product, work product, had been out there for about a year, end of the year 2002.

There was the delay in the passage of what's now known as SB-1038, which was expected in 2001, would clarify what was going to happen in 2002, that caused some concern for the generators in the year 2000, as we entered that time period. There was recognized a gap in what you were planning to do and your authorities to do it.

And I, for one, was -- approached the

staff with the interest of trying to get clarity as to what the Energy Commission would be doing for the production during 2002.

I was hearing rumors within my industry that there was one, a lack of certainty about what was happening; and, two, the fact that some companies were actually presuming that the money would be there, and they proceeding to produce electricity under that basis.

And I think I, early in February, had approached staff with the issue about we need clarification on this. And I think that is what resulted in what I will call the March 8th memo from the CEC that was meant to try to clarify what would be the Commission's intention.

And it was based on the premise that once 1038 actually got adopted there was an intention to pay for 2002 production.

And I think that notice, which was distributed fairly widely within the industry, was used by a number of companies as the basis for the Commission's latest statement, intention, policy statement or so forth, on that.

The next thing that really occurred from like a textual perspective is the fact that the passage of 2038 occurred in, I think, the August timeframe, which essentially adopted the CEC investment plan.

That investment plan had provisions for making payments in 2002; and had a tier price established in that at, I think, 5.5 cents fixed for a number of years.

The Legislature enacted that, in passing 1038 essentially endorsed that report from you. And made modifications in it and additional legislative language that was supposed to clarify or correct for things that they saw in the report they thought they wanted to weigh in on.

And then I'll note that on October 16th there was another, what I'll call, public notice from the Commission on it. It was a notice of hearing, which attachment A, I believe it was, again referred to the fact that there was an intention to pay for 2002 production.

I say that in the context that the generators who don't spend their life here at the Energy Commission, are actually out generating electricity, do see this stuff; and do hear, and watch what's going on.

And I think many of them, if not all of

them, had a strong presumption that there would be payments for the year 2002, based on the investment report and the announcements from the Energy Commission.

So they continued to operate under that presumption. And I presume modified or changed their behavior based on that presumption. And I think it's important that we take that into consideration.

The implications of the CEC statements and getting at the intent of the Legislature in passing SB-1038, which was essentially adopting the CEC-approved plan, was that it sent important regulatory, and I think in some sense, political messages.

And in this context in California today, the issue of regulatory certainty and political certainty is very fundamentally important to the energy industry as we dig our way out of the energy mess that we've found ourselves in the last couple years.

This industry, which has been there producing electricity during times of crisis, also depends on a ceratin amount of regulatory certainty and political certainty.

And historically the Energy Commission, when they have revised the guidebooks, as far as I can recall, has always revised the guidebooks on a going-forward basis. And I would recommend in this case that that applied, too. That to the extent there's any revisions, they be revised for production that is in a forward context and not for production that's happened in the past, as a matter of principle.

So, as a result of that I make the following recommendations:

One, that the revised guidebook be revised such that the 2002 production is considered. And secondly, revise the guidebook in such a way that the production is supplemented based on the CEC investment plan that was adopted by you and adopted by the Legislature in August for the year 2002, which would set a price at 5.5 cents for that year of production.

Because I think that is -- it sends the proper signals; it conveys a ceratin sense of certainty to generators as they move forward in the California marketplace.

The second issue that I wanted to address was what I call the going-forward pricing matrix. This is the box with the prices and the caps and so forth.

And there's, in my mind, essentially three issues that we need to address. One is that the 5.37 deals, as I call them, are excluded from participation in the program.

The second is what appears to be a lack of time of use pricing mechanism.

And the third is the apparent lack of an inflation factor.

Again, as background on this, I will note that this industry was a strong supporter of SB-1038, which was the Legislature's reauthorization of this program, the authorization to move forward.

We were there in the debates in the trenches. And during that debate it was clear that the Legislature was doing two things. One, it was adopting essentially the report that you had promulgated in June of 2001. And it was also making some corrections which, from the Legislature's perspective, was making corrections in order to improve the work product, I'll say.

COMMISSIONER GEESMAN: But there was no need to correct whatever ambiguity existed as to whether payments would be made for 2002 production?

MR. KELLY: In my mind, in the document, the guidebook, which had a provision for payment in 2002 at a specified price, the Legislature would rightly have concluded that that was what was going to happen for the year 2002, as did the industry make that conclusion.

As a practical matter, in excluding the 5.37 deals, you've essentially excluded probably, my guess is probably 90 percent of what would be otherwise eligible facilities of production in the State of California from this program.

And if the Legislature had intended on doing that, I think they would have done that by zeroing out that provision of the report by explicitly stating that there'd be zero funding for the existing account; or a modest amount of funding for people who do not have the 5.37 deal.

The Legislature didn't do that, and I think it's important to recognize that fact. And as a practical matter, many of the people who have those deals were the ones that were the strongest supporters in the legislative fighting that eventually got SB-1038 passed, got it out.

SB-1038 speaks to establishing certain goals for the existing program, improve competitiveness and secure for the state the environmental, economic and reliability benefits that continued operation of those facilities will provide.

It also states that the Energy Commission shall re-examine the tier structure to reflect market and contractual conditions, and also consider inflation when adjusting that structure.

And then it states that the Energy Commission shall establish a time differentiated incentive structure that encourages plants to run the maximum feasible amount of time, and to provide the higher incentive when the plants are receiving the lowest price. This is quoted from SB-1038.

And I asked why was this language included in SB-1038. The CEC investment plan of June 2001 adjusted the tier pricing. And it essentially established a 5.5 cent per kilowatt hour number for 2002 through 2006.

And in that report the rationale for that was that, and I quote, "that under SB-90 the target price decreased with the expectation that cost shifting would occur, particularly amongst the tier 1 technologies.

When this failed to occur and the target price for tier 1 technology dropped under the SB-90 program, biomass facilities were unable to generate as much electricity.

That is the rationale for why this Commission established the tier structure that it did.

The Legislature's response to that report, in passing SB-1038, was an adjustment to the CEC investment plan. And it essentially agreed with the tier pricing that was in the plan. And then added language regarding an adjustment for the inflation factor, quote, "The Commission believes" -- and I think this was in direct response to a comment that was actually in the report where the Commission had stated, and I quote, "The Commission believes that the price caps included in the existing renewables fund do not need to be adjusted for inflation."

And that was a debate that we had in a number of hearings in front of you, and was included in the report as the rationale for why you do not do that.

And here we have in 1038 a legislative intent that says the Commission shall consider this. I think it's in response to the fact that it was missing from the regular report. It's one of the instances where the Legislature stepped in and tried to perfect that report from that perspective.

Now, why is all this important? The implications are potentially very large. Reducing cost effective output from existing facilities will impair the ability of the IOUs to meet the RPS standard.

As new procurement of renewables is expected to be delayed, cost effective output from existing facilities is critical to meeting the RPS standard in the near term and over time.

As a practical matter, other than San Diego Gas and Electric I don't know if other utilities have executed any renewable contracts per the PUC decision that wanted them to do that before the end of the year by filing advice letters.

Those procurement decisions are being delayed. As a practical matter they're going to be delayed until probably next year when the SB-1078 implementation proceeding at the PUC will start. And in my estimation that is going to take a number of months, if not a full year, to complete.

In the meantime we run the risk of losing important generation from existing facilities which could be used by the IOUs to meet their target. And, Commissioner, as you pointed out, there's limited funds in the account the way things are structured under SB-1078 to procure new resources.

If the existing resources diminish, the output from those facilities diminishes because of the tier structure that you endorse and establish here.

And then there's still going to be a cap on the amount of new. And we don't know what that cap's going to be because we haven't had a procurement, and there doesn't seem to be any evidence that the utilities are actually going to enter into any contract before the end of the year this year, and certainly there won't be a full procurement until way late in 2003 under SB-1078.

So there's a huge risk that the

utilities are going to lose a significant amount of generation, renewable generation. We lose the environmental benefits, the jobs benefits and so forth.

And quite frankly, the utilities are going to lose the ability to count that against their RPS standard which has a rolling over effect. So, in my mind, they ought to be very incented to try to increase the output from these facilities, particularly if it's cost effective.

I suspect that a marginal increase in the tier funding that's before you in this account is significant in terms of achieving an incremental increase in generation from existing facilities.

So my recommendations are as follows: Retain the tier structure prescribed in the investment plan that was adopted by the Commission, particularly for the year 2002. Nothing has really changed since the Legislature acted.

Integrate a time of use pricing mechanism. It may be there, I don't see it. And I think it's important to develop a mechanism that reflects that intent from the Legislature.

And also integrate an inflation factor. Again, that may be there. My read of the CEC investment report from June 2001, there was an explicit acknowledgement that it was not there. And that's what the Legislature stepped in to ask the Commission to look at. So I make that recommendation.

And I'm available for any comments.

COMMISSIONER GEESMAN: Okay. Are there questions for Steven?

MR. TUTT: I just have one, I think. In SB-1038, the investment plan is incorporated by reference except for those parts that the law specifically changed or laid out, is that right?

MR. KELLY: Yeah.

MR. TUTT: I'm looking at the investment plan and it says on page 39 that, as we've always expected, that there should be flexibility in this. That the program design should be flexible enough to allow modifications in parameters as needed to adjust to changing market conditions.

And then it says one example of a situation that could trigger a change in program structure is the reconsideration of the fixed price contracts for existing renewable facilities that were considered in early 2001. In this case production incentives based on target prices may provide little benefit to the industry and the state.

So maybe that's one reason to justify the policy that the Committee has currently laid out. I wonder if you could comment on that?

MR. KELLY: Sure. I've been a strong supporter of this Committee and the work in the past guidebooks. And one of the components of that was flexibility. And I recognize that, that you may well have the flexibility and the authority to do whatever you want with these guidebooks.

But I think the more important issue is the fact that most of that flexibility was designed to allow you an opportunity and a mechanism to make changes as needed on a going-forward basis, and as circumstances changed in the future.

It's only been 40 months since the Legislature passed SB-1038, and I'd venture to say that very little, if anything, has changed since then.

So I'm not arguing that you would not

have the discretion to modify the program to meet the needs on a going-forward basis. I don't think a case has been made yet to show that there's a significant change from either from when you adopted the report of June of 2001, really, or when the Legislature formally adopted it and blessed it in August of last year, four months ago. It seems to me there's no condition that has changed in that regard.

The Legislature was aware of that, of the conditions that stood at that time when they enacted 38, SB-1038.

MR. TUTT: Would you agree that when we drafted and adopted the investment plan that there were no fixed price contracts in place at that time? Or that those fixed price contracts were --

MR. KELLY: I don't know if there were no --

MR. TUTT: -- not in place at least statewide?

MR. KELLY: Certainly the most of the generation was on SRAC And not on a fixed price contract. But when the plan was adopted it set a target price of 5.5 cents based on market conditions and a number of hearings that we had

had dealing with what the proper level ought to be.

That number exceeds the 5.37, and I'll offer that the companies that entered into the 5.37 deals were entering into those deals in the context that the Energy Commission was considering, and I think it blessed for some of them, a plan that set a target price at 5.5 cents.

I would imagine that a number of companies probably entered into those 5.37 deals with the strong presumption that they would be eligible for additional supplemental payments that would make those deals more economically attractive.

As you recall, the debate about the 5.37 deals was a long and arduous negotiation amongst parties. I don't think, as is the case with any bilateral contract, it's very seldom that both parties get everything they want. I think in this case there were -- entering into a 5.37 deal enabled those companies to get paid for the back due. And that was critical for the decision about the enter into that deal.

And, with the Energy Commission's report out there saying they were going to set a target price at 5.5, arguably a company would go into that deal to get their back payments, which was very significant for a number of companies, for most of them.

And with the presumption that they would be able to receive supplemental payments from this Commission to cover their needs.

COMMISSIONER GEESMAN: Other questions for Steven? Thank you, Steven.

MR. KELLY: Thank you.

COMMISSIONER GEESMAN: Peter Weiner.

MR. WEINER: I'd like to defer because I logically come after --

COMMISSIONER GEESMAN: Okay. Bill Carlson.

MR. CARLSON: Thank you, Commissioner. I've been madly sitting back there whacking away at my comments after, so I didn't repeat Steven's.

I am Bill Carlson of Wheelabrator. And I've drawn the short straw today and I'm speaking on behalf of the California Biomass Energy Alliance, which represents about 90 percent of all the biomass producers in California that have been acting participants in the existing renewables program since back in 1997.

We're approaching the end of a long process established to implement AB-995, legislation that continued the renewables program to 2012, with the first increment of 2002 through 2006 to be defined by this process.

I'd like to read a couple of short quotes from documents produced as part of this process that will explain why we take significant issue with the current Committee draft and that form the basis for our recommended changes. And, again, I will not repeat things that Steven has already said.

The first is from the Commission's June 2001 report to the Legislature that established the 5.5 cent target price for biomass beginning of 2002. Quote: Some biomass facilities have a lower core fuel cost which may allow them to operate at some level without additional incentives. However, to operate at levels approaching 100 percent of their capacity almost all biomass facilities must compete to obtain higher cost fuels."

"The further facilities must go to obtain fuel the higher the overall cost of the fuel becomes, primarily due to increased transportation costs. The biomass industry has demonstrated to the Commission that the cost of obtaining these marginal fuels is approximately 3.5 to 5 cents per kilowatt hour, including collection, processing and delivery costs." End quote.

The second is from a November 28, '01 letter to program participants from Commissioners Moore and Rosenfeld clarifying the treatment of those holding recently signed 5.37 cent replacement SRAC amendments. Quote:

"Because the 5.37 cents per kilowatt hour price is considered to be a [quote] "replacement" for SRAC" [end quote] the Electricity and Natural Gas Committee has determined that it will be treated as if it were SRAC for purposes of payments from the existing account." End quote.

I will not repeat the references to the 2002 payments that Steven made, or to the references to the inflation adjustment.

But lastly, I'll include one quick quote from SB-1038, itself, the legislation that established the hearing process that we are currently engaged in. Quote:

"For the first year biomass technologies the Energy Commission shall establish a time differentiated incentive structure that encourages plants to run the maximum feasible amount of time, and that provides a higher incentive when the plants are receiving the lowest price." End quote.

Taken together these quotes begin to define a tier 1, and specifically a biomass program quite narrowly. It is a program that recognizes that biomass plants have high and rising marginal costs at high capacity factors, and yet are compensated at relatively low rates during certain time periods, even the 85 percent of plants that are under the 5.37 substitute SRAC.

Clearly the evolving concept was to direct the existing funding to plants during those periods when marginal costs are above revenues.

And this is done in order to secure the environmental and economic benefits Californians derive by the operation, not the mere existence, of these plants.

The public goal is clearly operate existing biomass plants as much as is feasible, and to carefully use the fund to accomplish that.

We now turn to the Committee draft that is the subject of this hearing to see how it matches the expected program. The simple answer is that it falls short in virtually all areas.

Payments for 2002 are not included in the draft. Most biomass plants relied on statements by the staff and Commission in deciding whether to run at full output in 2002, even though absent program payments they would often be receiving in revenues less than their marginal costs.

All of us had the full expectation verified several times that the results of these workshops would be retroactive to January 1, '02. Others this morning will discuss their individual decisions to run at full capacity in 2002.

SB-1038 anticipates a time differentiated incentive structure that pays plants a higher incentive when prices are lowest; and adjusts those incentives over time according to the effects of inflation. The Committee draft has neither a time differentiated incentive structure, nor does it adjust for inflation.

The industry anticipated that those with the 5.37 at average SRAC would qualify for the program. The Committee draft eliminates that 85 percent of the industry from consideration. We thought this issue had been put to rest at the end of 2001 based on the memo that I read in a manner that would allow these plants to participate against the established targets.

