

**BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF CALIFORNIA**

Order Instituting Rulemaking to Promote Policy and Program Coordination and Integration in Electric Utility Resource Planning

Rulemaking 04-04-003  
(Filed April 1, 2004)

Order Instituting Rulemaking to Promote Consistency in Methodology and Input Assumptions in Commission Applications of Short-Run and Long-Run Avoided Costs, Including Pricing for Qualifying Facilities

Rulemaking 04-04-025  
(Filed April 22, 2004)

Application of Southern California Edison Company (U 338-E) for Applying the Market Index Formula and As-Available Capacity Prices Adopted in D.07-09-040 to Calculate Short-Run Avoided Cost for Payments to Qualifying Facilities Beginning July 2003 and Associated Relief

Application 08-11-001  
(Filed November 4, 2008)

Order Instituting Rulemaking into Implementation of Public Utilities Code Section 390

Rulemaking 99-11-022  
(Filed November 18, 1999)

Order Instituting Rulemaking to Integrate Procurement Policies and Consider Long-Term Procurement Plans

Rulemaking 06-02-013  
(Filed February 16, 2006)

**JOINT MOTION  
FOR APPROVAL OF QUALIFYING FACILITY AND  
COMBINED HEAT AND POWER PROGRAM SETTLEMENT AGREEMENT**

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## TABLE OF CONTENTS

	<b>Page</b>
I. FACTUAL AND PROCEDURAL BACKGROUND.....	4
A. PURPA and The Commission’s QF Program.....	4
B. State Policy Favoring CHP .....	6
C. CARB’s Climate Change Scoping Plan.....	6
D. Description Of the Settlement Process .....	7
II. SUMMARY OF THE PROPOSED SETTLEMENT AGREEMENT .....	8
A. Section 1 – Goals and Objectives .....	8
B. Section 2 – Settlement Periods .....	8
C. Section 3 – Transition PPA.....	9
D. Section 4 – CHP Procurement Process .....	9
E. Section 5 – MW Targets .....	10
F. Section 6 – GHG Emissions Reduction Targets.....	11
G. Section 7 – GHG Emission Accounting Methodology.....	13
H. Section 8 – Commission Jurisdictional Entities’ Reporting Requirements .....	13
I. Section 9 – CHP Auditor .....	14
J. Section 10 – SRAC Energy Pricing Structure .....	14
K. Section 11 – Legacy PPA Matters for Existing QFs.....	15
L. Section 12 – CAISO Tariff Compliance.....	16
M. Section 13 -- IOU Cost Recovery For CHP PPAs.....	16
N. Section 14 -- Settlement Of Pending And Anticipated Litigation .....	17
O. Section 15 – FERC 210(m) Application.....	18
P. Section 16 – Conditions Precedent and Settlement Effective Date .....	19
Q. Section 17 – Glossary .....	19
R. Attachments .....	19
III. THE SETTLEMENT AGREEMENT IS REASONABLE AND IN THE PUBLIC INTEREST.....	20
A. The Settlement Agreement Is Reasonable And Consistent With Existing Law .....	21
1. Consistent With State And Commission Policy, The Settlement Agreement Is Intended To Facilitate CHP Goals and Objectives.....	21

