

California Consumer Power And Conservation Financing Authority

LEGISLATIVE ANALYST'S OFFICE

Presented To:
Joint Legislative Audit Committee
Informational Hearing





The Analysis Requested of the LAO

- Provide a basic fiscal and policy analysis of SB 6x (Burton).
- Identify and describe the measure's key provisions.
- Discuss the stated mission and objectives of the California Consumer Power and Conservation Financing Authority (CPA) established by the bill.
- Summarize the CPA's activities thus far and discuss whether they are consistent with the measure's intent.
- Identify any significant policy issues associated with the CPA that may merit review or attention by the Legislature.



Principal Findings

- The CPA's activities thus far have been:
 - Generally consistent with SB 6x's basic intent.
 - Relatively limited, in part, reflecting its short history.
- The CPA's focus has recently changed significantly.
 - Until recently, its focus was on acquiring peaker-type generation capacity to provide an adequate electricity reserve margin for next summer.
 - Presently, it's focus has shifted to demand-side electricity solutions, such as increased conservation and interruptible programs.
- Regarding the CPA's required Energy Resource Investment Plan (ERIP):
 - It is still in its formative stage.
 - The CPA has recently begun to accelerate its efforts to meet its February 15 statutory deadline for the plan.
- Key issues exist relating to SB 6x that may merit further review by the Legislature in such areas as:
 - Governance.
 - Finances of the CPA and its loan programs.
 - The CPA's power of eminent domain.
 - The financing of electricity transmission investments.
 - Energy-related planning.
 - Structure of the state's energy-related entities.



Factors Leading Up to SB 6x and the CPA

- California deregulated its electricity generation market in 1996 with the enactment of AB 1890.
- As early as summer 2000, electricity supplies had tightened, prices were at historically high levels, and power blackouts occurred in some geographic areas.
- Things worsened this past winter.
 - Natural gas prices skyrocketed.
 - Electricity prices stayed high despite the low winter demand.
 - The state's large investor-owned utilities (IOUs) developed severe credit problems.
 - More blackouts occurred.
 - The state began purchasing electricity at a very high cost for the IOUs.
- The CPA was created in this environment in an effort to provide stability and rationality to California's electricity market.



Basic Structure and Characteristics of the CPA

- ☑ **Composition.** The CPA has a five-member governing board.
 - State Treasurer plus four appointees of the Governor.
 - For appointees, staggered four-year terms and Senate confirmation.
- ☑ **Reporting and Review.** The CPA is required to report on activities to Governor and Legislature due each January 1. In addition:
 - Operating budget subject to review and appropriation in annual state budget act.
 - Evaluation by Bureau of State Audits by January 1, 2005, regarding the CPA's effectiveness and the need for continuation after January 1, 2007.
- ☑ **Initial Funding.** The CPA received a \$10 million General Fund loan for start-up costs; it is to be self-funded thereafter from program-related activities.
- ☑ **Operational Procedures.** The CPA is:
 - Permitted to engage in sole-source contracts and is not subject to the state's normal competitive bidding process.
 - Not subject to otherwise applicable code provisions regarding contracted compensation for its chief executive officer and other contract personnel.



Responsibilities, Powers, and Tools of the CPA



Responsibilities. The CPA is charged with:

- Assuring a reliable supply of power at "just and reasonable" rates.
- Planning for a prudent energy reserve.
- Encouraging energy efficiency, conservation, and use of renewable resources.
- Developing a California ERIP.



Powers. To meet these goals, the CPA is authorized to:

- Purchase, lease, or build new power plants to supplement private and public power supplies.
- Finance energy conservation and renewable energy projects for businesses and consumers.
- Finance natural gas transportation and storage projects recommended by the California Public Utilities Commission (CPUC), as the retrofit of old and inefficient power plants.



Tools. To effectively exercise these powers and meet its responsibilities, the CPA has been granted:

- \$5 billion in revenue bonding authority.
- Eminent domain powers.