The industry anticipated that these workshops would attempt to work out a structure where perhaps both the funds from the agricultural biomass program in the general fund and the existing renewable ratepayer fund could be used by the industry.

This draft categorically eliminates the use of agricultural biomass funds. And that point has subsequently become moot with those funds being eliminated in the latest round of budget cuts.

We are left with these ratepayer funds targeted for existing renewables as the only potential source of funds to allow biomass plants to run during low revenue, high marginal cost periods.

The structure of the biomass industry is such that nearly all plants have a supply of local, relatively low cost fuel that will allow them to run at a fairly low annual capacity factor. Good business practice requires us to utilize such fuel during periods when revenues per kilowatt hour are the greatest.

As the plant operates more, fuel costs begin to rise steeply as the plants begin to reach out further and utilize fuels such as agricultural and forestry waste that have high collection and processing costs.

But it is the use of these very fuels that has the greatest environmental and economic benefit to Californians, as open burning of ag waste is avoided and forest health is improved.

Under existing contracts the cost of fuel, plus other variable costs, exceeds revenues during certain time periods without supplemental funding. Revenues fall as low as 4 cents per kilowatt hour under the 5.37 amendments, and are further degraded by the recent application of generator meter multipliers which lower final payment up to 10 percent in some cases.

The plants will simply not produce those kilowatt hours, and California will not gain the benefit of proper disposal of these waste materials.

The Energy Commission, Commission Staff and Legislature all understand this relationship as is evidenced by what I read earlier. But the Committee draft does not recognize this relationship.

So what will be the impact on the biomass industry if the current draft program is approved without change? A typical biomass plant will either curtail its operation or close between 30 and 60 percent of the hours in the year, those hours when revenue will be close to or below marginal cost.

In total, this will equate to a loss of perhaps 1- to 1.5 billion kilowatt hours annually of renewable energy; or over one-quarter of the current biomass industry output of 4.1 billion kilowatt hours.

This equates in natural resource terms to over 30,000 acres of orchard prunings and removals that will now be open burn. And over 60,000 acres of forest that will not be thinned and fire-proofed every year. We will show graphically this relationship in our written testimony.

In terms of the SB-1078, mandated growth in renewable electricity, the impact will also be major and negative. The loss of 1 billion kilowatt hours annually is a full 5 percent of the state's renewable electricity output that will have to be made up elsewhere to keep the program on track.

It is truly a false economy to think that by not spending the existing funds, and instead shifting them to the new program, that you can generate the billion kilowatt hours as cheaply as what the small subsidy to biomass plants during their low revenue periods.

As an alternative to the Committee draft, the CBEA reiterates its previous testimony before the staff workshop. That proposed program establishes a target price and cap of 5.5 and 1 cent per kilowatt hour respectively during on- and mid-peak periods, and a target price and cap of 6 and 1.5 cents during offpeak periods. Maintains the eligibility of those in 5.37 contract amendments. Allows those with other contracts comparable access to the program. And adjusts the schedule for inflation using the CPI.

The CPI adjustment is particularly important to the industry, as the cost of marginal fuel is totally subject to inflation.

This program creates the opportunity to run all plants at full output whenever feasible for the smallest amount of money. It meets both the letter and spirit of SB-1038, while doing so within the established budget.

It captures for Californians the full environmental and economic benefits of the biomass industry. And it advances the renewable energy mandate of the 1078 program.

Far from being complex, generating windfall profits, or being easily gained, the CBEA proposal relies on standard utility statements and established time of use distributions that are both approved by the CPUC and are long standing. These standard forms will be supplied to you with our written comments, along with a sample calculation spreadsheet that has been previously supplied.

Should any of these distributions change the Commission would be well within its mandates to reconstitute this program, as has been done in the past. Providing a small subsidy when revenues are below marginal cost is not a recipe for windfall profits.

In conclusion, we ask that you consider the CBEA proposal for the distribution of tier 1 biomass funds, as opposed to the current Committee draft.

The outcome of this proceeding is critical to the future of those remaining biomass plants in California, as it is to the future of the entire renewables program.

Thank you.

COMMISSIONER GEESMAN: Questions for Bill? Tony.

MR. GONCALVES: Bill, as far as the time of use, how would you recommend we apply that, for example, to facilities that are not under utility contract and whose time of use is not broken out in the same timeframe. Because both PG&E and Edison's peak, offpeak and so forth, timeframes don't necessarily match up.

What would be your recommendation for those who are not under a utility type contract?

MR. CARLSON: Okay, sure, now just to give you a little background. Both Edison and PG&E use a four-tier program. Some parts of the year you only have three tiers; others, you have four.

And typically -- we don't know, of course, with the DWR contracts essentially going away at the end of the year, we don't know what those new contracts will necessarily look like. Some of them may be new utility contracts with Edison, PG&E or San Diego out of the bid process. And so those may take care of themselves by being distributed.

The others, you know, one option is clearly to look at the average compensation and give that to those parties. Or, another method, of course, would be simply to compare their actual contract against the target prices and caps that you set up. And just compare during those periods the prices that they're actually receiving.

Because they have the same problem. They, again, have the problem with the high marginal cost fuels, if they're attempting to run all the time.

MR. GONCALVES: Just one other question. You mentioned the GMM factors, and I know all the time of use numbers are already, at least for PG&E have the GMM already included.

MR. CARLSON: Right.

MR. GONCALVES: How would you recommend

we deal with that?

MR. CARLSON: Yeah, the problem is that in the statement, itself, from PG&E, while they tell you how many kilowatt hours you generated in each of the periods, when they go to pay you they apply a GMM to it, so it's not -- it's almost as if for each plant you'll have to come up with an average GMM to apply.

The problem in biomass plants in particular is that they're typically so remote, because of access to their fuel supplies, that they're far from the load center; and the decrease in value of the kilowatt hours is more dramatic for a biomass plant than it is for most other technologies.

COMMISSIONER GEESMAN: Bill, remembering that we're a government agency with 20,000 different things to do, would you revisit your comments about complexity, as it relates to trying to create a time of use, or time differentiated payment structure on our side.

Is there a simpler way to do it than your original proposal in the workshop?

MR. CARLSON: There are, of course, several ways to do it. You can simply establish a single target price and then look at the average; that is one approach to take.

It doesn't -- we've always believed that the smallest amount of money applied against the shortest time periods, but still creating the proper incentives, is the way to utilize the fund.

COMMISSIONER GEESMAN: In the abstract I agree with that.

MR. CARLSON: Yeah. But then you run into the issue of complexity. Fortunately, the statements themselves yield most of the information you need. And we had prepared a simple Excel spreadsheet that you simply dump about four numbers into per month and it calculates the -- it's really fairly easily done. Tony has raised the biggest issue, which is what happens when you try to apply GMM multipliers. Because those change by hour.

So, like I say --

COMMISSIONER GEESMAN: But that's not a problem in the Edison service area.

MR. CARLSON: Yes, it is. Under the new ISO regs, I believe. Is that right, Tony?

MR. GONCALVES: I think the Edison ones --

MR. CARLSON: Or do they have the --

MR. GONCALVES: The GMM --

MR. CARLSON: Greg, you --

MR. GONCALVES: -- they've actually showed the actual generation, and then adjust it. So they show the actual generation, not -- unlike the PG&E where it shows the GMM adjusted numbers already. They actually show the actual by time of use.

MR. CARLSON: There's only a couple of biomass plants in the Edison territory, so --

COMMISSIONER GEESMAN: Well, we hope to change that.

MR. CARLSON: Thank you.

MR. TUTT: One more question?

MR. CARLSON: Sure, Tim.

MR. TUTT: You read something from the investment plan talking about high marginal cost fuels, and the ability to operate 100 percent or maximum amount of time.

I think one thing I'd pose to you that since the investment plan was drafted, I asked you this in the workshop, I guess I'll just ask it again.

We've all become aware that the state

has contracted for, for better or worse, for a significant amount of energy in offpeak times that we don't need.

And so does that change, in your mind, the economic benefit? Obviously there's a benefit for using the waste materials and biomass facility, but now there's actually we've become aware of an additional cost of doing it in offpeak times.

And how do you account for that in your proposal or your testimony?

MR. CARLSON: That's a good question, Tim. The answer to that, of course, that we believe is that the real value in a biomass plant in California is not necessarily its electricity.

The real value to California is the propose disposal of those waste materials that would otherwise be open-burn or accumulate in the forests.

And if you're, for instance if you're selling offpeak electricity for 4 cents under a 5.37 contract, you're still not, at least with current gas prices today, you're roughly probably at the market, very close to the market.

And if another .8 of a cent or a penny

would cause those waste materials to be utilized, that probably is still a better value for California instead of simply shutting the plant down and buying from some gas-fired generator.

COMMISSIONER BOYD: I think this little discourse is almost the most important component of this question today. I mean those who have known me for many years know that I've really been a supporter of biomass.

And most of our dialogue of late took place before the state took out the mortgage. And now, you know, now we're wrestling with that dilemma.

And I think Tim's question is right on. And I appreciate your response. I agree with your response. We have to wrestle with, collectively with the dilemma that we all find ourselves in.

So, look forward to trying to learn more today to wrestle our way out of this.

MR. CARLSON: Thank you.

COMMISSIONER GEESMAN: Thanks, Bill. Greg Lawyer. You're next, Peter.

MR. LAWYER: I appreciate you having me come on early. I'm going to talk a little bit about a plant owner/operator, and supplement a little bit about what's being said by Bill Carlson.

Colmac Energy, I'm President of Colmac Energy, Incorporated. We run a 47 megawatt biomass and petroleum coke-fired plant in southern California. It's at the north end of the Salton Sea in the greater Palm Springs area down there.

We've been running nearly 11 years. We had our ten-year anniversary on February the 2nd of this year. And as you know, under our contract with Southern California Edison we went from our fixed energy pricing to so-called SRAC energy pricing, or published energy pricing.

As part of our corporate planning activities we did an extensive six-year planning horizon. And at the time we did it the first time around we did not have the 5.37 cent amendment, and that six-year planning horizon said, well, we've got a chance under seasonal operation, i.e., the June, July, August, September operational period, to pick up our peak periods.

Well, under an SRAC of the 3.5, 4 cent variety, it was a nonstarter. That plant would have shut down under those conditions. We were salvaged to some extent with the advent of the

5.37 cent amendment. But that still is on the margin, as mentioned by Bill, during the offpeak periods where we're actually losing money during those periods.

Now, under our planning horizon we looked at several scenarios we could pick up some midpeak during the May, October, November periods, as well as during the summer periods. That would give us a six-month operating cycle. And then we also looked at year-round operating strategy using both the 5.37 cent amendment, coupled with the SB-1038 energy price supports.

Under the scenario where we would go to a seasonal operating characteristic, I think Bill's comments are important. There's a number of things beyond just the production of electricity that come into play here.

When we were approached by Southern California Edison several years ago to buy out our contract, well, Riverside County was the biggest people to come forward and say, hey, you can't do this; you can't shut this plant down because it's so important to our recycled waste stream.

As you recall, under AB-939 there's a requirement for cities and municipalities to increase their diversion from their county landfills. And they said they would be susceptible to hundreds of millions of dollars of fines because we're taking about 9 percent of the diversion into our plant on an annual basis.

The other thing that occurs is under our monitoring and enforcement agreement, which is our basically our permit for operation, we're required to take 100,000 tons per year of so-called offset fuel in the Coachella Valley.

Now, the Coachella Valley has had a habit over previous years of open-field burning. The crop rotations in that area require crops to be rotated fairly quickly. And, of course, you pile up residue from these crops; throw a match in it and off it goes.

Well, we had a requirement for 100,000 tons of offset fuel. When we bring that offset fuel -- we had a grinding operation, as well. We had a mobile grinder with a crew that's under our employ. It will go out and take these farmers' residuals, if you want to call it that; grind it and bring it into the plant. We can do about 100,000 tons a year, and we could burn this material with about 1 percent or less than 1 percent of the emissions that are evident from open-field burning. That's a very critical part of the air quality requirements there in Riverside County.

The other thing is, of course, the employment and economic infrastructure. We employ 52 people at the plant, but if you look beyond that to our supply infrastructure, which are beholden to this plant, these people work almost exclusively on our behalf, there's well over 100 people employed to do that.

Now, my fuel manager tells me, well, we go to a peaking strategy, as we call it, where we run during the peak period. It's going to be real difficult to keep that infrastructure together. And she says darn near impossible to keep those folks together right now, because they work on a two-week payable.

I mean they're living hand-to-mouth. We pay them every two weeks for their deliveries to the plant. And, of course, if we go down to a four-month operating cycle, they're going to have to do something. And we're probably going to have to subsidize them to some extent during the off years for future delivery, something like that.

So, that's another one of the critical parts of this equation.

So not just -- we'll do about maybe 380 million kilowatt hours this year. The plant will run at nearly 95 percent capacity factor. But the other three characteristics of emissions, the economics in the regional area, and the AB-939 diversion requirements are an integral part of this whole operation.

So, with that statement, I implore the Commission to consider full funding under the provisions of SB-1038.

COMMISSIONER GEESMAN: Questions for Greg? Thanks, Greg. Peter.

MR. WEINER: Thanks very much. I have a limited role today. I want to go back just a little bit because I've been involved with the Legislature's approach to biomass, and so some of biomass, for a number of years. And have recently been involved quite deeply in the PUC procurement decision.

And I guess the bottomline is that this is the bottomline; the buck stops here. And there are no other bucks.

If we go back just a little bit in time

we find that the waste board came out a few years ago to say that there were external benefits, environmental benefits that weren't counted by the market in terms of the service provided by biomass.

Even before that the Legislature added section 701.1 and 701.3 to the Public Utilities Code telling the PUC to try to quantify the environmental benefits offered by renewables. And until they could do so, and that's where 701.3 came in, we know that's kind of hard, so until you do that have a set-aside for renewables in terms of procurement plans by the IOUs.

The attempt now by the Commission to implement that provision is met unfortunately, I'm not sure -- I came in perhaps after you referenced statements by some of the other utilities. I heard what you said, Dan Richards said, and I, of course, fully support Dan in almost everything he says.

Unfortunately, from our point of view, and we've been on public record about this, Edison has not complied with the renewables mandate at the PUC. They haven't even filed an advice letter yet. And they've taken the position, we believe contrary to the express views of the Commission, that they don't have to have renewable power online until December 2003.

And they've also, of course, said the Commission has no authority to do this, and all the rest of it. Also, when they did a solicitation, which they, again have not finished, they said quite bluntly, we will not consider anything that's over a certain price, even though the Commission's order said it's competitive, be above or below.

With PG&E we've had similar problems that resulted in a number of biomass facilities not getting contracts through that solicitation because they decided, again, we believe contrary to the Commission mandate, to count existing geothermal as part of their 1 percent additional.

These are legal issues that we're pursuing before the Commission. But the bottomline, of course, is that the Commission, at this point, has not been able to say or provide long-term security for the biomass industry.

Moreover, with the construct of 1078 there is an increasing cry by the utilities that anything above what they consider to be quote, market, should be paid out of these kinds of funds.

If we then digress and go back a few years, to talk about what the Legislature has done, the ag grant funds were adopted as an administration initiative by the Governor at a Fresno economic summit. And I'm not sure whether Mr. Boyd was there at the time, I don't think you were, Mr. Geesman.

But it was done on the basis of environmental analyses by -- Ware at the time, who showed that day-in and day-out, good days, bad days, biomass facilities in the Valley reduced pollutants by 95 percent over open-field burning.

And a coalition came together of almost every local farm bureau in the Valley, every board of supervisors, a lot of city councils, environmental groups, including the Sierra Club, to all say we have to fund this. And if we can't do it through ratepayer, just payments for electricity, we should do it in some other way. And we came up with general fund monies.