**TABLE OF CONTENTS**  
**(continued)**

	<b>Page(s)</b>
2. Consistent With State And Commission Policy, The Settlement Agreement Is Intended To Facilitate GHG Emissions Reductions From CHP Facilities .....	22
3. The QF/CHP Program Procurement Process Is Consistent With The Commission’s Preference For Competitive Procurement .....	23
4. The Energy And Capacity Prices Are Reasonable And Consistent With Recent Commission Decisions .....	25
5. The QF/CHP Targets Are Appropriate. ....	26
6. The Semi-Annual Reports And CHP Auditor Process Are Consistent With Commission Policies Supporting Greater Public Information And Transparency .....	27
7. The Pro Forma PPAs and Legacy QF PPA Amendment.....	27
8. The Cost Recovery Proposal Is Reasonable And Consistent With California Law .....	32
9. The Settlement Resolves Numerous Pending And Anticipated Disputes.....	34
10. The Settlement Agreement Provides For Operationally Flexible Resources .....	35
B. The Settlement Agreement Is In The Public Interest.....	36
IV. THE JOINT PARTIES HAVE COMPLIED WITH THE REQUIREMENTS OF RULE 12.1(B).....	38
V. HEARINGS ARE NOT REQUIRED .....	38
VI. TIMING FOR REVIEW OF THE SETTLEMENT AGREEMENT AND CONDITIONS PRECEDENT FOR THE SETTLEMENT AGREEMENT TO BECOME EFFECTIVE.....	39
VII. CONCLUSION.....	41

**TABLE OF AUTHORITIES**

**Page(s)**

**CASES**

*Southern California Edison v. PUC*, 101 Cal.App.4<sup>th</sup> 982 (2002) ..... 4

**FERC DECISIONS AND ORDERS**

*New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation*, 130 FERC ¶ 61,216 (2010) ..... 5

Order No. 688 (Oct. 20, 2006)..... 5

**CALIFORNIA PUBLIC UTILITIES COMMISSION DECISIONS AND RESOLUTIONS**

*Re Pacific Gas & Electric Company*, D.88-12-083, 30 CPUC 2d 189 (1988)..... 20

D.03-12-062 ..... 24

D.04-01-050 ..... 23

D.04-12-048 ..... 16, 33

D.05-03-022 ..... 34

D.06-07-029 ..... 32

D.07-09-040 ..... passim

D.07-12-052 ..... 22, 23, 26, 35

D.08-09-012 ..... 16, 33, 34

D.08-10-037 ..... 22

D.08-11-008 ..... 23

D.09-10-017 ..... 20

D.09-12-042 ..... 32

D.10-04-055 ..... 32

D.10-06-031 ..... 34

Resolution E-4246 ..... 25

**STATUTES**

*Public Utility Regulatory Policies Act*, 16 U.S.C. § 796, *et seq.* ..... passim

§ 824a-3(m)..... 5, 18

18 CFR §292.205 ..... 30

Cal. Health & Saf. Code, § 38501, *et seq.* ..... 22

Cal. Pub. Util. Code § 216.6 ..... 30

**TABLE OF AUTHORITIES**  
**(continued)**

	<b>Page(s)</b>
Cal. Pub. Util. Code § 365.1(c)(1) .....	32
Cal. Pub. Util. Code § 372(a).....	6, 21
Cal. Pub. Util. Code § 8341 .....	30
Assem. Bill No. 1613 (2007-2008 Reg. Sess.) .....	24, 32
Assem. Bill No. 32 (2005-2006 Reg. Sess.) .....	6, 13, 22
Sen. Bill No. 695 (2009-2010 Reg. Sess.) .....	32

**CPUC RULES OF PRACTICE AND PROCEDURE**

Rule 12.1 .....	2, 3
Rule 12.1(b) .....	7, 38
Rule 12.1(d) .....	20

**MISCELLANEOUS**

Energy Action Plan II (Oct. 2005).....	21
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**JOINT MOTION  
FOR APPROVAL OF QUALIFYING FACILITY AND  
COMBINED HEAT AND POWER PROGRAM SETTLEMENT AGREEMENT**

The relationship among qualifying facilities (“QFs”), the investor-owned utilities (“IOUs”) and ratepayer advocate groups has been contentious and litigious for most of the last thirty years. After more than a year and a half of intensive negotiations, QF representatives, the IOUs, and ratepayer advocate groups have developed a proposed combined heat and power (“CHP”) settlement agreement (“Settlement Agreement”) that resolves numerous outstanding

