

STATE OF CALIFORNIA

Energy Resources Conservation and Development Commission

In the Matter of:) Docket No. 01-AFC-17
)
Application for Certification for the Inland Empire)
Energy Center)

**APPLICANT’S RESPONSE
TO
COMMITTEE SUPPLEMENTAL BRIEFING ORDER**

Pursuant to the Committee’s Supplemental Briefing Order (“Order”), Inland Empire Energy Center LLC (“Applicant”) hereby responds to the questions posed by that Order. The most important of these questions calls upon the Applicant to obtain a letter from the South Coast Air Quality Management District (“SCAQMD” or “District”) to the Committee, certifying that complete emissions offsets (including RTCs) have been identified pursuant to Public Resources Code § 25523(d)(2) for the Inland Empire Energy Center (“IEEC”). The District has provided the letter requested by the Committee. The District’s letter states: “[T]he District can certify, based on the information provided to the District through IEEC’s application to the District (and related submittals), that to the extent required under SCAQMD regulations, complete emission offsets for the Inland Empire Energy Center have been identified and will be obtained by the applicant within the time required by the District’s rules.

The Applicant respectfully submits that this certification, together with the evidence of record in this proceeding, conclusively demonstrates that the Applicant has fully satisfied the requirements of Public Resources Code § 25523(d)(2).

In further response to the Order, the Applicant hereby responds to the six specific questions posed in the Order. Each question is set forth below, followed by our response.

1. *Explain how the RECLAIM program works, i.e., registering RECLAIM trading credits (RTCs), purchase requirements, timelines (are the RTCs effective for the life of the project?; how long does the process take to complete the purchase process?), and expiration of RECLAIM program.*

A detailed description of the RECLAIM program is set forth in the direct written testimony of Gary Rubenstein (Ex. 2, pp. 5.1-12 to 5.1-13), in the oral testimony of Gary Rubenstein, John Yee and Danny Luong at the evidentiary hearing (9/30 RT 148-153, 158-180), and in the Applicant's Opening Brief.¹ (Applicant's Opening Brief, pp. 19-21)

As we explained in the Applicant's Opening Brief, RECLAIM Trading Credits, or RTCs, are not emission reduction credits. There are several key differences between ERCs and RTCs under SCAQMD regulations:

ERCs are issued in units of pounds per day; RTCs are issued in units of pounds.

ERCs have an indefinite lifetime, and are valid from the date of issuance by the District through the date they are used. Once used, ERCs no longer exist, but the facility which used/surrendered the ERCs has the ability to operate a facility at specified emission rates (related to the quantity of ERCs surrendered) in compliance with District rules for an indefinite period of time. In contrast, RTCs have a lifetime of one year, and are valid only for a specified calendar year and trading cycle. For example, RTCs for 2006 Cycle 1 can be used only in 2006 Cycle 1, and not during any other calendar year or trading cycle.

Once created, the value of an ERC (in terms of emissions) does not decline, except in rare cases where the SCAQMD can (and has) adopted regulations to discount the value of outstanding ERCs for specific regulatory purposes. RTCs were issued by the SCAQMD in a fixed amount, and allocated to specific sources, at the start of the RECLAIM program. The quantity of RTCs allocated by the District declined each year from the start of the RECLAIM program through 2003, and remains constant (unless changed by future regulations) for 2004 and beyond. (Ex. 2, pp. 5.1-12 to 5.1-13)

¹ For the Committee's reference, The RECLAIM regulations are set forth on the SCAQMD website at: <http://www.aqmd.gov/rules/html/tofc20.html>. The RECLAIM program is described by the SCAQMD at: <http://www.aqmd.gov/reclaim/reclaim.html>.