Those monies were enormously successful but they weren't arbitrary. They were based on a very careful study of the additional costs of agricultural fuel. Because without the incentives in some way what the biomass facilities found was that urban wood waste was a lot cheaper. And although they were required to burn some local ag waste, as part of offsets, it wasn't very much.

What we're looking at now, if we compare it to a figure certified by the air districts, as to the results of what happens when you burn ag fuel in biomass facilities, and you look at the loss that Bill Carlson referred to earlier, of about say 1.3 billion kilowatt hours, as a result of the proposed Commission implementation of 1038, we estimate that -- and these are pretty conservative estimates at this point if you grant us the assumption that people will not produce during these low cost periods -- if you lose 1.3 billion kilowatt hours that would be 1.3 million tons, bone dry tons, of ag waste.

Not everybody burns 100 percent ag waste. Some of them are burning 80, 60. But let's presume for a moment that it's only 50 percent ag waste. That would still be 650,000 tons of ag waste that would now be open field burned because there would be no market for it.

That would result in San Joaquin Valley

air in over 2400 more tons of PM10, and over 1300 more tons of NOx.

We know that the San Joaquin Air District, David Crow has been extremely supportive of the biomass facilities continuing operation only really because of air quality. I don't think he's focused on jobs and so on and so forth.

But strangely enough not only has the Farm Bureau been supportive, but other businesses have been supportive because of the radically severe air quality problems we've got in the Valley, and the impact on the economy of further constraints if you don't have some savings in this way. Because you'll have to get the air quality benefits somewhere and it means further ratcheting down in the economy there. So it has real multiplier effects in the Valley if these guys don't operate.

At this point, as you know, although the Governor has been supportive of the ag grant program, we have a little deficit, and we are facing real tough times. Last year it was preserved at 4 million; it is now proposed to take that 4 million off the table. So that we have no other source of funding.

And that 4 million was supposed to pay for the last half of 2002. If it's taken off the table the facilities that took out loans, made fuel contracts, paid the chippers to get the ag fuel will not have the money to pay back. And if this Commission then denies 2002 payments, we will have an even worse problem.

Unfortunately, it's not like Brazil; they don't get to go and have their debts forgiven. And what we're facing now is the closure or radically impaired operation of these facilities.

Because most of these facilities are operating at the margin the most they're getting out of it is debt service and costs. They can't afford a further constraint.

I'm not going to repeat all of the detrimental reliance materials that Bill referred to, and I think other people will talk about, in terms of how facilities relied on this 2002. But I'm personally familiar with a number of facilities that either booked it as income, or used it to get loans from their lenders, and are now facing real sharp financial problems because of the cumulative effect of the proposed implementation.

Others have testified quite eloquently it's a lot cheaper to keep these kilowatt hours of business than to build new ones. Our previous experience with biomass, and I think Greg Morris can probably speak to this a lot more eloquently than I can, has been that when plants shut down it takes five years, six years and an energy crisis to get them started up again.

There's millions of dollars in investments to be made once they shut down. Not only in terms of equipment maintenance, but in just restoring a whole workforce that disappears.

So, I concur with the recommendations of Steve Kelly and Bill Carlson. And thank you for your kindness.

COMMISSIONER GEESMAN: Questions for Peter?

COMMISSIONER BOYD: If I could, you heard my previous statement. As you know, in the mid '90s a lot of us sat around trying to figure out the economics, as one of the cliffs was coming along and couldn't get it done.

The social benefits were pretty well established by then, but no dollars go with social benefits. We hoped maybe they would. They haven't to this day. Come back into government and we're still facing the same problem.

How do we get some of these communities who were so supportive of this concept and who would have very significant costs associated with their activities, were we not taking care of their biomass this way. How do we get them to put a small increment of that savings forward to help pay this cost that -- you know, the general fund did for awhile. You're right about the Fresno economic summit and the dollars that were put there.

Also a condition on that program was an assumption on those dollars where we'll get it figured out and we'll solve it this time. And the general fund won't have to do this again.

Well, the electricity sky fell; the financial sky has fallen; and life is tough for all of us. And I'm not asking you to solve that problem today. I guess I'm just putting this question back out on the table.

Besides letters like we get from the San Joaquin Valley District saying we really want this program, how do we get some dollars, some small contributions associated with those positive values transferred into this arena so that there is adequate money? And everybody shares and shares kind of equally in the cost.

MR. WEINER: My short answer is if you couldn't solve this problem, how am I supposed to, but --

(Laughter.)

COMMISSIONER BOYD: You're out there in the private sector and you have all the answers.

MR. WEINER: Yeah, right. No, that's in Washington they think that way.

My feeling has been for quite awhile that some of the answers are out there, but they haven't been adopted by government in a way that can be utilized to generate those dollars.

Mr. Morris and others have quantified the external benefits that are offered by the biomass industry. And it can be differentiated by geography; it can be differentiated by fuel source. But nevertheless, they're, I think, more than 10 cents. Others may disagree, but they are certainly there. And they can be quantified by economists and others with the help, of course, of qualified air engineers and so on.

They can be. And what we haven't done in California is ever adopted an actual value that one could then take from the Executive Branch of the Legislature and say, look, we have quantified this; this is how it is.

And here's who's getting the benefit. And we need to now find out do they pay the full benefit so that the -- we often ask industry to internalize the negative externalities of their production. Here we're saying, we might be saying to the public, you should internalize the positive benefits that you're getting from this operation into your cost structure, say, of electricity.

I think it wouldn't work out that way in the end because we also have other kind of contravailing positions within government. That's why we had a high cost fund, for example, whereby urban telephone users subsidized rural service. We wanted people in rural areas to have telephone service. And it was otherwise a monstrous cost.

So those kinds of decisions, it seems to me, can be made on a social and political basis, but it helps enormously to have the Energy Commission or some other credible government agency say, yeah, this is what it's worth, and here's how it's happening, and here's why it's important.

At the Fresno summit we were able to show that the cost of going out and getting prunings, which are just physically more difficult to manage than orchard removals, and further away, was about $18 a ton more than orchard removals. And that a $10 a ton subsidy, or about a penny per kilowatt, would be enough to incentivize these facilities to burn that waste.

And that was an economic showing. And it was accepted at a political level as worth doing.

But at least the way I read the RPS funds, they were put there without that quantification for this purpose. And that's why tier 1 was mostly biomass, because it was recognized that that's who needed the money most to convey and obtain the benefits that we all wanted.

And the problem that I've got now is, you know, pretty simply, they went out and spent the money and now they're not going to get it back. And it isn't so simple a matter as, yeah, but we don't have a lot of money right now; we need to think about what we're going to do with it.

It affects very basically the economic viability of these facilities. And that's the problem that we have. They do have to pay for fuel.

But I do think that if this Committee were willing to do so, I'm assuming that the biomass community would be more than willing to participate in that discussion.

And although it doesn't necessarily translate into those communities providing dollars or figuring out how to get them, I think it can.

Just one last line, when we were before the Legislature last year and we had a $10 billion or $12- $14 billion deficit, the biomass program from that previous year was preserved because there was an incredible outpouring of support from quarters that I think the Legislature frankly didn't expect to take the time and trouble to do so. The support's a lot deeper, as well as broader, than people sometimes think in the Valley.

COMMISSIONER BOYD: Well, yours truly personally appealed to the Director of Finance on that point, so -- but we can only carry this so far, so --

MR. WEINER: Well, thank you very much.

COMMISSIONER GEESMAN: Thank you. Questions for Peter? Thank you.

Nancy Rader.

MS. RADER: Good morning, Commissioners Geesman and Boyd, and the Commission Staff. My name is Nancy Rader, Executive Director of the California Wind Energy Association.

We submitted written comments last week, so I'll keep these comments brief.

We urge the Committee to revise the existing program draft guidebook such that payments for 2002 production are made; and to adjust the program parameters annually by inflation.

We were as much surprised as disappointed to find out that these two changes are needed, because I think virtually everyone in the renewables community had expected these changes to be made.

Regarding the inflation adjustor, had Commission representatives not assured us that the language we agreed upon in SB-1038 was sufficient to insure that the inflation adjustments would be made, we would have sought more explicit language. And I think, received it.

On the 2002 payments we were assured, as folks have said, in a March letter from the Commission Staff, that 2002 payments would be made subject to the terms of the new legislation; and that legislation does not preclude 2002 payments.

In addition, the Committee's October 16 notice of staff workshops, which contained numerous questions regarding whether and how the program rules should be changed, did not even raise 2002 payments as a question. And several of the questions and statements implied that they would be made.

So, for us, remedying these issues is a matter of sustaining our trust in the Commission's word. And given that the renewables market is largely supported by policy, it's important that investors be able to rely on the stability of those policies.

Oftentimes, those who have invested in the existing facilities are the same firms who are investing in new facilities. And they don't base investments on a shaky foundation.

I want to just address briefly the substance of the changes we're requesting today. The Commission's existing renewables program would be essential in meeting the Legislature's recently adopted 20 percent renewables portfolio standard legislation.

To meet that goal production from the existing base of renewables will have to be preserved. And I just want to say that I think that the policies that the PUC adopts on the RPS for benchmark prices and other policy details are going to have far more bearing on whether we meet the 20 percent target than what you're going to be deciding here today.

The Commission's June 2001 report to the Governor and the Legislature make clear that the tier 2 existing wind program cost effectively reversed the declines in wind production that were occurring prior to 1998.

The tier 2 program provides energy price security that allows wind project operators to confidently invest in turbine maintenance and repairs. CalWEA members operated and maintained their projects this year on the assumption that 2002 production would be covered.

The goal of the tier 2 program is to cover the gap between the cost of operating existing wind projects and the energy payments that those projects receive. Those costs increase with inflation. If the target price and caps are not adjusted by inflation, the gap will not be fully bridged.

We urge you, therefore, to revise the guidelines to allow for 2002 payments, and to annually adjust the program parameters by inflation.

Thank you very much.

COMMISSIONER GEESMAN: Questions for Nancy?

MR. TUTT: I have a couple. Nancy, the costs of generating wind renewable energy increases with inflation because of labor and other input costs that increase with inflation. So you're saying the payments that we make should also reflect that cost increase, is that correct?

MS. RADER: Yeah, I mean you made the one jump. You recognized that inflation was important by making the adjustment for 2002. But then you don't make it every year even though costs, you know, everything else goes up every year.

MR. TUTT: I guess my question then is if there were any changes of, even decreases in costs because of productivity improvements in operating a wind facility, would we also reflect that in our payments as you go forward?

MS. RADER: Well, I mean I think --

MR. TUTT: Are there no increases in productivity?

MS. RADER: Well, you evaluated them. You had a consultant evaluate the costs of the existing facilities. I think you concluded that the target price was the right one. And to keep that current with inflation, you need to adjust it.

You know, I don't think there are a whole lot of improvements you can make in maintaining existing facilities. You really have to rip them out and put in the new turbines to make that jump.

And, of course, this program, I should add, did support the repowering of some 200 megawatts of existing facilities. So that's important to note, also.

MR. TUTT: Okay, my only other question

was you said that in this March 8th memo that we assured the renewable community of retroactive payment for 2002. And I just wanted to point out, Nancy, that it says we intend to make payment.

So that was an indication, but I don't know if I'd state it as an assurance.

COMMISSIONER GEESMAN: Well, let me jump in there, too, because I know this is an important question for all of you. And it is a very difficult situation.

But, the policy of the Commission, which I think you are entitled to rely upon, is set by the Commissioners. There's just no way of getting around that. And I don't think the letter that was sent out earlier in the year represented anything more than the staff's best intentions.

I think it's entitled to be relied upon as the staff's best intentions. But I don't think it's anything more than that.

I spent 20 years in the capital market. I know something about detrimental reliance. So, I think that statements about trust and when you've given your word, and the like, I think really need to be put in the right context.

Other questions for Nancy? Thank you.

MS. RADER: Thank you.

COMMISSIONER GEESMAN: Jack Pigott.

MR. PIGOTT: Good morning; I'm Jack Pigott. I'm here today to represent the Geothermal Energy Association.

I'm here today seeking parity. And we have submitted written comments, or we will submit them. There's a stack out in the back. And attached to the written comments is a chart. And it's a chart that's prepared by the Department of Energy. What it shows is the relative costs of different renewable technologies.

And what the chart shows is that geothermal power and wind power have similar costs. In fact, wind power is slightly less expensive.

And the draft guidebook provides unequal treatment; in fact, geothermal is not included, and thus picks favorites among renewables.

Geothermal is the largest nonhydro renewable operating in California. The costs of maintaining production is high, especially when you consider the risk-adjusted costs of drilling new production wells. All you need to do is look at the statistics across the state, the number of geothermal plants that are not operating up to full capacity.

Some geothermal projects do not receive capacity payments under power purchase agreements, but instead are operating on a merchant basis. Inclusion of geothermal in this program would help insure that investments are made so that these facilities are available to compete for power purchase agreements pursuant to the RPS when those are available.

Back to the chart here. The information suggests that geothermal and wind should be treated equally. Existing geothermal and wind will be competing for power purchase agreements in the future. And -- concern that the subsidy to one technology would skew the market.

And we would urge the Commission to include geothermal in tier 2. We believe that you have the flexibility to do this. And in our written comments we have cited provision of SB-1038 that would allow that. And would also refer to the PUC Code 399(6)(c)(8) where the Commission is to find that wind is a cost effective source of reliability and environmental benefits, compared to other eligible technologies.

Thanks.

COMMISSIONER GEESMAN: Questions for Jack? Thank you, Jack.

Mark Rentz.

MR. RENTZ: Thank you, Commissioners, Mark Rentz, California Forestry Association. I am Vice President of Environmental and Legal Affairs; and I'm also a professional forester.

Just a little background real quick on California Forestry Association so you understand why we're here today. Our members own over four million acres of forestland throughout the State of California. They produce over 90 percent of the wood products and paper products that come out of the State of California.

As well as they are a major contributor to energy production, biomass, or some people call it green energy production, over 600 megawatts of power are produced by our members' facilities. And they were a critical contributor to the energy crisis of 2001.

When I mentioned the four million acres that our members manage, keep in consideration that that does not take into account the small amount of industrial, private landowners; nor does it take into account the federal or state forest lands that are also, that we operate on, in part.

There's people that are going to come before you and have come before you today that are much more knowledgeable in the specifics of what is before this Commission today. But I would like to be real clear on what California Forestry Association's position is with regards to this matter.

We encourage, first of all, generally speaking, we encourage the California Energy Commission to look for opportunities to provide incentives for biomass energy plants to run at full capacity throughout the state. And I'll explain from our perspective why that's our general position in a moment.

Specifically with regards to the matter before you today, we'd encourage the Commission to address the concerns and adopt the recommended changes brought forward by the various members of the California Biomass Energy Alliance. Several of those members are CFA members, as well.

I'm going to take a little different perspective and give you kind of a forester's perspective, or a forestry perspective on why I think it's very important what you're dealing with today.

Obviously we want CEC to -- we hope that you'll provide assurances that our members will have financial and regulatory certainty in maintaining their operations. And that is a very big challenge for you all today, given the budget concerns that we all are aware of.

As a representative of the Forestry Association and a professional forester, I must encourage the Commission just to look beyond the immediate responsibilities you have, both fiscally and regulatorily, and consider more of an integrated perspective.

Earlier I heard some concerns raised by one of you gentlemen, and I kind of would like you to look at it from a more integrated perspective, and I think you'd possibly understand our position.

I heard the term earlier that you raised, Mr. Geesman, about subsidizing. And I would encourage you to look at the term subsidizing from a more global perspective. The biomass energy industry also subsidizes a couple things that are very important to the State of

California. They subsidize human health and safety, as was discussed earlier by providing an opportunity for clean, green energy that reduces the air quality concerns that we have here in the State of California, pollution concerns.