QF-related disputes and allows for a smooth transition from the California Public Utilities Commission's ("Commission") existing QF Program to a new QF/CHP Program to preserve resource diversity, fuel efficiency, greenhouse gas ("GHG") emissions reductions and other benefits and contributions of CHP. In addition, the Settlement Agreement facilitates additional CHP benefits and contributions by promoting new, lower GHG emitting CHP facilities and encouraging the repowering, operational changes through utility pre-scheduling, or retirement of existing, higher GHG emitting CHP facilities. Finally, the Settlement Agreement appropriately allocates the costs of the QF/CHP Program to all customers in California who benefit from the CHP portfolio. In short, the Settlement Agreement provides a reasonable, prudent and well-balanced approach to the development of QFs and CHP facilities in California to ensure customer benefits associated with CHP over the near- and long-term.

The parties to the proposed Settlement Agreement represent numerous different groups and interests. These parties include the three investor-owned utilities ("IOUs") -- Pacific Gas and Electric Company ("PG&E"), Southern California Edison Company ("SCE"), and San Diego Gas & Electric Company ("SDG&E"); cogeneration and combined heat and power qualifying facility ("CHP QF") representatives -- the California Cogeneration Council ("CCC"), the Independent Energy Producers Association ("IEP"), the Cogeneration Association of California ("CAC"), and the Energy Producers and Users Coalition ("EPUC"); and statewide consumer and ratepayer groups -- the Division of Ratepayer Advocates ("DRA") and The Utility Reform Network ("TURN") (the parties are referred to hereinafter individually as a "Party" and collectively as the "Joint Parties").

Pursuant to Rule 12.1 (a) of the California Public Utilities Commission's ("Commission") Rules of Practice and Procedure, the Joint Parties respectfully file this *Joint Motion for Approval of Qualifying Facility and Combined Heat and Power Program Settlement*

*Agreement* (“Joint Motion”) proposing adoption of the attached Settlement Agreement.<sup>1</sup> While each of these groups have separate interests and concerns, the Joint Parties have worked together to develop a comprehensive framework for a QF/CHP Program in California that will encourage the development of efficient CHP, provide environmental benefits through reduced GHG emissions, resolve outstanding QF disputes and provide clear direction going forward on contentious QF issues including costs. During the settlement process, the Joint Parties were required to compromise and develop solutions. None of the Joint Parties received everything it wanted, and each of the Joint Parties was required to compromise in specific areas so that an overall settlement could be reached. The resulting Settlement Agreement represents a balance of the parties’ interests. Consistent with Commission Rule 12.1, the Joint Parties are providing a statement of the factual and legal considerations that are addressed in the Settlement Agreement and demonstrate that the Settlement Agreement is reasonable in light of the whole record, consistent with law, and in the public interest. For these reasons, the Joint Parties respectfully request that the Settlement Agreement be approved by the Commission without modification.<sup>2</sup>

In addition to this Joint Motion, the Joint Parties are filing a Motion for Expedited Consideration of Joint Motion For Approval of Qualifying Facility and Combined Heat and Power Settlement Agreement (“Motion for Expedited Consideration”). In Section VI, below, the Joint Parties provide a proposed schedule for Commission consideration of the Settlement Agreement. The same schedule is included in the Motion for Expedited Consideration.

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<sup>1</sup> The Settlement Agreement is attached as Attachment A to this motion.

<sup>2</sup> Each of the Joint Parties expressly reserves its rights to take positions contrary to the positions taken and arguments made in this motion if the Commission does not approve the Settlement Agreement without modification.

## **I. FACTUAL AND PROCEDURAL BACKGROUND**

### **A. PURPA and The Commission's QF Program**

In 1978, Congress enacted the Public Utility Regulatory Policies Act ("PURPA"), which was part of a national effort to promote energy independence and efficiency.<sup>3</sup> Under PURPA and the Federal Energy Regulatory Commission's ("FERC") subsequent regulations implementing PURPA, qualifying cogeneration and small power production facilities were provided certain benefits and exemptions. State regulatory agencies were delegated responsibility for developing QF programs and determining avoided-cost pricing. The Commission implemented PURPA in the early 1980s by adopting for the IOUs a number of standard form power purchase agreements ("PPAs") that were available to QFs and established energy and capacity prices to be paid under these PPAs. Many QFs signed these PPAs and built cogeneration and small power production facilities to provide energy and capacity to the IOUs.