For these reasons, the regulatory requirements and deadlines established by the SCAQMD for new sources are different for ERCs than for RTCs.. The SCAQMD requires that ERCs for new sources be surrendered prior to issuance of the permit to construct for a project. In contrast, the SCAQMD requires that a new source demonstrate that it has sufficient RTCs in its account, prior to the commencement of operation, to cover the expected emissions during the first twelve months of operation. For subsequent years, a new source is required to demonstrate that it has sufficient RTCs in its account prior to the start of each compliance year to cover the expected emissions during that compliance year. (Ex. 2, p. 5.1-12)

Thus, for ERCs, the SCAQMD requires that credits that cover a project's emissions for its entire life be surrendered prior to construction of a new facility. For RTCs, the SCAQMD requires that credits that cover a project's expected emissions for one year be deposited in the facilities account prior to the start of each year. This distinction is important to understand the meaning and applicability of Public Resources Code § 25523(d)(2).

In response to specific issues raised in Question #1, above the Applicant also offers the following comments:

RECLAIM credits are not created by "registration"; in other words RTCs can not be created by individual companies, except under unusual circumstances not relevant to this proceeding. Instead, the SCAQMD (1) determines which facilities will be designated as eligible RECLAIM facilities, (2) maintains the account for each RECLAIM facility and (3) records the RTCs held by each RECLAIM facility. Once a RECLAIM facility has been designated by SCAQMD, the facility may register trades (sales) by an authorized account representative (broker) for an RTC holder. When RTCs are sold, the sale is not completed until the transaction has been recorded by the SCAQMD.

The sale of RTCs from one RECLAIM facility to another is governed by SCAQMD rules, and these rules set forth the requirements for purchasing RTCs. In the context of new source review, RTCs are subject to different purchase requirements for existing facilities (those in existence when the RECLAIM program was created) and for new facilities. For new facilities such as IEEC, RTCs must be in the facility's account prior to the commencement of operation during each RECLAIM year. There are no advance purchase requirements (i.e., for future years) under the RECLAIM program. Although IEEC may choose to acquire credits for future years to satisfy lenders, there is no such requirement under the RECLAIM program.

RECLAIM credits have a defined lifetime of one year. They are defined in terms of a trading year, trading cycle and trading zone. For example, one may own 100,000 pounds of 2004 Cycle 2 RTCs for the Coastal trading zone. These RTCs are valid between July 1, 2004 and Jun 30, 2005, which constitutes Cycle 2 of the 2004 trading year. The RTCs cannot be used during any other period, and they can be used only to reconcile ("offset") emissions which occur during those twelve months. They cannot be extended or modified in any way to apply to a different time period. (There are two zones – Coastal and Inland. In general, Inland RTCs can be used only at Inland facilities; Coastal RTCs can be used at either Inland or Coast facilities.)

The purchase of RTCs can be accomplished within a matter of days, through a broker registered with the SCAQMD, once an agreement has been reached between a seller and buyer.

The RECLAIM program has no expiration date.

2. *In order for Applicant to secure the requisite amount of RECLAIM Trading Credits (RTCs) before plant operation, will the Applicant need to purchase the RTCs from a third party/parties rather than from the District's RECLAIM registry? If so, what guarantees currently exist to ensure that the appropriate RTCs will be available at operation?*

The Applicant cannot purchase RTCs from the District's RECLAIM registry; the registry is merely a listing of the owners of RTCs. The Applicant will have to purchase RTCs from a willing seller.

There are no "guarantees" that the required quantity of RTCs will be available at the time when they will be needed by the Applicant. On the other hand, based on the evidence of record, there is no reason to question that RTC's will be available when they are needed. Since the program began in 1994 there has been a continuous and robust market. Approximately 300 facilities participate in the RECLAIM program. (7/30 RT 174) Moreover, as SCAQMD staff testified, "Since 2001 the market has developed to have futures, options and future purchases, which are certainly recognized as a demonstration of availability." (*Id.* at 173)

Most importantly, no party, including the Staff, has questioned the future availability of RTCs. Mr. Birdsall testified clearly that he believes, for a price, the Applicant *will* be able to go forward and purchase RTCs he sees as required by the district and at the time required by the district prior to the district issuing its permit to operate. (7/30 RT 284). There is simply no evidentiary basis in this record to support any concern regarding the availability of RTCs for this project.