They provide environmental protection by providing a source of outlet for materials that otherwise could not be removed from the forested landscape. We improve water quality, wildlife and fisheries habitat, recreational opportunities, and provide protections for the rural communities, or what were once considered rural communities, and now become known as the urban wildlife interface that continues to grow into the forested landscape.

That we subsidize through our energy, those benefits to the state and citizens of California.

If you look at the budget, as you raised, Mr. Boyd, concern of the budget, I'd encourage you to take an integrated look and perhaps talk to the Director of the Department of Forestry; or talk to the Regional Forester who manages over 11 million acres here in the State of California of Forest Service lands.

As you know, last year California experienced the worst fire season in its history. The costs associated, the budgetary costs to both the state and the federal government, go off the chart. And if you look at the projections for the out years, that curve is not going to flatten. It will continue to rise.

So, there is an integrated perspective of looking at the budget of what you can do here to help reduce fuels, will be a beneficial and a fiscal benefit to firefighting and bringing about healthy forests in the State of California.

I think it's also important to realize that while last year was a catastrophic fire year of insurmountable proportions, there were hundreds of communities at risk throughout the state. And in fact we have a map, and I will try and provide you next week a copy of that map, that identifies all the communities at risk. And there's an equal number in southern California as in the Sierras or in the northern California where the forested landscape is. All are in desperate need of removing various forms of biomass.

There is a threat to human health and safety, as I mentioned, as far as the air we breathe, the loss of human life, loss of property, and as you know, up in the northern part of the state, the actual loss of several communities as a result of forest fires.

The economics, I'm sure others will talk about. But I think it's important for you to realize that a lot of the biomass facilities that our members deal with are in rural communities. They rely on any form of economic certainty in those communities. They provide employment. And there is an economic downside if these facilities shut down.

Most of the operations that actually grab the forest fuel, put it in the trucks and bring it to the mills are small family operated. They are not large corporate entities. And those will be the first ones to go if those facilities are not in place. So you're talking about small family operations. I'm sure others will talk about it in greater detail today.

So, in conclusion, what I would say to you, this is a problem that everybody is struggling with, from Governor Davis and the California Department of Forestry, and I might note here that California is the first, and as far as I know, the only state in the country that has a California State fire plan. And an integral part of that fire plan is biomass removal.

And the President of the United States, the White House, as you know from the headlines this week, is also dealing with this issue through the President's Healthy Forest Initiative. An integral part of the success of that initiative is the ability to remove biomass and take it to someplace where it stored, dealt with, other than just burning it on the ground.

The opportunities to burn forest fuels on the ground are shrinking; they're not increasing, as you know, with the urban interface. And the California Air Resources Board is constrained on prescribed burning. So that option is becoming less of a reality, as opposed to more of it. Even though may people would like to see more prescribed burning.

So in conclusion I'd encourage this Commission to take any action it could to maintain a robust biomass energy industry in the state. I'd hope that we could come to, and resolve that, provide financial and regulatory stability.

I think California leads the country,

and will continue to lead the country in providing an excellent example of the opportunity to promote biomass or green energy. And I encourage the Commission to take seriously, I know you will take seriously, but consider adopting the recommendations from the California Biomass Energy Alliance.

I thank you for your time today, sir, and if --

COMMISSIONER GEESMAN: Thank you, Mark.

MR. RENTZ: -- there's any questions I can answer, I'll be glad to.

COMMISSIONER GEESMAN: Are there questions for Mark?

COMMISSIONER BOYD: I'd like to make a comment, if I might.

MR. RENTZ: Yes, sir.

COMMISSIONER BOYD: I appreciate your comments. And as you maybe picked up the drift from earlier dialogue, I know this area reasonably well. And I appreciate your asking us to take an integrated look at things.

just to save anyone else in the audience trying to educate me on this subject, why, for the three years prior to taking this job earlier this year I was Chief of Staff of the Resources Agency, and ran the State's Biomass Task Force, where we tried to wrestle with all the questions that you brought forward. And begged and pleaded for monies and what-have-you to recognize this dilemma.

I would ask you -- and then 20 years before that I was an air quality expert, I don't know about that, but an air-head, they say in that industry.

In any event, I'm well educated. And I appreciate all these benefits that the dilemma we've wrestled with, and that's part of my dialogue with Peter, is how to get the monies apportioned to pay for that.

So, is the President, in his plan, going to put up some dollars in recognition of this benefit that will help us pay for that? I will admit the general fund dollars avoided in fighting forest fires is a ripe target. And working with CDF and Andrea for years, we've tried to make that argument without as much success as we would like.

The same with the ag people, and the air quality people. They all get a benefit. How can we get a few dollars out of each community of interest to help pay this beneficial cost. Right now we're making electricity ratepayers, in effect, pay that cost for everybody except those few times when we get a general fund infusion. And then the economy goes south again and we lose the dollars.

So, we all need to work together on this; but -- this is an important audience, but there are a lot of other audiences.

You make a very good case, and I urge you to keep carrying your argument forward to other forums who control dollars or industry sectors or other interest sectors who get a benefit, who may have access to a way to get a little financing into this arena so we can have a balanced equation in what pays for this general good.

MR. RENTZ: Can I respond to that just briefly, sir?

COMMISSIONER BOYD: Please do.

MR. RENTZ: I think you make a very valid point, and I think that's probably going to be the biggest challenge, especially, as we all know, in these austere times of budget.

Part of the President's Healthy Forest

Initiative, and I wasn't there to participate in that development, but I know Director Tuttle was involved at some level for some part of the time, so I encourage you to communicate with her.

But part of the President's Healthy Forest Initiative is a result of the Western Governors Council that brought up this issue and developed a Western Governors Plan on fire and fuel reduction.

And I know, as a fact, reading over that plan, just the issue that you raised is an issue that was very significant to that plan, is what I think you're calling the funding issue. And I know the White House, the Secretary of Agriculture, who happens to come from the State of California, and the Secretary of Interior, very well aware that that is an integral component.

I think that -- I don't deny that I think that would be a very big challenge for all of us in these tough times to try and find that funding.

With regards to your second aspect, as far as the various communities, I think the gentleman preceding me gave a very good idea. And I think California has the resources, and I'm talking about the knowledge resources and the educational resources, to do that.

I would encourage some sort of integrated analysis, if it hasn't been done already, and obviously, Mr. Boyd, you have a lot more background than I do in this issue, try to look at a cost/benefit to all the various communities so there is a persuasive argument to be made as to why they should be contributing. You are offsetting in the costs if you're dealing with waste. You're offsetting with dealing with the costs of air pollution when you have catastrophic fires.

I know that was one of the big issues when they were dealing with the rice burning here in the Central Valley, was showing the offsetting costs that were gained by the cost attributed to another program besides burning.

So, I would encourage that as a preliminary step if it has not already been undertaken.

Can I answer any more for you, sir?

Thank you for your time, I appreciate it.

COMMISSIONER GEESMAN: Thanks, Mark.

Brian Dahle.

MR. DAHLE: Brian Dahle; I'm a Lassen County elected Supervisor, and I'm here representing Regional Council of Rural Counties. Thirty counties in the state; we're all rural. We encompass the area where a lot of these plants are based.

Everything that I want to talk about has mainly been covered today, but I would like to just give you a perspective from the Rural Counties outlook on this.

I come from a town where there's 500 people in the town. We have one local mill there with a biomass plant connected to it. The mill has been since shut down in the last couple years due to a variety of reasons, not enough saw logs and not enough energy prices. They went off the cliff.

So I'd like to -- as Supervisors we deal with the air quality, we deal with solid waste issues, landfills, and we deal with water issues. All three of those things are impacted by biomass.

As you know, thinning the forest helps reduce the catastrophic wildfires that we've been having, and the particulate matters that go into the air from that. And then also filtration for the water when it comes into our streams.

So we would encourage that you fund biomass plants at 100 percent of the time. The reason being is when they go up and down like this, when you're a small operator, family-owned business, most of our biomass removal people are small family-owned business. They have two or three pieces of equipment. They hire the trucking company to come in and pull it out, so the fluctuation in that time, they can't sustain that through the years. So they need to have a full slate so that they can plan.

And also, when you're buying some of these pieces of equipment at $300,000 apiece, it's very difficult to get your bank to go with you when you don't have a steady job for that equipment to be running out there.

So, I would encourage you -- and the 29 counties also passed a resolution wanting you to give these biomass plants full funding and we would totally 100 percent support that.

COMMISSIONER GEESMAN: Questions for Brian? Thank you, sir.

MR. DAHLE: Thank you.

COMMISSIONER GEESMAN: Bob Marino.

MR. MARINO: Thank you. I promise to use just a small portion of your time, Commissioner. I represent Fairhaven Power Company. Fairhaven Power Company is located in Humboldt County.

And I might say at this point that in recent history or recent memory Humboldt County had better weather than Sacramento this morning.

(Laughter.)

COMMISSIONER BOYD: This is a good Humboldt day, isn't it?

MR. MARINO: It promises not to be that case on the way back.

Fairhaven Power Company came online in September of 1986, and has a SO4 contract with PG&E. And did not participate in the 5.37 agreement.

Fairhaven Power Company burns hog fuel in 180,000 pound Riley Stoker Boiler with a water-cooled stationary grate. Natural gas is used as a stabilizer, as well as a startup fuel.

From 1997 till 2001 Fairhaven Power burned over 1.13 million tons of hog fuel, and over 8.9 million therms of natural gas to produce almost 900,000 megawatts to the grid.

From January 1st until December 1st of this year Fairhaven Power consumed almost 240,000 tons of hog fuel and 1.2 million therms of gas to produce over 89,000 megawatts to the grid. Over 62,000 megawatts was produced during period A of this year.

At the same time SRAC pricing averaged .03369 cents per kilowatt hour in peak time; to an average of .02992 cents per kilowatt hour in super offpeak hours.

In early 2002, facing projected shortages of hog fuel, Fairhaven Power shut down for approximately one month to conserve fuel. We also contracted for extra fuel derived from forest sources, forest waste products.

This fuel is not only more expensive, which has been testified to earlier, but there are other factors involved that directly impact power plants that burn this type of fuel.

It is dirtier than saw mill residual fuels. This type of fuel often increases maintenance costs related to the excessive wear on the boiler components. It is often extremely dry and prone to combusting while in storage, a problem that we faced at one time.

These decisions were made to insure that adequate supplies of hog fuel were available for the remainder of the year, and with the expectation of receiving CEC payments for 2002. The anticipated CEC payment was earmarked to defray the higher cost of that fuel which was purchased, as well as to offset the low SRAC prices.

A portion of the funds was also set aside to be set aside for use for major overhaul of our turbine generator coming up.

In summary, Fairhaven Power Company will be substantially impacted without a retroactive payment from the CEC for 2002. We firmly believe, as members of the CBEA, that a target price of 5.5 cents per kilowatt hour with a cap of one cent for tier 1 renewable generators will encourage us, as well as other plants, to achieve maximum generation.

Mr. Lawyer hit it on the head. If forced to curtail operations for a period of time perhaps seasonally, the workforce is severely impacted. Skilled and trained power plant operators are not readily available. So when you do go to fire up again where is your skilled labor force?

Thank you, Commissioner.

COMMISSIONER GEESMAN: Any questions for Mr. Marino? Thank you, sir.

MR. TUTT: I have one question, if you could answer. Your SO4 contract, you're off the cliff on that?

MR. MARINO: Yes, sir.

MR. TUTT: And is there a reason you can tell us why you didn't take the 5.37 deal, out of curiosity?

MR. MARINO: I can't answer that. I've only been in the management circle of Fairhaven Power for this year. And those decisions were made prior to that.

COMMISSIONER GEESMAN: Thank you, Bob.

MR. MARINO: Thank you.

COMMISSIONER GEESMAN: John Prevost.

MR. PREVOST: Thank you, Commissioners, for the opportunity to speak to you today. I have to admit when I first thought about coming down and talking to you, I was somewhat embarrassed when I felt I was going to come down and ask you for handouts.

And the more I thought about it the more I recognized that the money that's in the renewable energy fund is not handout money. It doesn't belong to the Energy Commission; it doesn't belong to the state. It came from the ratepayers to be disbursed to support renewable energy. And in 2002 $135 million were collected.

We've been involved in this process since 1997, as was mentioned earlier, through workshops with the Energy Commission Staff, with people from the Public Utilities Commission, Ratepayer Advocate Groups, environmental groups, the utilities and this stuff was well argued, well thought out and well laid out, with the anticipation that this would be ongoing programs as the Legislature approved it.

You can talk around the fact that yeah, we didn't really say we were going to do this, we didn't do this, we didn't do that, but the fact of the matter is that you made a proposal, this Commission made a proposal to the Legislature, and the Legislature approved that, period.

And those numbers that were in there, the reason that we were told by staff that we weren't being paid in 2002 when that legislation got passed; after it was passed they said it was not an emergency legislation so we had to wait till January.

So that is the fact of the matter.

I'd like to talk a little bit about our plant in particular, and not regurgitate on things that you've already heard. And I'd like to start by talking a little bit about the cliff.

We've been generating power in Scotia since the late 1800s. So we've been around awhile. We weren't hooked to the utility until 1986. And when we connected to the utility our thought process was that our main goal was to feed ourselves. And if we had any left we'd sell it. Therefore we had a standard offer 1 contract. And we went off the cliff in 1986, the day we signed the contract.

So we've been on SRAC until June of 2001 or July of 2001 when we signed the contract with 5.37 cents as an in-lieu contract. Not as, has been referred to in this documentation, as a high dollar fixed price contract.

These contracts were the result of negotiations with the state, with the representatives out of the Governor's Office, with the utilities and with the generators to come up with a contract that was going to put some stability in the state's electrical situation. And it did that.

Twenty percent of the state's generation comes from qualifying facilities who took those 5.37 cent average contracts which were in-lieu SRAC payments.

We came before this Commission and argued that those were, in fact, in-lieu SRAC payments; and this Commission did, in fact, pay us based on the fact that they were those, and not high dollar fixed price contracts.

I'd like to kind of tell you very quickly the impact on what we did last year as one company. We burned 600,000 tons of fuel in 2002. We will have burned to 600,000. 50,000 tons of that fuel came out of in-forest fuels or material that we pulled out of the forest, okay.

The in-forest stuff that we get on the north coast where we're at is probably the most expensive biomass fuel in the state. It's hard to get; it's hard to pull in; and it's hard to be able to make money hauling limbs in dump trucks to get them to an area where you can get a chipper or a tub grinder or whatever you're going to use to make fuel and get that in a chip truck.

So that 50,000 tons of fuel that we brought in was brought in with the anticipation that we were going to receive this funding. That fuel is not cheap. 50,000 tons generated 25,000 megawatts, 25 million kilowatts into the grid last year.

And when you look at what the funding that we would have gotten in 2002 and how that's impacted that, we're talking two tons of fuel for a megawatt.

So, you know, at the time we were getting, I think, 4.48 cents -- .48 dollars, 4.8 cents for that energy on average in the summer period when we pulled that fuel in.

Had we known we were not going to get this funding we would not have brought that fuel in. We would have open-burned it. 50,000 tons. And I'm here to tell you that 2003 going forward that 50,000 tons is going to get open-burned. It's expensive to bring it in. And without funding we're not going to be able to do that.

I talked earlier about the funding and how it comes from the ratepayers on a public goods charge, we are the largest generator, renewable generator in northwestern California. And we're also probably the largest utility customer in northwest California.

We have three external facilities where we have to buy power back from the utility; we can't run; we can't wheel power to those facilities; we can't do direct access. And we're buying that power back, and we're paying public goods charges on those bills. And they are big.

So, this is not something that we're not a part of on both sides of the fence, because we are.

You talked about earlier about using the funding that came from the ratepayers in the best way possible. And I've gone back and looked over some of the figures. And I hear a lot of stuff about new generation being the best of the future. It's all new. Well, if you can't protect the people that are standing here today, who are these new people going to be?