Since the Commission implemented the QF program in the 1980s, there have been disputes between the QFs, IOUs and ratepayer advocates including: contract terms, Short-Run Avoided Cost ("SRAC") pricing, capacity payments, contract extensions and terminations, and the availability of new contracts. Many of these disputes are still pending at the Commission. Section 14 of the Settlement identifies disputes pending at the Commission regarding several proceedings, including: retroactive adjustments to SRAC pricing; disputes over pricing and ability to execute PPA extensions; motions for prospective QF PPA options; SRAC disputes dating back to the 2000-2001 energy crisis; disputes concerning administrative heat rates ("AHR") used to calculate SRAC; and applications for rehearing and petitions for modification

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<sup>3</sup> 16 U.S.C. § 796, *et seq.*; *see also Southern California Edison v. PUC*, 101 Cal.App.4<sup>th</sup> 982, 986-87 (2002) (describing PURPA).

of numerous QF decisions.<sup>4</sup> In addition to these disputes pending at the Commission, there are also disputes pending in the California Court of Appeal.<sup>5</sup>

Not only is the Commission faced with disputes regarding existing QF PPAs and the existing QF program, the Commission is also faced with challenges as to how to implement the QF program going forward. For example, in Decision (“D.”) 07-09-040, the Commission recognized that it would need to address the impact of the California Independent System Operator’s (“CAISO”) Market Redesign and Technology Upgrade (“MRTU”) on SRAC and the QF program.<sup>6</sup> The Commission also has before it disputes over the terms and conditions of the new QF Standard Offer Contract (“SOC”)<sup>7</sup> and disputes over the amount of QF capacity to include in the Long-Term Procurement Process (“LTTP”).<sup>8</sup>

On the federal level, recently there have been changes to the PURPA purchase obligation. In October 2006, FERC issued Order No. 688:

... revising its regulations governing utilities’ obligations to purchase electric energy produced by QFs. Order No. 688 implements PURPA section 210(m), which provides for termination of the requirement that an electric utility enter into power purchase obligations or contracts to purchase electric energy from QFs, if the Commission finds the QFs have nondiscriminatory access to markets.<sup>9</sup>

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<sup>4</sup> See Term Sheet, §§ 14.1 – 14.2.

<sup>5</sup> *Id.* at § 14.2.4.

<sup>6</sup> D.07-09-040 at p. 68.

<sup>7</sup> See *e.g.*, Draft Resolution E-4242 and comments filed by parties concerning the draft resolution.

<sup>8</sup> *Joint Petition for Modification of D.07-12-052 by Southern California Edison Company (U 338-E), Pacific Gas & Electric Company (U 39-E), and San Diego Gas & Electric Company (U 902-E)*, filed December 17, 2008 in R.06-02-013.

<sup>9</sup> *New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation*, 130 FERC ¶ 61,216 (2010) at P. 3 (footnotes omitted).

Although the California IOUs have not yet sought from FERC a termination of their PURPA purchase obligation for QFs larger than 20 MW, the changes in PURPA further support a re-examination of California's existing QF program.

Given the numerous outstanding disputes, changes in PURPA, and challenges in determining a QF and CHP Program ("QF/CHP Program") going forward, the Joint Parties, California customers and the Commission will benefit from a Settlement that: (1) resolves the outstanding disputes; (2) sets out a clear path for the implementation of a cogeneration QF and CHP Program in California; and, (3) makes available additional PPA options for QFs under the QF/CHP Program ("CHP PPAs").