3. *If the project is constructed and RTCs cannot be purchased and other ERCs are not available, and the IEEC cannot obtain a Permit to Operate from the Air District, what will the impacts be to the environment? Will the IEEC be able to operate? If so, under what circumstances?*

IEEC has no plans to begin construction without first acquiring all of the necessary RTCs, and to our knowledge, there is no lender in the United States who would provide

financing to begin construction without all necessary approvals in place, including having the RTCs necessary to operate the plant. Further, in the unlikely event that RTCs are not available for purchase (which has never occurred during the entire life of the RECLAIM program), IEEC would be unable to commence operation. Consequently, there would be no adverse impacts to the environment. (Construction impacts for IEEC are fully mitigated by SCAQMD and CEC requirements, and do not rely upon RTCs.) There are no circumstances under which IEEC would be able to operate under the conditions hypothesized in the question, and, therefore, there could be no impacts on the environment from a facility that does not operate.

4. *Does Staff need to have the RTCs identified more specifically in order to complete its CEQA analysis and if so, why?*

The answer to this question is clearly no. During the evidentiary hearings the Staff expressly testified that it does not need to have the RTCs specifically identified in order to complete its analysis.

MR. ELLISON: Well, assuming that we're talking about authentic RTC's that the district recognizes as valid, would the selection of particular RTC's change staff's analysis or its conditions in any way?

MR. BIRDSALL: I don't believe so, no.

MR. ELLISON: Now that's not true for ERC's, correct?

MR. BIRDSALL: That's correct, it is not true for ERC's.

MR. ELLISON: And isn't it true that one of the reasons you need to identify ERC's is because it does potentially change the staff's analysis depending upon which ones are identified?

MR. BIRDSALL: I can't speculate why the Warren-Alquist Act requires identification of offsets, but indeed when staff analyzes an Applicant's offset package we take into consideration where the offset comes from, the quality of the offset, and if it is an ERC we'd look at it for the environmental constraints. Meaning is it located an approximal distance from the source, has the EPA blessed the authenticity of the ERC, and so on.

MR. ELLISON: But with respect to RTC's that's not the case?

MR. BIRDSALL: With respect to the RTC's, no, we don't have geographic specific constraints, at least for this particular project we don't. And we don't question the authenticity of the credit or whether or not it's surplus, for example." (7/30 RT 279-280)

5. *Has the Energy Commission certified any other power plant projects in which the air emission offset package was not completely identified or in which offsets were not secured prior to certification? Please list projects and be specific about the circumstances of each case. If the offsets were not secured, but identified, please explain how those offsets were identified.*

According to the evidence of record in this proceeding, the Commission has licensed two other power plant projects (Magnolia and Malburg) within SCAQMD's jurisdiction since Public Resources Code § 25523(d)(2) was amended. A third project within the District (El Segundo) is currently pending before the Commission. Unfortunately, the extent to which these other projects identified or secured offsets prior to certification is not clear from the record of those proceedings.

Staff originally testified that the El Segundo project had obtained only 90% of its first year offsets. (Ex 68, p. 5; 7/30 RT 239) However, in its Reply Brief, Staff attempted to retract this testimony and offered new evidence and argument to impeach its own witness.² (Staff Reply Brief, p.2). Similarly, while the Staff's written testimony asserted that "Staff has recently approved other projects that held or had agreements to acquire very close to 100 percent of the first-year RTCs" (Ex. 68, p. 5), the Staff's witness was not able to testify as to nature of these agreements. (7/30 RT 238).

² The Staff's Reply Brief attributes its prior testimony regarding El Segundo to "confusion" and seeks to cure the confusion by asking the Committee to take official notice of the entire record in the El Segundo case. *Staff Reply Brief, p. 2) The Applicant objects to the introduction of new testimony and substantial new evidence through a Reply Brief.