Right now you've got funds encumbered, virtually half of the money that was collected between 1998 and 2001, $541 million, roughly half of that money is encumbered in new plants.

Thirteen percent, 200 megawatts of those plants are online.

And every week that you people have meetings, you got new plants coming in here telling you how, beyond their control, they can't get those plants online. One of the reasons they can't get them online is because there's no place to put the power. They can't sell it. They can't move it.

In the last two years our company has spent a little over $1 million trying to increase our capacity. And we've done that. And guess what? It's sitting there because we can't move it.

So we've got almost 8 megawatts of power that's sitting there that we can't get out the door, renewable energy, green energy.

So, when you talk about the RPS and you talk about all these things that are going to solve the problems, you got to recognize when you go right back down to the utility, let's ask these utilities, how much renewable energy did you increase last year in 2002. How much are you going to increase in 2003. And when you try to get the stuff from the PUC, guess what? It's all blacked out. You can't see any of it.

So, other than secondhand information you don't know how much they're buying, but I'll tell you, it's not very much. And it probably won't be much going forward.

We talked about the net positive impact on the environment. I think that's been well stated. I won't go into that. But I would like to talk a little bit about the waste stream that comes out of these plants.

If you burn those 6 million tons a year that we burn of fuel, you generate ash. In 1990 38 percent of the solid waste going into the Humboldt County Landfill was ash from three power plants, two of which are still standing today, ourselves and Fairhaven.

AB-939 told the counties and the communities in this state they had to reduce what goes into those landfills by 50 percent by 2000. That 38 percent that was going in there in 1990, none is going in today. Every single ton of ash that we generate is recycled as ag supplement.

Humboldt County met their 50 percent almost on our backs. So when you look at not only are we burning the waste product, we're doing it in a good manner. We're reducing the fire loads in our forests. We're getting rid of stuff that used to be burned in teepee burners. And we're taking the product, the waste product from that that used to go to our landfills, and we're recycling it. And I think the recycling part is pretty universal throughout the state. I think most of the biomass plants are recycling that ash today.

I guess I'm here to ask you to honor, I think, the intent of the Commission when they went to the Legislature prior to SB-1038. I would ask you to strongly consider looking at the money that you've got encumbered for new plants that isn't happening. Seems to me that we're $20 million worth of plants -- Enron. I don't know if they'll ever get built. And there's probably a lot of plants that are on that new list that will never get built for a number of reasons. One of which, they can't move the power.

So, I would ask you to really strongly consider that, and look before you take money out of this existing fund and move it over to other areas in the program. That you strongly consider that there is a commitment not only by the

Legislature, but by the Governor, to continue to fund renewable energy plants.

So, what we're doing right here is pulling the plug on virtually the entire biomass community in the State of California.

I thank you for your time, appreciate it. And if there are any questions, I'd be more than glad to answer them.

COMMISSIONER GEESMAN: Questions for John?

MR. PREVOST: Thank you.

COMMISSIONER GEESMAN: Thank you, sir. Bob Ellery.

MR. ELLERY: Good morning; my name is Bob Ellery with Sierra Pacific Industries. We have seven facilities in California, four of which, starting a couple weeks ago, went back under contract with PG&E and with the 5.37 deal.

We have three other facilities that one of which sells power to Sierra Pacific Power Corp. and two that are in the open market, so to speak, as new facilities. One of which is funded actually under the new program, one of the few facilities that actually went online.

My comments today deal with, again, like everybody else, the 2002 money. Our facility in Loyalton was originally part of the sawmill. The sawmill was taken down due to lack of logs -- so it's now a stand-alone power plant.

We have struggled to keep that facility running. And quite frankly without the Energy Commission's support I doubt it would survive.

While I hear what you're saying from a legal point of view, we clearly relied on staff's letter that we would get funded in 2002. And made operating decisions and operated the plant the way we did because of that.

There is no doubt that, you know, if we don't get funding going forward, like I said, whether or not it would survive at all I don't know. But clearly we would reduce generation in the offpeak hours. We don't get enough, even get close to paying the incremental cost of that marginal fuel. So Loyalton would severely be impacted.

As far as the other facilities we're the largest private landowner in California. A lot of the marginal fuel comes from us and our facilities. It is very expensive. Ranges anywhere from probably $40 a BET to over 60.

Commissioner Boyd asked about, you know, subsidies from others. I will tell you from the private sector we subsidize that fuel. We look at the real value to our timberlands of removing that fuel versus open-field burning it versus leaving it in there.

And we assign a value. And that value, quite frankly, is higher than your support. And so, you know, when we look at saying well, those marginal tons are not going to be subsidized by the Energy Commission, I can assure you it will be a direct result in the reduction of kilowatts. As we cannot step up and double our support because of your reduction.

Those fuels are getting further and further away. With the environmental regulations in California our cost structures are going up exponentially. The more you can't cut down obviously the cost structure goes up. So, it will absolutely reduce our generation at all facilities.

There's been questions of staff about complexity of putting in a time of use program. I don't think it's that complex. Most of it is PG&E. There is only one facility, like I say we sell to Sierra Pacific Power Corp. I think there's only two with Edison. And there's probably less than, I'd guess less than ten facilities that are in the open market.

So I don't think it's very complex or difficult to set up a structure that deals with the, you know, those few facilities, other than PG&E.

And I guess -- my last comment is --

COMMISSIONER GEESMAN: Let me ask you there, Bob, -- process that would track every amendment to those contracts so that a well intentioned lawyer could not amend the contract in such a way as to maximize the flow of funds coming from the state?

MR. ELLERY: Having spent two years fighting with PG&E in litigation I'll tell you that is not easy. That's number one. Number two, we submit the invoices. You don't need to track amendments. You see the invoices.

Number three, what is the utility's incentive to do something that gives us more money and has no benefit to them? And the answer is none.

So the only way you could even think

about it is you'd have to basically say I'll take a lower rate so that we can somehow get more money out of the Energy Commission fund. I don't know any facility around that wants to take that on.

There's absolutely no incentive to do that. It just doesn't make sense. So I don't think that's -- like I say, you get the invoices anyway. So you could immediately pick that up.

COMMISSIONER GEESMAN: Remember, we're a government agency with 20,000 different things to do.

MR. ELLERY: Your staff has done a great job of this in the past, and I have ultimate confidence they could continue to do it. I know when I've had a problem submitting an invoice, it's been late, they're on me like that. So I have no doubt in my mind that they couldn't do a good job.

I guess in closing I'll just refer you to your own calendar. What we're really talking about is the biomass, you know. This is December 2003. And what we're trying to do is make sure we have as much biomass power online in December 2003 as we do in December 2002.

And what you're proposing, in my

opinion, will not result in that.

Thank you.

COMMISSIONER GEESMAN: Questions for Bob?

MR. MASRI: Quick one. Bob, when you say, just to make sure I understood you correctly, do it for non PG&E facilities, -- differentiation, is that what you were saying?

MR. ELLERY: Well, I'm saying you can do it for non PG&E facilities; there's not that many of us. Again, the rate structures are actually less complex than PG&E.

So you want to say here's a structure, can it fit in? Sure. I don't think -- if that's the overriding issue that results and you decided not to put in the rate structure, I would tell you put it in.

You know, for example, Sierra Pacific Power Corp., I have two rate structures; it's peak or offpeak, but my energy price is the same. Doesn't matter. Create as many rate structures as you want, my price is the same.

With the market, the market, as you know, with CalISO market is peak and offpeak. I mean it's a 6-by-16 peak, all other hours are offpeak. You know, we get lots of meter data. If you want us to restructure it in the format to fit your needs, okay, that's not hard.

As Bill said, I think CBEA has given you an Excel spreadsheet that could, you know, at least on the PG&E stuff, makes it simple, plug in a few numbers.

If you're saying to me you want to transfer some of that complexity to me that says here's my meter statement from the CalISO or from my scheduling coordinator, you want it reformatted into however you want it reformatted, we'll do it.

MR. TUTT: I just have a quick question for you, Bob. You have some facilities that are under the 5.37 deals and some that are out in the market, is that right?

MR. ELLERY: As we speak today, yes.

(Laughter.)

MR. TUTT: I was wondering if you could speculate or compare, because you've been doing this for awhile, in most of the year 2000, prior to the energy crisis, facilities were operating under SRAC; our target price for the tier 1 was 4 cents, our cap was 1 cent.

And comparing the revenue streams of

facilities in that year to what you're getting, say, under the 5.37 deals, or in current year with the 5.37 deal or without, how do they compare?

MR. ELLERY: The obvious answer is if you want to look at annual revenue stream from a 5.37 deal versus an annual revenue stream from an SRAC deal, there's a reason everybody took 5.37. Okay? It's obvious.

But that's not the way we operate plants. Okay? Because, you know, I don't operate to lose money. So, what does it mean with a 5.37 deal? Yes, we are more profitable. But the way I maximize my profit is not to lose money. So I don't run if I can't either at least break even.

And so you look at now the way they've got it structured, in my opinion it's crazy, because they reduce the rate in the summertime when the state needs the power. And they give me an incentive to run in the wintertime when they claim they have an excess.

That's not our structure, but, okay. We deal with that. So, okay, in the summertime we will reduce output those offpeak and super offpeak hours. That's a fact.

I mean when I have to go out in the

forest and spend $60 a BDT I can't make 4 cent kilowatts with it. I mean we'll contribute some of that, but I'm not going to contribute all 20 bucks.

So, and the problem with the -- okay, and I think most private people do that. I would, and I'm not familiar with the ag waste, but I'll bet those farmers are contributing, also, some way.

The problem is when you get off of the private lands onto the state and federal lands. And that's where the program falls apart, quite frankly.

We've been working for a long time trying to get federal subsidies and state subsidies and we have been very unsuccessful.

COMMISSIONER GEESMAN: Other questions? Thanks, Bob.

MR. ELLERY: Thank you.

COMMISSIONER GEESMAN: Kelly Lloyd.

MR. LLOYD: Good afternoon. My name is Kelly Lloyd. I'm a Certified Public Accountant and the Chief Financial Officer for EnXco, Inc. EnXco is a renewable energy company. Its corporate headquarters is located in Palm Springs, California.

EnXco has 13 wind energy companies in California. And our net ownership is 176 megawatts.

From January 2002 through April EnXco earned, they recorded on its financial statements, $223,000 in CEC funds. We did this based upon the following:

In March this year we received a letter from the CEC that Steven Kelly and others referred upon. This letter led us to believe that once SB-1038 was passed we would have to wait until January 2003 in order to receive our CEC 2002 earnings.

We did not have reason to believe that payment was in doubt. Only the timing of such payment.

In the second half of 2002 our company was sold. The CEC receivable was included in the sale of the company. EnXco plans on using this money to reinvest in California wind energy projects. In 2003 we plan on developing and bringing online 60 megawatts of new wind energy facilities in California.

In conclusion, EnXco believes that we

have earned the CEC money, and we have included these funds in our financial statements, and have provided those statements to our auditors.

EnXco needs this money to continue to develop new wind energy projects in California and to maintain existing projects we have.

Thank you for your time.

COMMISSIONER GEESMAN: Was the company, prior to sale, a publicly traded company?

MR. LLOYD: Private before; private now.

COMMISSIONER GEESMAN: Okay. And you said you carried it in your financial statements, but in your audited financials is it reflected?

MR. LLOYD: Yes, it is.

COMMISSIONER GEESMAN: And was the audit performed according to GAAP?

MR. LLOYD: We use accrual based accounting, that's correct.

COMMISSIONER GEESMAN: Other questions for Kelly? Marwan.

MR. MASRI: Is your facility on 5.37?

MR. LLOYD: All of our facilities are on 5.37.

MR. MASRI: So when you book that money, how did you estimate, not knowing what the target is, what the cap is at the time? Did you just estimate the amount of money? Or --

MR. LLOYD: I'm sorry, the --

MR. MASRI: -- the matter of accrued payments of CEC --

MR. LLOYD: I understand, I understand your question. Seven of our facilities are located in southern California. The 5.37 started in May for Southern California Edison, and I believe in July 2001 for PG&E. So this receivable is only related to the Southern California Edison.

How did we book it was based upon the same format prior to 2002, the SRAC rate. And then we, you know, we made the calculation just like we had done in prior months. Came up with the dollar amount. Recorded the entry.

MR. MASRI: The problem is for that period of time there were no parameters in place as far as target and cap, only the previous program.

MR. LLOYD: But, see, --

MR. MASRI: And so my question is --

MR. LLOYD: Okay, let me answer this --

MR. MASRI: -- you had to assume something to do that, and --

MR. LLOYD: Sure. What we relied upon was this -- I know it's been stated before that, you know, we didn't rely upon the Commission, you know, Commissioner, for this. But, as you may know, in the private sector this letter was actually signed by an accounting manager.

So we thought, you know, unbeknownst to us, that, for instance in our company if a development or construction manager or accounting manager or any other manager signs a letter, generally we adhere to it, because the CEO can't sign every letter.

So, you know, we relied upon that letter for our justification.

MR. TUTT: Kelly, did you say that you had booked this amount in your books for the January through April period only? Is that what you --

MR. LLOYD: That's correct.

MR. TUTT: Thank you.

COMMISSIONER GEESMAN: Other questions for Mr. Lloyd? Thank you, Kelly.

MR. LLOYD: You're welcome.

COMMISSIONER GEESMAN: Richard Steed.

MR. STEED: Commissioners, panel, my

name is Richard Steed. I'm General Manager for Eel River Sawmills which owns -- and the Power Company. I'd like to give a brief background without going over what Bob Marino went over.

Our company was founded in 1957 by Melvin McClain. It consisted of, in the last year, three sawmills and our power company. Those sawmills were shut down. The reason is because of historically low lumber prices and historically high log prices. And then lo and behold, PG&E doesn't pay for our power.

And in our company when we hit hard times with the lumber market we used our profits from the power company to help float the sawmills. So during that time that we didn't get paid from PG&E, we were forced to close our mills.

Now we went out this year and purchased very expensive hog fuel that was produced by two local ranchers. And one of the gentlemen hit it right on the head earlier, that a lot of your small chipping companies are small family-ran businesses. And the two that we use are.

We went out and, as a company, relying upon the 2002 payment, purchased fuel in preparation for Period A. Whereas we all know the

SRAC prices for May, June and July were pretty bad. Now, they're not that bad. I wish I had that fuel for that three-month period still stockpiled.

Tomorrow we are down, as a company, we will be out of hog fuel. The hog fuel shortages are due to our closure of our mills and another local sawmill company.

I'm just going to be real brief. We did rely on the Commission's payment totally. We were planning a six-week shutdown to try to stockpile some hog fuel so we could start back up.

We will not purchase any forest fuel next year because we cannot go out and make this mistake again, and then the 2003 payment not be made for some reason.

So I'm going to end it with that, but I would encourage that you seriously consider looking and making the 2002 payment, because as a company, we've lost -- we've gone from 475 employees down to 35 remaining, and that's the power company. And without that payment we are faced with a real hard decision to start up after our shutdown.

Thank you.

COMMISSIONER GEESMAN: Questions for Mr. Steed? Thank you, sir.

Mitch Schultz -- or Milton Schultz, I'm sorry.

MR. SCHULTZ: I looked around, I am Milton Schultz. I am General Manager of Burney Forest Power. It's a 30 megawatt biomass fuel plant located in Shasta County. This year we will be burning approximately 500,000 tons of fuel.

I'd like to just mention one capability our plant has. We were, in 1998 we were released from our contract with PG&E and were able to go out on the open market and sell electricity. We were one of the few plants that had that ability.

During that time we found that we could go from a zero load to full load at 30 megawatts within a half hour. Likewise, we could drop off from 30 megawatts down to a zero load within a half hour.