The CPA's Revenue Bonding Authority

- \$5 billion in revenue bonds is available for energy investments:
 - \$4 billion for power generating facilities.
 - \$1 billion for energy conservation purposes.
 - Can result in below-market loan rates if tax exempt.
- The bonds must be self supported from the projects being financed, such as from:
 - Sales of electricity from energy generating projects.
 - Savings in electricity bills resulting from energy conservation projects.
- For the bonds to be marketable, a secure and sufficient revenue stream is needed. For example:
 - Electricity generating facilities must have power sales contracts.
 - Generation and conservation projects must produce sufficient benefits to both pay basic debt service and the CPA's expenses.



Implementation Activities to Date

The statute that created the CPA became operative on August 13, 2001. Since then, the following has occurred:

- The CPA's board of directors, chief executive officer, and chief counsel have been appointed, six public meetings have been held, and approximately \$1.5 million in loaned funds have been allocated for the CPA's initial operations.
- A proposal has been submitted for the expenditure of the remaining \$8.5 million of the \$10 million initial loan.
- A request for qualifications (RFQ) for a financial advisor has been issued.
- The CPA received proposals and signed nonbinding letters of intent (LOIs) to provide financing for roughly 5,500 megawatts (MW) of new peaker and renewable electricity generation.
- A two-day public forum and a variety of interagency meetings have been held with the California Energy Commission, Independent System Operator, and the CPUC in conjunction with development of the ERIP.
- A detailed protocol for selecting and handling generation proposals has been adopted.



Early Challenges Encountered

- ☑ **Mid-Course Change Involving Investment Objectives.** The CPA's staff recently made a fundamental switch in its investment focus.
 - A prime initial focus was on peakers—31 LOIs for 3,200 MW.
 - These have been suspended.
 - Renewable generation projects also have been considered—48 LOIs for 2,300 MW.
 - Current emphasis is on demand-side management, including conservation.

- ☑ **Progress on Investment Plan.** The ERIP is still in early development.
 - Broad draft outline exists.
 - Proposed topics have been identified.
 - A two-day public work session was recently held to discuss various plan elements and review the potential roles of both state agencies and private parties.
 - The CPA Board approved the expenditure of up to \$400,000 for out-source contracts to provide data and analyses for the plan.
 - Detail and specifics have yet to come.

- ☑ **Contracting Issues.** The media has noted potential conflicts of interest involving Navigant Consulting, Inc., a major CPA service provider.
 - This provider assisted the CPA in evaluating applications for generation projects to be funded by the CPA.
 - Some of these applicants also were clients of Navigant.
 - The CPA has since terminated its association with Navigant.



Legislative Considerations



Governance. Is the Legislature adequately represented, given:

- Its absence on the CPA's board?
- The CPA's key mission in dealing with issues involving California's current energy situation and energy future?
- The Legislature's lack of role in the ERIP?



Financial Issues. The CPA's source of financing for its operations and programs is revenue bonds.

- Are these bonds feasible for the projects the CPA is currently contemplating? (Some unresolved concerns have been raised in this area.)
- If not, should alternative funding for the CPA and its projects be considered?



Eminent Domain. Some of the language involving eminent domain in SB 6x may merit review to ensure that the CPA's powers can be effectively used, including:

- Designation of the governing board for eminent domain purposes.
- Providing for the up-front payment required in eminent domain proceedings.
- The "more necessary use" requirement.
- Jurisdiction for establishing property valuation.



Legislative Considerations

Continued

- Transmission Facilities.** The CPA has no current authority to finance transmission line improvements. Should this be reevaluated, given:

 - The current financial position of the IOUs, including the Pacific Gas and Electric Company bankruptcy proceeding?
 - The significant need for certain transmission improvements, including Path 15 which links Northern and Southern California?
 - The current federal proposal in this area?
- Energy Resource Investment Plan.** What should be the specific elements in the ERIP that is being developed? For example:

 - What should be the role of supply-side versus demand-side strategies in meeting the state's electricity needs?
 - What should the state's reserve margin be?
 - What should be the role of renewable energy?
 - What transmission improvements are needed?
- Reorganization of State Energy-Related Agencies.** California has a number of different energy-related entities.

 - Potential exists for inefficiencies, unnecessary duplication, and conflicts of responsibility among these entities.
 - What steps are needed to avoid such problems, such as changing or consolidating their roles, functions, and duties?