#### **B. State Policy Favoring CHP**

Public Utilities Code Section 372(a) and Energy Action Plan II both demonstrate that state policy supports the development of "efficient, environmentally beneficial" CHP. In the 2009 Integrated Energy Policy Report ("IEPR"), the California Energy Commission ("CEC") recommended the continued support and development of CHP as a means to meet state green house gas ("GHG") goals and other policy objectives.<sup>10</sup>

#### **C. CARB's Climate Change Scoping Plan**

On December 11, 2008, the California Air Resources Board ("CARB") adopted the Climate Change Scoping Plan for California pursuant to Assembly Bill ("AB") 32 (the "CARB Scoping Plan").<sup>11</sup> In the CARB Scoping Plan, CARB noted that,

[c]ombined heat and power (CHP), also referred to as cogeneration, produces electricity and useful thermal energy in an integrated system. The widespread development of efficient CHP systems would help displace the need to develop new, or expand existing, power plants. This measure sets a target of an additional 4,000 MW of installed CHP capacity by 2020, enough to displace

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<sup>10</sup> See, 2009 IEPR at pp. 8-9.

<sup>11</sup> See, [http://www.arb.ca.gov/cc/scopingplan/document/adopted\\_scoping\\_plan.pdf](http://www.arb.ca.gov/cc/scopingplan/document/adopted_scoping_plan.pdf).

approximately 30,000 GWh of demand from other power generation sources.<sup>12</sup>

Although CARB has not yet issued final GHG regulations, the CARB Scoping Plan indicates support for the development of efficient CHP.

#### **D. Description Of the Settlement Process**

Recognizing the need to resolve outstanding disputes and to establish a new CHP program for California going forward, in May 2009, the Joint Parties and Commission representatives met to lay out a settlement framework. Since that time, the Joint Parties have conducted frequent and lengthy meetings and worked diligently to negotiate the Settlement Agreement now presented to the Commission. The Joint Parties had divergent interests, many of which had been escalated in proceedings at the Commission and before the appellate court, which had to be accommodated. As a result, the Settlement Agreement represents a compromise that should be evaluated as an integrated package. The Settlement Agreement is over 75 pages long and provides a detailed and comprehensive framework for a QF/CHP Program in California. In addition to the Settlement Agreement Term Sheet (“Term Sheet”), the Joint Parties also negotiated four *Pro Forma* PPAs and standard amendments for Legacy QF PPAs for each of the IOUs that will be used as a part of the QF/CHP Program.

Taken as a whole, the Settlement Agreement, including the *Pro Forma* PPAs and amendments described in more detail below, represent a reasonable and appropriate resolution of the many QF issues presently under consideration before the Commission and in other forum. Consequently, the Commission should adopt the Settlement Agreement in its entirety and without change.

Consistent with Rule 12.1(b), the Joint Parties, on September 24, 2010, provided notice to the service lists in these proceedings of a formal settlement conference.<sup>13</sup> The conference was

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<sup>12</sup> CARB Scoping Plan, at pp. 42-43 (footnotes omitted).

conducted on October 7, 2010. An overview of the proposed Settlement Agreement was presented, participants were able to ask questions and provide comments. Those that were interested in joining to support the Settlement Agreement were invited to do so. After the settlement conference was completed and participants were given an opportunity to review and comment on the Settlement Agreement, this Joint Motion was filed.

## **II. SUMMARY OF THE PROPOSED SETTLEMENT AGREEMENT**

This section includes a summary of the key terms of each section of the Term Sheet, as well as the *Pro Forma* PPAs and the *Pro Forma* PPA amendments included with the Settlement Agreement.<sup>14</sup> Given the length of the Settlement Agreement, this section is only intended to be a summary of key terms. Any inconsistencies between this summary and the Term Sheet should be governed by the Term Sheet.

### **A. Section 1 – Goals and Objectives**

This section outlines the goals and objectives of the Settlement Agreement.

### **B. Section 2 – Settlement Periods**

This section describes the three periods covered by the Settlement Agreement – the Transition Period, the Initial Program Period, and the Second Program Period. The Transition Period is designed to facilitate the transition from the existing QF Program to the new QF/CHP Program. During the Initial Program Period, which overlaps with the Transition Period, the IOUs have specific Megawatt (“MW”) Targets (“MW Targets”) for entering into new PPAs with

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<sup>13</sup> Because of widespread interest in matters at issue in these proceedings, notice of potential settlement was also provided to the service lists in R.03-10-003, R.07-05-025, and R.08-06-024.