The fuel that we have consists of approximately 50 to 75 percent of in-forest thinnings, and the balance being mill waste. The cost of fuel could vary up to, for us, $42 per bone dry ton. And a bone dry ton really equates to a megawatt. So, in other words, it's $42 a megawatt for the cost of fuel.

Other variable costs that we have, such as ash disposal, chemicals, water, some labor costs, amount to $2 or more per megawatt, giving our variable costs equal $44.

We sell our electricity to PG&E under the 5.37 per kilowatt contract amendment. But because of our location and the GMM factor, the generator meter multiplier factor, we only receive 96.8 percent of the payment. In other words, 5.37 equates to us as 51.98 cents.

Now, John Prevost didn't mention it, but he has about a 91 percent GMM factor. In other words, almost 10 percent, the 5.37 means something just close to, you know, 4.8 cents.

But we're not paid on an annual average. For example, in the summer we received $44.63 per megawatt hour during super offpeak hours. Apply the GMM factor, means we were only paid $43.20, or an amount less than our variable costs, the $44.

Using the same calculation during offpeak hours we only receive $44.98 per megawatt hour. Now, barely covering our variable or marginal costs.

These offpeak and super offpeak hours

amount to approximately 60 percent of our total hours. What are our options?

At current prices, and without the CEC funding for tier 1 funding, Burney Forest Power must curtail operations during offpeak and super offpeak hours. It's the same thing that is faced by all of the other operators.

The limited generation that we do will be a big advantage to us. We will minimize our fuel purchases and start reducing fuel costs. We should end up in a better financial performance at the end of the year with our less production.

In the meantime PG&E will have lost some 75,000 megawatts of renewable energy, or 35 percent of our total annual generation. In addition, there will be 150,000 tons of fuel that we did not bring out of the forest from our high priced material. So much for SB-1078.

If you have any questions I'd be happy to answer them.

COMMISSIONER GEESMAN: Questions? Marwan.

MR. MASRI: Milton, nobody touched on this, but you're comparing the costs of the fuel with the energy revenue. Do any of your facilities receive capacity payments at all?

MR. SCHULTZ: Yes.

MR. MASRI: And does that help a little bit in covering the costs?

MR. SCHULTZ: Oh, the summer, the capacity payment, we have to run to that. But you must remember that's just during, well, the six hours in the summer of onpeak, and then the seven hours of partial peak, for a total of 13 hours during the five weekdays.

On the weekend in the summer that's the time we'll shut down because it's not meeting the costs on marginal cost. And there's no incentive to run.

We have to run to get that capacity payment. In the winter the capacity payment doesn't amount to nearly as much, but with the energy prices higher, over -- on peak time, peak hours, we need to run to do it.

We're losing money in the winter, but we lose less because of the high energy rates.

COMMISSIONER GEESMAN: Other questions for Milton? Thank you, sir.

We're going to take a one-hour lunch break. We've probably got about an hour left when we come back. And I want to encourage everybody to come back.

Let me also remind those of you that cannot come back, and that have written comments, to please submit those no later than the close of business on Monday.

We'll be back at 1:30.

(Whereupon, at 12:30 p.m., the hearing was adjourned, to reconvene at 1:30 p.m., this same day.)

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AFTERNOON SESSION

1:38 p.m.

COMMISSIONER GEESMAN: Commissioner Boyd will join us shortly. We're going to start off with Gregg Morris. Is Gregg in the room? You're first up, Gregg.

MR. MORRIS: Hi, Commissioner Geesman and staff. It's my pleasure to be here today. You've heard a lot about biomass already and I don't want to repeat everything you've heard. But I do want to highlight a few things that I think would be interesting.

And, in fact, I want to start out by saying congratulations to the Committee and the program that you've run in the past. You're responsible, as far as I can tell, for the diversion of some, and I'm talking about now the renewable transition fund program you ran during that four-year period, for the diversion of some 8 million tons of solid waste in the state. That stuff would have been either in a landfill or it would have been open burned. And some 100,000 acres of forests have been treated for fire risk reduction as a result.

And I'm talking about the incremental

amount of biomass that was used above what would have been used had the funds not been there. And I'm not even trying to count whether or not one or more facilities might have shut down. You may have bought even more than I've just mentioned.

The fact is that the program worked very well. We have the documentation to show that the overall capacity factor in the industry went up about 10 percent during the very period in which they were going off the cliff. And you, without the -- program in place, would have seen exactly the opposite happen.

So that's really what's at stake here. What's at stake here is trying to get the most that we can out of the existing biomass industry.

I've done extensive work, you know, and it's been referenced a little bit here today, that the economic value of the environmental benefits of biomass power production are somewhere in the range of 10 cents-plus per kilowatt hour.

And very simply put, those benefits come from using biomass, not from having a facility there to provide capital, but from the actual production and use of biomass, each ton that's used in the biomass plant has found a better environmental fate than it would have had, had it not been used in the biomass plant.

So, that's really what's at stake here. Biomass power production is an inherently expensive form of power. That's a real problem because it's also such a valuable form of power from the environmental perspective. It has these unique characteristics of waste disposal in addition to displacement of fossil fuels.

It costs about 7.5 cents a kilowatt hour to produce biomass power in an existing biomass power plant. And that includes capital operations and fuel.

And right now, the people who are generating, on the basis, for example, the 5.37 cent contracts, are getting about 7.3 cents a kilowatt hour, if you figure in the average 2 cent capacity payment that they're getting.

So, indeed, that's the right range, the minimum that they need to operate. And they are operating. So we can see what's happened as a result, first of your program during the late '90s, and now the fact that they have these contracts at the right rates.

But there's no question that they will

not maximize their output during those periods of time when their marginal costs exceeds the revenues available.

What's at stake here? This year -- well, I did a survey of the biomass industry around April through July. And according to their projections for 2002 at that time, they were going to operate at an unprecedented capacity factor; up about 5 percent from the previous year. And actually up about a half billion kilowatt hours from the previous year.

Now, a couple of new facilities opened during the year, so it's -- but, as far as capacity factor goes, it went up about 5 percent.

Therefore, if the facilities produce what they were projecting sort of figure that they would produce this year, that's about 4 billion kilowatt hours of biomass power; and that's out of a total renewable production, let's say in 2001, was about 23 billion kilowatt hours.

So, we're looking at, you know, a significant fraction, 15 percent of the total renewables coming from biomass.

We have at risk here about let's say a billion kilowatt hours per year of power that the same fleet of producers will not produce if they don't have the right incentives during those offpeak hours.

And what does that mean? Well, again, it means we will have some 2 million tons a year of waste material going to the landfill, going to the open burn piles. We'll have less forestland treated for risk production.

It also has a tremendous implication for our ability to meet the RPS standard. I've been doing some modeling and scenario work in trying to figure out what does it mean for California -- 20 percent RPS 15 years from today.

And the answer is under any set of assumptions it's real tough. For example, if we don't double geothermal production capacity in the state there's no other combination, in my opinion, of renewables that could meet 20 percent.

The same thing is true for wind. If we don't triple wind in the state, we cannot meet the RPS. And, in fact, if we only triple wind and only double geothermal we'll probably not be able to meet the RPS. One of those is going to have to do more than that, and the other at least that. And I'm still filling in with the other renewables.

That's how difficult it will be to make that. And if we lose a quarter of the biomass industry's output today, and we don't see any growth in the biomass industry, and I think it would be unlikely if we're going to see shrinkage in the existing facilities, I think the possibility of new facilities would be nil, that makes it even more difficult.

Everything else will have to be compensated by something like 10 percent more of everything else than we would need already to make it if we had the biomass industry not only continue to produce, but even to grow.

So, what does that mean in terms of money and investment? I figure that right now to meet the RPS standard we would need to put in over the 15-year period something like $16- to $20 billion worth of new renewables, if all existing renewables continue to operate at the level that they're capable of.

If we lose a billion kilowatt hours a year of biomass we will have to invest an extra billion dollars in new renewable capacity to produce that same amount of energy.

That's what's at stake here. It'll be a great strain to get there under the best of circumstances. If we lose one of our keystone renewable supplies, or even part of it, it'll be that much more difficult. We will lose the ability to make the RPS; we'll lose the benefits, the specific waste disposal benefits that biomass provides.

And that's why I urge you to keep biomass in the existing renewable program; to incentivize it during those specific time periods when an incentive is the difference between full production or greatly curtailed production.

We're talking about 30 percent of the annual hours, the offpeak and super offpeak summer periods for the PG&E facilities, for example, which are the majority of them.

The amount that they need is a penny or less per kilowatt hour during those periods. And it will make all the difference in the world. It's a good deal for California.

COMMISSIONER GEESMAN: Do you have a suggestion as to how we do that in a way that is within our administrative competence?

MR. MORRIS: Well, I think you've

demonstrated in the past that that's worked very well. I don't -- I'm not a biomass power plant operator/owner. I don't actually, you know, -- I'm not part of that process. But I assume that it went well, and that it ought to be do-able.

COMMISSIONER GEESMAN: Marwan.

MR. MASRI: Gregg, you were here four years ago or five years ago when we started this, when we were talking about numbers and costs and so on.

MR. MORRIS: Um-hum.

MR. MASRI: There were periods of time, '99, '98, 2000 when SRAC was in the 2 to 3 cents, penny or penny and a half came on top of that, for 4.5 cents. Seems like plants were very happy.

What has changed between then and now? So now we have 7.5 cents cost. And that that level of revenue is no longer sufficient. In fact, need about twice as much. What has changed?

MR. MORRIS: I don't think anything's changed. The 7.5 cents total, but we always had that for those who have the standard offer 4 contracts still, the 2 cent capacity payment. So, let's say 5.5 cents is the target.

And your target used to be 5. And if we

had 3 cent SRAC we were up to 4.5. And 4.5 at that point, which is 6.5, let's say, in the total, is more than enough to cover the operating costs. It is not enough to cover their true capital requirements. But it covers some of them, some of those capital requirements.

And so they limped, but they continued to operate.

MR. MASRI: Now, given the age of these plants, isn't capital requirement pretty much retired by now? Or close to it? Where are those plants?

MR. MORRIS: Well, substantially amortized, it would be another penny, if they were new plants we'd be talking 8.5 cents.

But anyway, you know, there's still investors, there's still loans outstanding, or leases, you know. They're less than they would have been, but by no means are they gone.

MR. MASRI: And this total cost of 7.5 cents is an average, right?

MR. MORRIS: Of course.

MR. MASRI: I mean do you have an idea what the distribution of that is, what percent of the plants? You know, obviously the cogen plants and so on are not, you know, -- lower costs.

What are we talking about here? What percent of the plants really have this type of cost?

(Parties speaking simultaneously.)

MR. MORRIS: Well, you know, it's an average. I've done extensive survey in the plants in California, outside of California, and that it's an average cost.

It's made up of, you know, a capital component of about 2 cents plus --

MR. MASRI: But it's an average cost for an average plant, is my question --

MR. MORRIS: Yes. Yeah, bigger plants have a little economy of scale benefit compared with the smaller ones. But every plant has its own special -- you know, fluidized beds are more expensive to maintain than grate systems, in general. There's always --

MR. MASRI: And maybe this is a question for the industry, but maybe you can address it, given your expertise, Gregg. Is there room to shift production from super offpeak and offpeak to other periods? Are those plants running full bore in those periods, so therefore they cannot

increase production on the onpeak to make up for
the fact that it's not economic offpeak?

MR. MORRIS: Right. Boy, I mean again, every plant has its own physical characteristics that makes it a little bit hard to generalize about that, but generally speaking they are producing at full capability during onpeak hours. So you can figure there's not much unless they have a contractual complication, and a couple of them do, where they have to stay below certain limit for their regulatory requirements.

MR. MASRI: Thank you.

MR. MORRIS: But, in general, not much --

MR. HOFFSIS: Gregg, I have a question, too. There have been periods of time where the short run, where the cost prices are actually rather attractive. We were looking yesterday about a 12-month period where it was averaging around 9 cents or so over that entire period.

So, when times are good like that why wouldn't -- or wouldn't plants take that opportunity to retire their loans, or to -- what happens to that money if you don't --

MR. SPEAKER: We have this bosses that

like to make money.

MR. MORRIS: Well, I could say a few things. I'm not one of those plants, so I can't tell you from personal experience, other than to say that, yes, there was a period; there was also a period of time when, I like to say, that the industry was making unprecedented profits on paper. And they were on the verge of bankruptcy because, in fact, they weren't getting paid.

So a lot of them had a lot of debts to pay, had accumulated during that five-month period where there were no payments. Biomass is a very high cash flow to retention business compared with a lot of other businesses.

And that cash flow out for these operations continues or they shut down. So part of it was that. But, you know, maybe part of it was cashing some profit out, too. I don't know.

And it's important for everybody to understand with biomass, too, and I put it in my written comments, there's a fuel supply curve in this state. Because we're operating at a very high output right now, 4 billion kilowatt hours per year, fuel costs are higher than they were a couple of years ago when we were down more like at

3 billion kilowatt hours a year. The fuel price has gone up from an average of let's say, 25, 26, now to the low 30s.

If we want to maintain maximal output we're going to have to deal with that higher priced fuel because obviously the more fuel you use the more you go up that fuel supply curve. Unfortunately, that's just the way it is. Not only for each plant individually, but for the industry, as a whole.

MR. TUTT: I had a couple of questions, Gregg. Do biomass facilities typically have a 24-hour black-start capability? Can they shut down and come back on within a day?

MR. MORRIS: Well, again, each facility has its own distinct characteristics. I mean one facility just said --

MR. TUTT: I know --

MR. MORRIS: -- they could do it in a half an hour, --

MR. TUTT: Yeah, I saw that.

MR. MORRIS: -- other facilities can hardly cycle at all. So each one, it depends. I don't know that there's a general answer to that question.

MR. TUTT: Okay. Biomass facilities gather a variety of fuels. Is there anytime when they associate a particular fuel with a particular hour of generation? Or, I mean is it typically just brought in and sort of averaged in piles and then burned -- or burned as they see fit?

MR. MORRIS: Yeah, as far as I know, and most of them certainly operate this way. They have typically a month or more storage capacity. Some of them as much as six months storage capacity.

So, yes, you're receiving fuel; you're moving it around; you're managing it; and each one has their own approach to that. They're blending it to some degree. Some get mostly one kind of fuel; some get a broad spectrum. So all those things are true.

But, no, I mean, yeah, I don't think there's a specific time when you say I want urban fuel for this, or --

MR. TUTT: Finally, you mentioned the fuel prices were higher because demand is higher and kilowatt hours being produced are higher. Is there some kind of long-term or medium-term elasticity in the fuel supply market, so that with higher prices more fuel will become available over time to moderate that growth in fuel prices?

MR. MORRIS: I don't know if it moderates the growth in fuel prices, but certainly, as you produce more fuel you're going to get into higher priced fuel.

Now, you know, the fuel producing industry will respond to the market and try and increase its capacity. But if there having to go farther afield to more expensive sources, that's the way it is.

MR. TUTT: Okay, thanks.

COMMISSIONER GEESMAN: Other questions for Gregg? Thank you.

MR. MORRIS: Thank you.

COMMISSIONER GEESMAN: Steve Ponder.

MR. PONDER: Thank you, Commissioners. FPL Energy -- my name is Steve Ponder; I work for FPL Energy. And we own SEGS facilities, 160 megawatts, SEGS 8 and 9, and also about 600 megawatts of wind energy plants in the state.

And what I wanted to address was just the assumption that our company made, unfortunately in part upon my recommendation, about a year ago. And the working assumption was that we were going to get revenue for 2002 from the existing program.

And we did that based upon, in part upon my recommendation, and also kicking around internally, and looking at things we heard at the Legislature. And you've heard of the other three or four sources. I won't go back over them.

But, for whatever reason, that was the working assumption. And I just want to go through the list of impact that that, if we don't receive funds, is going to have upon us.

