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County of Santa Cruz

DEPARTMENT OF PUBLIC WORKS

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AGENDA: FEBRUARY 9, 1999

January 28, 1999

SANTA CRUZ COUNTY BOARD OF SUPERVISORS

701 Ocean Street
Santa Cruz, California 95060

SUBJECT: BUENA VISTA LANDFILL GAS POWER PROJECT

Members of the Board:

On December 15, 1998, Public Works provided your Board with a status report on the Buena Vista Landfill Gas Power Project, which included copies of three of the draft agreements necessary to implement this proposed project. The primary purpose of this report was to receive direction from your Board regarding our department's proposal to develop this project as a joint public/private venture. Your Board approved, in concept, the development of this project as a public/private joint venture. Under this development plan much of the risk would be allocated to the private operator of the facility, Brown, Vence and Associates (BVA) Lfg, Corporation with the County receiving offsetting benefits in the form of risk avoidance, financial guarantee for debt and equity repayment, avoided costs for landfill gas collection field operations, and a small financial return on the project. This is a beneficial alternative project structure for the County in light of the financial guarantees and the allocation of most of the operational risk to BVA Lfg, Corporation. Your Board provided additional direction to consider structuring the agreements with BVA Lfg, Corporation for a five-year period, instead of the proposed ten-year period, with the County option of taking control of the project at year five or extending the term with BVA Lfg, Corporation, for an added five-year period.

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Staff from Public Works, County Counsel, and the County Administrative Office met with representatives from BVA Lfg, Corporation, to discuss the alternative contract structuring proposed by your Board, and all concurred that this revision was feasible. BVA Lfg, Corporation further proposed to structure the agreements in such a way to allow the County to take over operations at any time during the initial ten-year period if the County determines the market and operating conditions would be to our benefit. This will allow the County to weigh the operational and market conditions on an annual basis and assume project control if and when conditions warrant. The Electric Generation Facility Lease agreement that will define this revised condition will be returned to your Board at a later date along with the other final agreements as discussed below.

As we have outlined in previous correspondence, one of the three primary sources of operating revenue for projects of this type is the Federal Section 29 tax credits. In order to improve the negotiating position of the County and BVA Lfg, Corporation with regards to placement of the final tax credit investment, we are recommending execution of the three attached agreements as a first step. These agreements are generically referred to as "GASCO" agreements and pertain specifically to the fuels production component of the project. At a later date we will return with the "GENCO" agreements which are specific to the electrical generation component end of the project. Execution of the GASCO agreements will provide the County and BVA Lfg, Corporation with a stronger negotiating position with which to finalize the Section 29 Tax Credit investment and will further reduce County risk by better defining the financial aspects of the project prior to commitment of capital (step 2 GENCO agreements). We will be able to take these executed gas production agreements to the investor to show a strong commitment to development of this project, which will likely result in a greater investment return to the project.

The three attached GASCO agreements are as follows:

- Landfill Gas Field Facilities Lease Agreement (Revenue) - This agreement assigns the rights for all landfill gas and the physical collection system to BVA Lfg, Corporation for the purpose of gas production to serve the landfill gas power project and any other beneficial use projects created during the term of the agreement that may be subject to receiving Section 29 tax credits. The value of this lease agreement to the County is \$30,000 per year.
- Landfill Gas Field Facilities Operation and Maintenance Agreement (Revenue) - This agreement provides for the County's maintenance and operation of the landfill gas collection system including the duties, obligations and conditions for delivery of landfill gas to the power project. Under this agreement the County will maintain its regulatory compliance responsibilities regarding operation of the existing and expanded landfill gas collection system and its by-products, while also guarantying delivery of landfill gas to the leased power project in both defined volume and quality. The value of this operations and maintenance agreement to the County is \$35,000 per year and may increase if collection system operations and maintenance are expanded to accommodate other beneficial use projects for excess landfill gas developed during the term of the agreement.

- Landfill Gas Purchase Agreement (Expense) - This agreement provides for the County purchase of all collected landfill gas from BVA Lfg, Corporation for use in the County-owned landfill gas power project and any other beneficial use projects created during the term of the agreement. The cost of this agreement to the County is estimated at \$60,000 per year, but may increase if other beneficial use projects for excess landfill gas are developed during the term of the agreement.

As you can see, the revenue and expense values of these three agreements are revenue neutral at this juncture in project development. You will find clauses within each of these agreements that render them null and void after six months if we are not successful in securing or negotiating the remaining GENCO agreements and related tax credit investment arrangements. Execution of these agreements at this time will not commit the County to this project nor expose the County to any unnecessary risks. However, execution of these agreements as the first step toward project completion will improve our negotiating position for the tax credit investment as stated above. Please note that the financial revenue or expense for each of these agreements may be further adjusted in conjunction with the GENCO agreement approvals to reflect negotiated changes in the overall project cash flow. In order to execute these three agreements, your Board will also have to approve the attached resolution accepting unanticipated revenue for the two revenue agreements with BVA Lfg, Corporation.

Attached you will also find a flow chart and summary description of all the various contractual agreements, both GASCO and GENCO, that will require County approval prior to commencing construction. Staff will also be providing a brief presentation on the project structure outlined in this attachment.