<sup>14</sup> The fact that a specific provision in the Settlement Agreement is not discussed here does not explicitly or implicitly imply that any provision or term of the Settlement Agreement is more or less important. Moreover, if there is any unintended ambiguity created by the summary below as compared to specific Settlement Agreement terms, the specific provisions in the Settlement Agreement or applicable PPAs and amendments are controlling. The Settlement Agreement is an integrated package and each provision and term was carefully negotiated as a part of that integrated package.

CHP and other facilities. In the Second Program Period, the IOUs procure any portion of the MW Targets that they did not procure during the Initial Program Period and additional CHP capacity to meet GHG Emissions Reduction Targets (“GHG Targets”) or other CHP procurement targets established by the Commission. SDG&E has a target to procure an additional 51 MW during the Second Program Period.

**C. Section 3 – Transition PPA**

This section describes the eligibility requirements for QF and CHP facilities for a PPA during the Transition Period and the pricing for Transition Period PPAs.<sup>15</sup> The “Transition Standard Contract for Existing Qualifying Cogeneration Facilities” (“Transition PPA”) is included as an exhibit to the Term Sheet and is an attachment to the Settlement Agreement.

**D. Section 4 – CHP Procurement Process**

This section describes the various aspects of the CHP procurement process under the new QF/CHP Program. First, Section 4.2 describes the new CHP Request for Offers (“CHP RFO”) process under which the IOUs will procure generation from CHP facilities to meet MW Targets and GHG Targets specified in the Settlement Agreement.<sup>16</sup> Section 4.2 includes eligibility requirements for CHP participating in the RFOs (Section 4.2.2), the delivery terms of PPAs resulting from the RFOs (Section 4.2.3), pricing (Section 4.2.4), and RFO evaluation and selection criteria (Section 4.2.5). In addition, the Joint Parties developed a Pro Forma power purchase agreement for CHP RFOs (“CHP RFO PPA”) that will be attached as an exhibit to the Term Sheet.

Section 4 also describes the procurement processes for CHP other than through CHP RFOs that will count towards meeting MW and GHG Targets. Specifically, Sections 4.3 - 4.6

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<sup>15</sup> Term Sheet, §§ 3.1 – 3.2.

<sup>16</sup> The MW Targets and GHG Targets are described in Sections 5 and 6 of the Term Sheet, respectively.

describe bilaterally negotiated CHP PPAs, PPAs under the AB 1613 feed-in tariff, PPAs for QFs of 20 MW or less under PURPA, and Optional As-Available PPAs for certain large CHP facilities that have significant on-site load and specific operating characteristics. Section 4.7 addresses utility-owned CHP and limits the contribution of utility-owned facilities to ten percent (10%) of each IOU's GHG Target. IOU-owned facilities will not count toward the MW Targets in the Initial Program Period. Section 4.8 describes "utility prescheduled facilities" which are existing QF facilities that convert to IOU-dispatchable generating facilities.<sup>17</sup> Finally, Section 4.9 addresses new behind-the-meter CHP facilities as one of the procurement options under the QF/CHP Program.

Section 4.10 specifies the Commission approval process required for new PPAs arising from the procurement options in the QF/CHP Program. This includes Tier 2 advice letter filings for existing CHP facilities that execute the CHP RFO PPA without material modification, and a Tier 3 advice letter process for all other CHP PPAs. CHP PPAs that are less than five years in duration do not require Commission pre-approval but will be reported in the IOUs' Quarterly Compliance Reports and CHP Program Semi-Annual Report.

Section 4.11 specifies information that CHP facilities must provide to the IOUs on an annual basis for monitoring purposes and Section 4.12 specifies the timing for commencement of deliveries from a CHP facility that has entered into a new CHP PPA.