The Applicant believes that a detailed examination of the specific circumstances is neither necessary nor prudent. Even if it were true that the project owners in other cases happened to hold most or all of first year RTCs prior to certification, it is important to note that these RTCs would be held or acquired as the result of a business judgment by the project owners and not because of a requirement imposed by the Commission as a condition of certification.³ The record of these proceedings does not readily reveal whether the RTCs were held because the project owner happened to hold the credits in their account, were acquired because the Staff threatened to withhold their recommendation of approval of the project or were acquired for some other reason. In any event, this is the first case in which the Commission has been called upon to decide whether a project owner should be required, as a matter of law, to obtain RTCS prior to certification of the application. As described in detail in our opening briefs, the history of Section 25523(d) makes clear that the Legislature specifically amended this law (with the Commission's agreement) to harmonize Commission policy with the District rules with regard to the timing of offset acquisition. The staff's position here flies in the face of this amendment and would put Commission policy once again in conflict with the District rules. Moreover, as pointed out below, it would create such conflict without any public interest justification for doing so.

If the Committee is inclined to examine the precedent of recent proceedings⁴, the Applicant respectfully submits that the most relevant point of comparison between the instant

³ The Staff's witness agreed that an Applicant should not be required to do more than is necessary to meet a legal standard, merely because other Applicants may have voluntarily chosen to do more than is required to meet the standard. (7/30 RT 286-287)

⁴ Question 5, insofar as it requests information regarding the specific circumstances of other recent proceedings, is somewhat surprising, given the Committee's guidance at the start of the proceeding: "We would like to remind the parties that the findings made in this case will be based wholly on the written and oral evidence presented during these proceedings. We discourage discussion of agreements, positions advanced, or decisions made in other recent proceedings. None of these are precedential or binding in these proceedings." (7/30 RT 7-8)

case and these other projects is the Condition of Certification relating to RTCs. In the instant case, Condition AQ-27 as proposed by Staff (and which is fully agreed to by the Applicant) provides as follows:

AQ-27 This equipment shall not be operated unless the operator demonstrates to the Executive Officer that the facility holds sufficient RTCs to offset the prorated annual emissions increase for the first compliance year of operation. In addition, this equipment shall not be operated unless the operator demonstrates to the Executive Officer that, at the commencement of each compliance year after the first compliance year of operation, the facility holds sufficient RTCs in an amount equal to the annual emissions increase.

This Condition, which was similarly adopted in the Magnolia and Malburg cases and is proposed in the El Segundo case, makes the issue of prior identification essentially a moot question. As long as there is a requirement in place that the facility cannot be operated unless the operator first demonstrates that the facility holds sufficient RTCs, the public interest is fully protected. While the Staff urges that RTCs be secured prior to certification by the Commission, the Staff has failed to explain, much less prove, how acquisition prior to certification serves to advance the public interest any better than Condition AQ-27. Is the environment or public health *improved* by requiring acquisition of RTC prior to certification, rather than prior to operation? Clearly not. Therefore, because the public interest is fully satisfied by AQ-27 and because AQ-27 guarantees that the project will not operate without the operator holding all necessary RTCs, it is not necessary for the Commission to impose the additional, superfluous condition that these RTCs be secured prior to certification.

6. *Discuss the relevance of cost in determining whether the project complies with applicable law, i.e., CEQA.*

In the context of the RECLAIM program, the identification of particular RTCs as well as the cost of securing RTCs is not relevant to the determinations that the Commission must make under CEQA. (Please see our response to Question #3, above.)

However, as a general rule, in determining whether a project complies with CEQA, economic or cost factors are among the many factors that may be considered by a public agency.