A new issue has also surfaced regarding the issuance of a Permit to construct from the Monterey Bay Unified Air Pollution Control District (Air District). Staff was notified last month that this project would require pollution credit offsets for Oxides of Nitrogen. The Air District maintains a "Community Bank" of pollution credits for use in Public Service Projects such as ours. This Bank provides Public Service Projects with the necessary pollution credits (tons/year) at no cost. The alternative would be to purchase these credits from their "regular" credit bank at market rates, which are currently at \$8,000 to \$10,000 per credit. However, we were recently informed that a never used policy exists that limits the amount of Community Bank credits we can receive in any one year to 50 percent of the existing pollution credits available in the Bank. The Community Bank has 76 credits available and our project will require 74. Air District staff strongly supports our project and has recommended to the Air District Board that the old 50 percent policy be set aside for our project to receive the full credit allocation needed. Air District staffs recommendation was based on the fact that in the 15-year history of the Community Bank, there have only been two permanent withdrawals and both were for a landfill gas-to-electricity project at the Marina Landfill in Monterey County. In conjunction with this recommendation, Air District staff has also proposed options for refunding the bank or providing exemptions for Public Service Projects to allow future expansions and new public service projects to benefit from this program.

Status of the Community Bank and the staff recommendation regarding our Landfill Gas Power Project was considered at the January 20, 1999, Air District Board meeting. At that meeting the Air District Board members directed staff to provide the County with a 50 percent credit allocation from the Community Bank, per the existing policy, and directed staff to return at the February meeting with a detailed report on the impacts and implications of fully funding the County's project, refunding the Community Bank and provision of exemptions for Public Service Projects. We expect to have this issue fully resolved when we return to your Board with the GENCO agreements next month and will provide a complete discussion of the impacts regarding the Air District's final decision on this matter. In light of the extreme importance of the Air District's decision next month regarding our project and the future of the community Bank Program, we are recommending your Board submit a letter of support for our proposed project to the Air District Board. Public Works staff will work in conjunction with the Board Chairperson to draft a letter of support on behalf of your Board.

In summary, the proposed public/private joint venture arrangement for this project will have many benefits for the County and is structured to allow the County to take full operational and financial control of the project at any point during the ten-year term of these agreements. While the structure of these many agreements appears to be complex, they are necessary in order to comply with tax code regulations regarding Section 29 tax credits. This process is a legally approved and tested investment strategy typical for all types of public and private renewable energy projects. The actions being recommended for your Board pose minimal risk to the County, have no financial impacts, and will place the County and BVA Lfg, Corporation in a better position to negotiate the best possible tax credit investment arrangement.

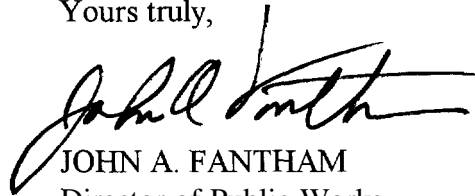
As a final note, we are pleased to inform your Board that the California Energy Commission (CEC) has approved our grant funding for this project in the amount of \$767,600. The funding agreement between the County and the CEC is attached for your consideration and approval. The CEC funding is based upon energy production and will not begin to accrue until after the proposed facility startup late this year.

It is therefore recommended that the Board of Supervisors take the following action:

1. Accept this status report on the Buena Vista Landfill Gas Power Project,
2. Adopt the attached resolution accepting unanticipated revenue in the amount of \$65,000.00.
3. Approve the attached revenue agreement with Brown, Vence and Associates Lfg, Corporation for lease of the Gas Field Facilities at the Buena Vista Landfill in the amount of \$30,000 per year and authorize the Director of Public Works to sign the agreement on behalf of the County.
4. Approve the attached revenue agreement with Brown, Vence and Associates Lfg, Corporation for operation and maintenance of the leased Gas Field Facilities at the Buena Vista Landfill in the amount of \$35,000 per year and authorize the Director of Public Works to sign the agreement on behalf of the County.

5. Approve the attached agreement with Brown, Vence and Associates Lfg, Corporation for purchase of gas produced from the Buena Vista Landfill for use in the future landfill gas power facility and other beneficial projects for an amount not-to-exceed \$60,000 and authorize the Director of Public Works to sign the agreement on behalf of the County.
6. Approve the attached funding agreement between the County and California Energy Commission in the amount of \$767,600 and authorize the Director of Public Works to sign four copies of the agreement on behalf of the County.
7. Direct Public Works to return on or before March 23, 1999, with all remaining agreements necessary to initiate construction of the Buena Vista Landfill Gas Power Project.
8. Direct Public Works, in conjunction with the Chairperson of the Board, to draft a letter to the Monterey Bay Unified Air Pollution Control District on behalf of the Board of Supervisors supporting our proposed Landfill Gas Power Project and requesting full allocation of Community Bank pollution credits as proposed by District staff.

Yours truly,

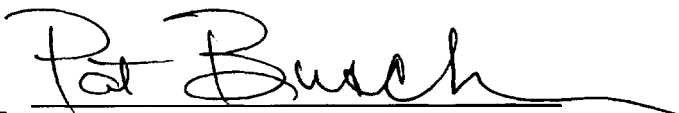


JOHN A. FANTHAM
Director of Public Works

RPM:mg

Attachments

RECOMMENDED FOR APPROVAL:

Acting 
County Administrative Officer

Copy to: Public Works
General Services (w/a)
Auditor-Controller
Brown, Vence and Associates Lfg, Corporation (w/a)