One way that this assumption was used was during the negotiation with Edison for the 5.37 cents, one of the options that any of the people that were involved in negotiation could have chosen was to have a floating SRAC rate.

And we elected, based upon the assumption that there would be funds available below the tier 2 target, I think, was 3.5 cents, that it would be best for us to take a floating rate. And we did that.

And so if we don't get the funds, then part of those negotiations, which was about a year and a half or so ago, you know, that'll just be revenue lost, from our perspective.

The other situation that came up this last year is we sold several small geothermal plants to an unrelated entity. And the situation is similar to what Kelly Lloyd was talking to with EnXco, although he was -- his company was acquired by somebody.

We had to make a decision on how we were going to treat the funds from the existing account. And so basically they were treated as receivables. And so we actually went on and since the way the revenues are calculated on the geothermal plants, we actually paid royalties based upon having an imputed amount for what that amount of CEC funds would be. So we're going to have to go back and unwind that somehow.

The other issue is with the lenders. We have a number of projects that are project financed. And we do certain financial statements that are certified by a company officer. We book the funds for these projects.

And so now that's going to -- if we do have to go back and change that, that will affect potentially restating the financial statements, debt coverage ratios and probably all kind of fallout that I think Mr. Geesman's probably a lot more aware of than I am, if we go back and have to change some of the assumptions.

And the final point I wanted to make is on future investments. And our company's in a bit of an ironic situation here. We actually have already started construction out of a new program for two projects, an 80 megawatt and a 70 megawatt project called High Winds. And it's out in Solano County. And we just issued a $100 million wind turbine order for that plant. And we're already under construction and we've got a target date of July 1 next year to be up and running.

And so we're planning on and doing future business in the State of California. And, you know, we're doing work all over the western United States. But what we're looking for in any state that we do business is regulatory certainty.

And so some of these assumptions that we were working under, that we basically had sort of -- it seems to be a moving ball within California.

For instance, at the Public Utilities Commission right now, you know, they're supposed to be implementing the procurement rules. And then their first decision comes out and they say that if there's changed circumstances under this contract that you sign up with someone, then they can go back and open up the contract.

So, as you all know, that's just an absolute non starter, whether or not, I mean a lender would not go with it. And then any officer in our company that would take that up to the upper management would probably get shot.

So, we're not going to proceed, you know, in a procurement unless that particular issue is addressed.

We're also transmission constrained. And I know that, Commissioner Geesman, that's one of the items that you're going to straighten out for all of us in the State of California. We appreciate it.

COMMISSIONER GEESMAN: Single handedly.

(Laughter.)

MR. PONDER: But anyway, I think between the ISO and the regulatory bodies, it definitely has not been, and the lack of creditworthy counterparties, I mean significant on this wind project I just talked about in Solano County. It's Pacific Power Marketing is who the counterparty is. And they intend on coming in and taking on some of the credit risk for us, actually, is really what their part of the deal is.

So it was too risky for us, but they will go and somehow swing deals within the State of California.

So, what we want to do, I think the more regulatory certainty we have, then we've got internal hurdle rates that any project has to clear. And if you're comparing California to Texas, you know, yeah, maybe we can do a wind project today for 2.5 or 3 cents in Texas. There might be a 1 cent premium based upon the -- our view of the regulatory certainty or uncertainty in a state like California, or anyplace else that we're working.

So, I think there's a potential cost to the consumers by having assumptions, you know, that we work under, that ends up in some disappointments in other places in the country.

So, I guess I would encourage you to, like everyone else that has said before, is to do a funding for 2002. And then to, you know, look forward also into 2003, see how far we get with the procurement.

I think the working assumption, and I hate to put thoughts or words in your mouth, but I would assume part of what your thinking was in the way this is written on the proposed decision would be that there is going to be a procurement process that worked. There is going to be a need for additional funds in the new side.

I question how quickly that's going to happen. I think benchmark pricing, things that may happen at the PUC, uncertainty of the financial situations of both the -- two of the major utilities in this state put a cloud over this for at least a year or two.

So, anyway, I just hope that the existing program has worked very well, the new program has worked very well, and I think the, as I've said many times up here, I think you've got a great staff that has implemented a lot of this. And so I'd just encourage you to sort of stick to the things that have worked so far, and then, you know, maybe look at this again down the road at some point.

COMMISSIONER GEESMAN: Steve, what would you have done if the legislation hadn't passed, in terms of having booked the anticipated revenues?

MR. PONDER: What would we have done differently?

COMMISSIONER GEESMAN: If 1038 --

MR. PONDER: Had not passed?

COMMISSIONER GEESMAN: -- had not passed.

MR. PONDER: At that point we would have had to do the things I think we're talking about. We'd have to make a public announcement, things like that. I mean unfortunately we're publicly traded, and on a consolidated basis.

And so -- and, Commissioner Geesman, our company is very conservative. We often start building plants before we even make the announcement, which is sort of the opposite end of the spectrum from lots of other people.

And the reason is we've learned that our share value, there's a much bigger hit for the surprises that the market gets, rather than sometime the puffing that you do on the other end.

And so unfortunately we're, you know, -- and I think part of the -- probably take part of the hit internally, but the group I worked with, we based our assumptions based upon our best knowledge at the time a year or so ago.

COMMISSIONER GEESMAN: Fair enough. Other questions for Steve? Thanks very much.

Ralph Sanders.

MR. SANDERS: My name is Ralph Sanders and I'm representing HL Power Company. They are a 30 megawatt net plant located in eastern Lassen County in the rural section of the state.

One of the things that has not been mentioned here today that impacts the rural areas where most of these plants are located, we are very big taxpayers in these counties. And each time we reduce our operating, we reduce our tax revenue to the counties, which, you know, we don't mind not paying taxes, but the county minds not getting those taxes.

(Laughter.)

MR. SANDERS: But one of the other things that was mentioned briefly that all of us are facing to some degree is this generator meter modifier that we were hit with with the ISO.

Our contract is with PG&E. And in our contract we have line loss calculations and line loss generation that we have to provide to PG&E. That did not go away when the ISO decided to take 5 percent of our power.

So even with the contract that we signed for the substitute SRAC, the 5.37, we do not get 5.37. So that's made it more difficult.

We provide good paying jobs for the community plus the support of all the fuel gathering programs in our area. Our area would be really hit hard if they lost the good paying jobs that we provide in our county.

We, of course, do not anticipate shutting the plant down. I would anticipate that we will have to reduce generation without the support of the biomass funding.

I believe that we have presented a good case today. And I would just encourage the Commission to re-look at this and let's move back to the language of our previous program. And try to keep the existing plants operating as much as we can at 100 percent. And we will support that effort, and we will sure try to stay in business to support the state and the RPS program, and the benefits that we provide to the state in emissions reductions and helping to fireproof our forests.

Because once these plants go away, there is no place to put that material. And we've worked very hard to try to get a lot of these programs introduced over the years. And we are trying very hard to hang on to be part of the solution of that problem.

Thank you.

COMMISSIONER GEESMAN: Thank you, Ralph. Are there any questions for Ralph?

MR. MASRI: The GMM adjustment is about what, 10 percent of the 5.37? What is the impact of that?

MR. SANDERS: At our plant it's 5 percent.

MR. MASRI: Five percent.

MR. SANDERS: Some plants are higher. And I think some plants are slightly lower, but our plant is 5 percent.

MR. MASRI: Thank you.

COMMISSIONER GEESMAN: Paul Wood.

MR. WOOD: Commissioner, I don't think there's anything that I can add that hasn't already been said. Coventa Energy would urge the Commission to support the CBEA's position on the investment plan.

COMMISSIONER GEESMAN: Okay, I appreciate that. Eric Wills.

MR. WILLS: Good afternoon,

Commissioners, staff. My name's Eric Wills and I'm President of Sunray Energy. We have 44 megawatts of solar power.

And I'm not going to repeat all the things you've heard today. I have a unique situation I think that's different than most people in the room.

I have a discounted contract; it's not a GMM discount, it's a true discount, off SRAC. I believe that -- imagine this is probably Tony's slide that he's going to present today.

MR. TUTT: He did already.

COMMISSIONER GEESMAN: He already did it.

MR. WILLS: Okay. It's a result of my contract, because those are conversations I've had with him.

So I'd like to explain our position here. We signed the 5.37 amendment. But we didn't sign the 5.37 amendment for the price. We have not seen a discernible impact in our price, I'll go through that, because of the discounts we have.

We signed it because of Edison's representations that they'd pay us on time.

Because of Edison's representation that, hey, if all you guys do this, there's a chance we won't go into bankruptcy. We signed it for the release of claims. We signed this thing for a lot of other reasons.

And in 2001, between 2001 and 2002 our facilities have received between 41 and 60 percent of Edison's avoided cost. For the year 2000 my energy rate was about 3 cents versus SRAC of 7.5 cents. For January through April of 2002 my energy rate was about 2.3 cents; SRAC was over 3 cents.

And then from May through December when the 5.37 cent deal kicked in, my rate 2.7 cents versus 5.37.

So I don't get this big impact. And the problem that I have with the guidebook is that if you sign the 5.37 deal you're out. Well, I don't get 5.37. I've never gotten it, and I don't think it's fair to exclude us.

The other part of this goes into, I think, the intent of SB-1038, and also provisions that are in 1038 and also in the guidelines.

In 1038, section 15383.5(c)(2)(c) it says that the production incentive paid to facilities is based on the difference between the market clearing price for electricity and enrollment target price.

Under this same section market clearing price is determined by the Commission based on the energy price paid, which I emphasize, to nonutility power generators.

It's our view that the intent of this is to base the energy rate based on what's been paid the utility. I don't get the 5.37, I get something less.

On page 3 of the draft guidebook it says the market clearing price for facilities that do not receive payments based on the utility's short run avoided costs and do not have fixed energy price contract is based on the actual energy price received by the facility. Again, the amount that's paid to that facility.

Also on page 3, section 2 of the draft guidebook, for facilities with a fixed price energy contract the value of the market clearing price shall be the monthly average energy price specified in the contract with DWR, CPA and IOU.

So, under that scenario if you had a 4 cent fixed price contract with DWR, or even the

IOU, you'd be eligible under this program. Whereas, when I'm getting 2.5 cents because I signed this 5.37 cent deal, I'm not. And I don't think that's fair.

The other part of this is in SB-1038 there's a provision in there that says the Energy Commission may establish a different incentive rate within the same technology tier to account for discounted contracts.

That language was a direct result of conversations between the solar industry, the Legislator, our political adviser, and he Commission's legislative representative, all of whom were working on 1038. And is a direct result of our contact and discussions that we've had.

And the intent was that we, in fact, may receive a higher rate, but not no rate at that time. And we believe that by using the proxy, the 5.37 cent proxy, that that's discriminatory against us from that perspective, also.

Because when you use the 5.37 cents or a rate that we don't receive, then obviously, you know, we're excluded on a basis of which we don't think is appropriate.

COMMISSIONER GEESMAN: So tell me how is

it that you read the legislation to manifest an intent that you get a higher rate?

MR. WILLS: It says that you may establish a different incentive rate. Doesn't say higher, I agree with you, --

COMMISSIONER GEESMAN: Okay, but why are you suggesting that your intent was, and you think the Legislature's intent was that you get a higher rate?

MR. WILLS: Because those were the discussions that we were having when 1038 was crafted.

COMMISSIONER GEESMAN: And why was it that you were to be entitled to a higher rate?

MR. WILLS: Because of the discounted contract.

COMMISSIONER GEESMAN: Okay, so anybody with a discounted contract?

MR. WILLS: Anybody.

COMMISSIONER GEESMAN: Okay.

MR. WILLS: But, again, I don't think there's a lot of discounted contracts out there. This was an issue that we pushed for over a year in discussions that we had for over a year. And that's the result of those conversations.

Our plant is a peaker. Most of our generation is on in midpeak. We don't have a lot of offpeak or super offpeak, so the additional generation that we could do would be during, in our view, periods when California is short of power.

Any questions or comments?

COMMISSIONER GEESMAN: Staff questions?

MR. HOFFSIS: Yeah, how did that discounted contract come about in the first place, if you can elucidate on that a little bit? And is there something physically different about the cost structure of your plants that are from other similar plants in the same area?

MR. WILLS: There aren't very many similar plants than ours. Our two plants were prototype R&D facilities when they were first built. So they're not the most efficient plants out there. That was the basis to improve the technology.

That discounted contract came into effect back in the early '80s, before standard offer 2s, before standard offer 4s. Edison wanted to have a solar park so they provided us land and some other things. And they had a discounted contract.

A lot has been done since the early '80s. But that was the original basis for a lot of these discounts that are in there.

MR. HOFFSIS: If it preceded the standard offer contracts, it wasn't a discount off the short run avoided costs originally, or --

MR. WILLS: Originally it's off of L.A. Basin, keep oil heat rate, whatever. But that is not the case now. Now it's a discount -- I mean in our contract we have, and again it would not be complex to administer because I know one of your goals is to make simplicity.

In our rate that we get from the utility it is very clear the energy rate that we receive is very easy to calculate in a time period weighted average price. It's a five-second exercise to calculate out of that.

So, right now our contract we have discounts based on gross domestic product, based on natural gas prices, based on the 5.37. There's a lot of different variables in there.

But the net result is the energy price. And so that's what we're talking about. It's the time period weighted average price. And what we actually -- and, again, I want to get back to what we actually receive, the net that we receive.

MR. TUTT: Did your discounting formula change when you signed the 5.37 deal? Was it related to --

MR. WILLS: Yeah, it took out SRAC and they put 5.37; then they discounted that.

COMMISSIONER GEESMAN: Other questions for Eric? Thank you very much.

MR. WILLS: Thank you.

COMMISSIONER GEESMAN: Michael Theroux.

MR. THEROUX: Good afternoon, Commissioners, staff.

I would like to address the relationship of the existing account to what you have in front of you, both in looking at the new accounts and as we move into the RPS.

First of all I would urge you to adhere to what clearly is seen as a clear intent, and to proceed with the payments as such, and not to find yourself in a situation of shifting funds for programs that we do not yet have designed, away from areas that have, in the past, been the structure. So, point one, leave well enough alone, and look at what we have in front of us as a separate issue.

Commissioner Boyd, you have asked repeatedly if there are mechanisms that we might be able to develop that will allow funding of areas that so far we haven't been able to find money for.

I believe that there are, without radically disrupting our projects, at least some of those determinations you do have in front of you still. The point would be this: You can preferentially develop the programs that you have in front of you in, say, the new accounts, the relationship to the RPS, in such a way that they not only do not deplete or damage existing accounts, but in such a way that you may be able to give preference to projects in, for example, the new account that would actually show a benefit to existing facilities.

Last year Arthur D. Little's Company, on contract to the Energy Commission, before they imploded, produced a large document for the PIER program. Stan Blazewicz being the lead on that. And one of the major tenets of that document discussed something called the value network.

A value network as what they saw as the

single most damaging lack within our ability to inability to deploy distributed generation. A value network has a tenet that says you have to pay for what you're doing along the way. And it's more than one piece. There's a whole process, particularly when we work with hard commodities. There is a chain of events from the first generation all the way through to the end use.

In the development of the biomass industry and in particular in the changes that we saw with the PURPA regulations in 1996, and the shifts in the contracts, what happened was for many reasons, but what actually occurred was a collapse; a collapse of the infrastructure that supplied the commodity that had to be relied upon.

And as that distance from source, from the facility, itself, grew, as the funds were dropped away the ability for any one plant to reach out further to those more diverse sources fell away. And the small rural communities in many cases became stranded in their ability to do anything.

As we reduce the distance of huristics to go out, we lost the diversity of the sources. The comments made here today that deal with the difficulty and the increasing costs of the biomass materials at further distances, and the difficulty of the rising cost of feedstocks with a rising power plant, suggest again that part of that puzzle has to do with the loss of diversity of sources.