“CEQA establishes a duty for public agencies to avoid or minimize environmental damage where feasible.” (California Code of Regulations, Title 14, Section 15021(1)). “A public agency should not approve a project as proposed if there are feasible alternatives or mitigation measures available that would substantially lessen any significant effects that the project would have on the environment.” (*Id.*). “In deciding whether changes in a project are feasible, an agency may consider specific economic, environmental, legal, social, and technological factors.” (*Id.*). Thus, “CEQA recognizes that in determining whether and how a project should be approved, a public agency has an obligation to balance a variety of public objectives, including economic, environmental, and social factors and in particular the goal of providing a decent home and satisfying living environment for every Californian.” (*Id.*).

It is important to note that while cost is certainly a factor to be considered by a public agency in determining whether a particular mitigation measure is feasible, under CEQA such mitigation is imposed as a precondition of undertaking the project. The mitigation is not imposed as a precondition of receiving the license. For example, a public agency may identify the best available control technology to be utilized if the project is constructed, but a decision may not require that this mitigation measure actually be purchased prior to issuance of the license. Similarly, the Commission may proscribe the quantity of RTCs to be acquired if the project is constructed, but CEQA certainly does not authorize the Commission to require that the offsets (or RTCs) be purchased prior to issuance of the license.

Conclusion

In conclusion, the District has certified, as requested by the Committee, "that to the extent required under SCAQMD regulations, complete emission offsets for the Inland Empire Energy Center have been identified and will be obtained by the applicant within the time required by the District's rules." Condition AQ-27 will ensure that that the facility holds sufficient RTCs to offset the annual emissions increase for the first compliance year and each subsequent year of operation. No party disputes that these RTCs will be available. And no party has offered any evidence to suggest that the public interest would be better served or that the environment would be better protected by requiring RTCs to be obtained prior to certification.

Respectfully submitted,

Dated: October 24, 2003

ELLISON, SCHNEIDER & HARRIS L.L.P.

By  _____

Greggory L. Wheatland, Esq.
Christopher T. Ellison, Esq.
Attorneys for Inland Empire Energy Center LLC

STATE OF CALIFORNIA

Energy Resources Conservation
and Development Commission

In the Matter of:

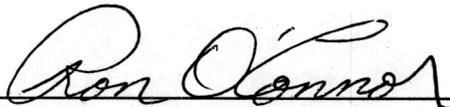
Application for Certification for the
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PROOF OF SERVICE

I, Ron O'Connor, declare that on October 24, 2003, I deposited copies of the attached *Applicant's Response to Committee Supplemental Briefing Order* in the United States mail in Sacramento, California, with first-class postage thereon fully prepaid and addressed to all parties on the attached service list.

I declare under the penalty of perjury that the foregoing is true and correct.



Ron O'Connor

SERVICE LIST
01-AFC-17

Greg Lamberg
IEEC Project Manager
4160 Dublin Blvd.
Dublin, CA 94568-3139

Michael Hatfield
Calpine Corporation
4160 Dublin Blvd.
Dublin, CA 94568-3139

Jenifer Morris
NJ Resources, LLC
555 East Ocean Blvd., #224
Long Beach, CA 90802

Jane Lockhardt, Esq.
Ann Trowbridge, Esq.
Downey, Brand, Seymour & Rower
555 Capitol Mall, 10th Floor
Sacramento, CA 95814-4686

Electricity Oversight Board
770 L Street, Suite 1250
Sacramento, CA 95814

Paul Clanon, Director
Energy Division
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Rachel Johnson
Assmblyman Longville
201 N. E Street, Suite 205
San Bernardino, CA 92401

CURE

c/o Marc D. Joseph, Esq.
Mark R. Wolfe, Esq.
Adams Broadwell Joseph & Cardozo
651 Gateway Blvd., Suite 900
So. San Francisco, CA 94080

Romoland School District
c/o Mark Luesebrink, Esq.
Jeffrey M. Oderman, Esq.
Rutan & Tucker Attorneys at Law
611 Anton Blvd., 14th Fl.
Costa Mesa, CA 92626

Eastern Municipal Water District
Attn: Dick Heil
P.O. Box 8300
Perris, CA 92572-8300

Independent System Operator
Jeffery Miller
151 Blue Ravine Road
Folsom, CA 95630