If we take the templates that are being developed through documents such as the PIER program and ADL's value network, and many of the other -- many, many of the other, the CERTS programs and Berkeley's work on -- Chris Marnay's work on distributed generation, if we look at deployment of networks, and we apply that to the biomass industry, we might be able to show ways, a model, to where we can support the infrastructure but not on the back of the biomass industry.

CBEA has called consistently since day one for a lower, something that would supply that, something that would equate with zero dollar fuel. May I give an analogy?

In the '80s we worked with the wildly fluctuating commodity of used newspaper, trying to recover newspaper. How in the world can you get a half-foot tall stack of newspaper out of 15,000 garages into a pile big enough that Weyerhauser will provide a long-term contract for?

The manner in which that was done, the communities paid for that staged aggregation. And it worked its way forward into a big pile, and a contract was developed. It was horrible. It took forever to get that stabilized. But that commodity futures market finally stabilized.

We are not seeing our communities pay to provide wood chip to the big plants. It's been a decade and nobody's doing that. That money hasn't come forward. But that money perhaps can be generated, or at least a portion of it can be supplied and supported by the programs that you envision now with the new program and the RPS.

We have the ability to establish what I would refer to as utilization hubs in those far-flung areas. And as we look at projects that might use the new funds, and we look at ways to generate contracts toward the RPS might I suggest that you positively weight programs, projects, policies that will help that infrastructure; that will plant self-sustaining mechanisms in that infrastructure.

We can go into detail. I'll be happy to work with you. The U.S. Combined Heat and Power

Association that I am representing today is specifically interested in these models and how they can be applied to agricultural wastes and forest and community wastes. And we believe that there are reasons that we can move forward in those areas and make a self-sustaining infrastructure.

Why does that apply today? First of all, don't gut what you've done. And secondly, as you begin to look at the new programs and the RPS relationships, and the interrelation of the existing to the new, watch very carefully so that you give a positive weighting to programs and projects that benefit the existing structure that you've already helped to establish.

I'll leave my comments at that today. There's so many pieces to this puzzle I would hesitate to try to get further off track on the existing than I already have. But I'd be happy to work with the Commission and the staff to discuss those models and how we might be able to apply them back into this process, as we move forward in our development of the new account.

COMMISSIONER GEESMAN: Any questions for Michael? Thanks very much.

COMMISSIONER BOYD: Thank you, Michael.

COMMISSIONER GEESMAN: Tandy McMannes.

MR. McMANNES: Good afternoon. My name is Tandy McMannes. I'm the Chief Financial Officer for Kramer Junction Company, for the general partner for five solar projects located in the Mojave Desert, each at a 30 megawatt capacity.

These facilities consistently produce in excess of 150 megawatts in total, using solar as their primary fuel during periods when California needs energy the most.

I appreciate the opportunity to come and speak to you regarding the December 2002 draft guidebook.

The draft guidebook starts out stating for its purpose its design is to improve the competitiveness of existing instate renewable generating facilities. So, so far we were on board. We're all on the same goal.

As we were reading through the draft guidebook, though, however under funding eligibility it's stated that a facility is not eligible for funding if it is selling its generation under a high, fixed priced contract.

What that does is that eliminates all

nine of the solar facilities that are in existence, and eliminates the funding to 354 megawatts of solar facilities.

We believe that there must be some confusion, you know, surrounding the signing of these 5.37 contracts. If we can just go back in time, the signing of these contracts was the end result of a very difficult process, both for the new industry and for California.

The factors that were involved in signing those contracts were the energy prices in 2000 and 2001 were significantly higher during periods than the 5.37 cents.

There was severe energy shortages at the time. And at the time, also, the utilities had failed to pay the renewables for five months worth of generation.

So signing those contracts, like Eric pointed out, was more than just the 5.37 cents. It was to get paid for five months worth of past due payments; it was to release the claims; there was a host of reasons why we signed those 5.37 contracts.

Signing those contracts also benefit California as a hedge against future price increases in natural gas. California obviously became dependent upon the use of natural gas and generation from gas which became painfully obvious during the 2000 and 2001 energy crisis.

In our opinion the draft guidebook cannot comply with its very own stated purpose by eliminating all of the SEGS facilities from funding eligibility. We believe that if the draft guidebook were implemented it would actually increase California's dependence on fossil fuel generation.

We also believe it would be harder to achieve the goal of the SB-1078 or a 20 percent renewable in the State of California.

What we concluded was that maintaining the 5.5 cent target price in the 2001 investment plan, and also keeping the 1 cent cap, which is, we believe, consistent with the number of written and oral communications from the CEC, we believe is consistent with the Legislature and consistent with the intent of the Governor.

So I guess without repeating a lot of what's been said before me, I'd like just to briefly, for the record, state what we felt was representations from the CEC, what was the intent of the Legislature, what was the intent of the Governor, and what is going to be the impact to the SEGS if we do implement this program.

Initially we were told that payments would be made under the AB-1890 program until funds ran out, sometime in March or April. So based on that, we did book to our financial statements renewable funds for the first quarter.

We've talked about a number of either letters or notices after that. There was the November 28th notice; the March 8th letter; also most recently, the October 16th notice of staff workshop. All of these either made representations to or regarding the 5.37 contract or payments back to January 1st of 2002.

We also worked closely with the CEC at the California Legislature, all with the intent of implementing a program that we, at the time, understood to be the 2001 investment plan. At no time during our working with you did the CEC or the Legislature or other bodies, did we ever have any reason to doubt that we would receive these funds, unless, of course, the legislation didn't pass.

If the legislation didn't pass, then we

were assured that we would revert back to the balance of the AB-1890 funds until they ran out, which was sometime, like I said, in March or April.

Based on the guidebook now, obviously the prudent thing to do is to not anticipate those funds unless there can be changes to the guidebook. What we will have to do beginning early in 2003 is begin to defer maintenance, because we did expect to receive those funds.

We had booked, like I said, those funds based on reliance of representations by the CEC, and hoping the work we did at the Legislature anticipating that we would receive legislation that was based on the 2001 plan.

We will begin to defer maintenance in 2003, which will have the result of reducing our solar output. We believe, once again impacting the ultimate goal of our 20 percent renewable.

If I could just spend a second just trying to think about, you know, back in time when we were, you know, not only what we felt like representations were from the CEC, but what was the intent of the Legislature.

In passing SB-1038 the California

Legislature stated that, and I don't need to read the whole thing, but basically it was 20 percent of the funds collected shall be used for programs that are designed to improve the competitiveness of existing instate renewable electricity generation.

The Legislature was aware of the 5.37 contracts. And, in fact, even before SB-1038 there was an effort to pass legislation, I believe AB-47, 47X, which actually incorporated the 5.37 cents. So they were aware of the 5.37 cent contracts while they were passing SB-1038.

I believe that they adjusted for that in the legislation, because under the original plan renewables received 45 percent of the total fund. Under the new plan renewables, existing renewables were to receive 20 percent of the total fund.

We believe that if the California Legislature had intended to exclude all solar generation from this plan they would have done so in legislation.

There was another issue brought up about the SB-1078. These aren't part of my notes, but it did bring to mind the question that was brought up earlier, I believe it was by Commissioner Boyd, I can't remember, it was a long time ago.

But, there was a concern that the CEC wants to have adequate funds to actually be able to fund additional generation that would come with the utilities requirements for their additional renewable generation.

I find it odd, though, that the utilities would expect the CEC, which, and it has been brought up more than once, that you're working with a limited amount of funds. There's only so many funds available that you have to deal with. Why they would expect you to subsidize their CPUC renewable process.

The CPUC has come out and said that contracts for renewable generation signed at 5.37 cents or below deemed reasonable. But yet the utilities are going to sign nothing close to the 5.37. In fact, I read in the statements they provided to the CEC from the October meeting, that they're actually encouraging the price cap to be raised above the 1 cent. So, they would go and market, they would go sign renewable generation for a rate that would probably be significantly below the 5.37. And then expect the CEC to fund the difference.

It's ironic to me, in a period of limited funds, and of the CPUC saying that they would deem those contracts reasonable, that the utilities would be looking to you guys to subsidize. And basically, since those funds are funds that we felt were ultimately designated for existing renewables, we're basically funding that effort. We don't think that was the intent of the Legislature.

Regarding representations or the intent of California's Governor. On September 12, 2002, he signed SB-1038, and he issued a press release saying the measure authorizes the Energy Commission to continue the administration of the renewable energy program for five additional years. Also stating that this further protects California's environment and quality of life.

Well, that may be the case for the renewable requirement that will be filled by the utilities, but it certainly isn't the case with existing renewables.

The draft guidebook will not protect California's environment and quality of life while eliminating funds to 354 megawatts of what we consider the most friendly environmental energy in

California. There may be some exceptions taken to that, but --

Basically our recommendation, we want to keep it simple. We think the original system was simple. There was a market price based on the time weighted period, SRAC, which in the case with Edison, is published monthly.

For the period of generation prior to the 5.37 cent contracts we would recommend that we use the what it was at the time, the Malin based SRAC, to compare that against the 5.5 cents.

After the period of the 5.37 contract what we would suggest you use is, in our case there's a bifurcation. Seventy-five percent of our output is priced at 5.37. So that's fixed for the five-year period. It's rather simple to calculate.

Twenty-five percent of our output is priced to a Topock SRAC. And that also is published monthly by utility, which brings to mind another issue that Eric had brought up, is that we're not even receiving 5.37.

So when we look at the contract we look, I mean the draft report, it says that anybody who signed the 5.37 contract is excluded from the plan, it didn't seem appropriate that when they would exclude all the solar projects which don't even receive the whole 5.37 cent.

We also believe that the target price and the cap price should be adjusted annually for inflation. All of our costs go up each year. Your costs go up every year. So we think it would be appropriate to adjust it for that.

We do commend the CEC on its previous programs, where it had successfully adopted programs, more renewable facilities, and look forward to the opportunity to working with you in the future to continue that program.

COMMISSIONER GEESMAN: Tandy, is Kramer Junction a publicly traded company?

MR. McMANNES: No, it's not. It's a private company.

COMMISSIONER GEESMAN: And when you have your financials audited, is that according to GAAP accounting?

MR. McMANNES: Well, the financials -- we haven't had an audit of our financials during the period in question, so --

COMMISSIONER GEESMAN: Okay.

MR. McMANNES: -- clearly if the draft

guidebook gets adopted, we will not have that as an issue.

COMMISSIONER GEESMAN: Fair enough. Other questions for Tandy?

MR. TUTT: Tandy, I guess I'd like to ask you the same question I think I asked earlier, and that is in terms of intent the Legislature developed SB-1038, incorporated the investment plan. And the investment plan specifically says that if the long-term fixed-price contracts that were being considered get signed, we should go back and potentially reevaluate whether or not we should be making payments under the target price market price scheme.

I'm paraphrasing; the exact language is in there. But, doesn't that reflect also the Legislature's and the Governor's intent?

MR. McMANNES: I don't believe it was the intent of the Legislature or the Governor to exclude 100 percent of California's solar generation from the support.

I think that the generation we produce is at a time, most of it is at a time when California is short; they're not long when we're doing our generation.

I think that in your attempt to make it simple you have missed some important distinctions that even though we are, at this point, still recommending the 5.5 cent, we're still recommending the 2001 investment plan, we think that you should recognize that we're not receiving 5.37 cents.

So, if the Legislature said, and those who signed it, they should have made the distinction. Or would defer to you that distinction that like Eric, and like us, and like Harper, that there are some that need to be looked at, that we're not receiving that; that's not the rate we're receiving.

And the value that we add to California is similar, I think, but different than the value that the biomass adds to California. And Commissioner Boyd, you said well, somewhere out there we may be able to find somebody who's willing to give you that value.

I mean the cost of going to war in Iraq, the cost of Kuwait, the cost of fossil fuel is far greater than the $4 we paid for mmBtu for natural gas. But, you know, they don't have to pay their true costs.

Well, what I would suggest is that the Legislature represent suggested or authorize the CEC to be that body who provides that value that no other party's going to provide.

It's like the military. I mean, who's going to sign up to pay taxes for the military? You're not going to do it. You know, the way you got to do it is by the government. The government's the only one who's going to step in and add value where a value should be, or tax where a tax should be in order to pay for the true cost.

As a society we haven't yet begun to tax the full cost of fossil fuel. We're certainly not now giving any value to the other side of the equation.

So I would hope the CEC would say, as a last stop resort, Commissioner Boyd, if there isn't any other option for support for the true value that the tier 1 technologies bring to California, well, you know, unfortunately it's the job that we have to do in the short-run, and with the goal continuing into the future to see if there's not another way we can get value for solar thermal and for biomass.

And we know they're both separate and different, but yet they both do add value to California.

MR. TUTT: Okay. Maybe one more question. Again, I think I asked before of somebody in the biomass industry, back in 2000 you were operating under a 4 cent target price, maybe 3, 3.5 cent SRAC, a 1 cent cap. You were getting revenues, energy revenues of maybe 4, 4.5 cents per kilowatt hour for most of the year.

Are you better off or worse off under the 5.37 contract you're under today?

MR. McMANNES: When you asked that question I thought there was a couple answers that were important, I will try to bring up. At this time, without having everything in front of me, it's hard to know all the variables. There's a lot of numbers out there.

But just as an example, my boss was sitting here a few minutes ago. She had to unfortunately leave and go back to Denver. But before the energy crisis, as an example, you know, our average energy bill for energy purchases from the utility was, you know, between $10- and $15,000 a year.

After the energy crisis, and the first 1 cent rate increase, and then the 3 cent rate increase, we now have about $30,000 a month. So there's a 100 percent increase because of the unfortunate circumstances California found itself in.

We don't really see any relief in the future, given that the utilities are still bankrupt and we still have to use the money that's been collected to pay for, you know, ultimately solving that problem.

Then there is, you know, 9/11. I mean that's the last thing any of us needed. And it was a terrible human tragedy. So if we can get past the human tragedy, we now get in a situation of having to deal with the economics of the situation. I mean insurance costs are just absolutely going out of sight.

So, from the standpoint of costs, we're in a different world. We're in a different world unfortunately due to accidents, whether they're of our own making, like deregulation, or they're of a different making.

There's also expectations. What we do is we invest in solar fields. Our energy comes from the sun, but effectively it's got to be collected in a solar field. So our energy really comes from our employees.

We have 500,000 mirrors out in the middle of the desert, and 50,000 ACE tubes. With an employee base that has to maintain this 30-year fuel source that had to be built on the first day of operation and maintained over the 30 years of the project.

Based on the expectations of receiving the funds that we anticipated, we made certain investments in the solar field. One can't invest more than one has. So, have things changed since that program first came out? Yeah, dramatically.

Is it easy to go through, and go through every single one of them? That would be hard to do, but it's a good question.

COMMISSIONER GEESMAN: Other questions for Tandy? Thank you very much.

MR. McMANNES: Okay, thank you.

COMMISSIONER GEESMAN: Is there anyone else who wishes to address the Committee? Okay, well, then we're going to wrap this up.

As I said before, I would appreciate it if anyone with written comments files those as quickly as possible.

We'll close the docket at the end of the day on Monday. So you do have until Monday to submit written comments. But earlier would be better.

And with that we'll be adjourned. Thank you very much.

(Whereupon, at 3:45 p.m., the hearing was adjourned.)

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CERTIFICATE OF REPORTER

I, PETER PETTY, an Electronic Reporter, do hereby certify that I am a disinterested person herein; that I recorded the foregoing California Energy Commission Hearing; that it was thereafter transcribed into typewriting.

I further certify that I am not of counsel or attorney for any of the parties to said hearing, nor in any way interested in outcome of said hearing.

IN WITNESS WHEREOF, I have hereunto set my hand this 22nd day of December, 2002.