#### **E. Section 5 – MW Targets**

Section 5 establishes a total MW Target for the IOUs of 2,949 MW during the Initial Program Period and a total MW Target of 3,000 MW for the entire QF/CHP Program. Section 5.1.2 includes a chart allocating this MW Target to three target periods for each of the IOUs. For example, the first MW Target for SCE, PG&E, and SDG&E are 630 MW, 630 MW, and 60

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<sup>17</sup> This provision in the Settlement Agreement is described in more detail in Section III.A.9, below.

MW, respectively. SDG&E has a specified MW Target during the Second Program Period. If the IOUs have not fulfilled the MW Targets assigned to them for the Initial Program Period they will also need to procure MWs during the latter period to fulfill those targets.

Section 5.1.4 provides that the IOUs are required to conduct three CHP RFOs during the Initial Program Period to seek CHP PPAs to meet the MW Targets. The number of CHP RFOs during the Second Program Period will be established in the LTPP proceedings.<sup>18</sup>

Section 5.2 includes detailed counting rules as to how CHP PPAs executed during the Initial Program Period, whether through a CHP RFO or another procurement process, count toward the MW Targets. Section 5.3 clarifies the appropriate use of the MW counting procedure.

Section 5.4 addresses justifications for an IOU's failure to meet its MW Target. These justifications include lack of sufficient offers in the RFOs, the efficiency of CHP participating in the procurement programs, excessive offer prices<sup>19</sup>, and the amount of GHG reductions.

#### **F. Section 6 – GHG Emissions Reduction Targets**

One of the key benefits of the Settlement Agreement is the implementation of a CHP Program designed to reduce GHG, consistent with the CARB Scoping Plan. Section 6.1 describes the Settlement Agreement strategy for reducing GHG, including maintaining existing, efficient CHP facilities, adding new, efficient CHP resources and achieving the GHG Targets by December 31, 2020. Section 6.2 addresses maintaining the GHG emissions reductions from existing CHP and establishing new targets for GHG reductions from new facilities. In particular, the Settlement Agreement establishes a GHG Emissions Reduction Target or “GHG Target” of 4.3 million-metric tons (“MMT”) for the IOUs and 0.5 MMT for Energy Service Providers

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<sup>18</sup> Term Sheet, § 5.1.4.7.

<sup>19</sup> An IOU claiming that RFO offer prices are excessive must support its claim with information from independent or publicly available sources. *Id.*, § 5.4.1.

(“ESPs”) and Community Choice Aggregators (“CCA”).<sup>20</sup> These targets are based on the 6.7 MMT GHG reduction attributable to CHP in the CARB Scoping Plan.<sup>21</sup> Based on the current percentage of retail sales in California, the 6.7 MMT would be allocated as follows: (1) 4.3 MMT to the IOUs; (2) 0.5 MMT to ESPs and CCAs; and (3) 1.9 MMT to publicly-owned utilities (“POUs”).<sup>22</sup> The Commission does not have jurisdiction over POUs, but can set GHG Emissions Reduction Targets for the IOUs, ESPs and CCAs.

Section 6.2.2.3.3 provides for the adjustment of the allocation of the GHG Targets based on changes in retail sales during the term of the Settlement Agreement.<sup>23</sup> Thus, for example, if customers depart utility service for ESPs or CCAs, the GHG Targets for the IOUs will decrease and the targets for the ESPs and CCAs will increase. The GHG Targets can also be adjusted among the IOUs.

Section 6.3 identifies the GHG Target allocated to ESPs and CCAs and indicates that it is the preference of the Joint Parties that these non-IOU load-serving entities (“LSEs”) achieve these targets by entering into CHP PPAs. However, if these non-IOU LSEs are not required to enter into CHP PPAs, the IOUs will procure the appropriate amount of CHP for these LSEs to meet their GHG Target and the costs of this procurement by the IOUs will then be allocated to the customers of non-IOU LSEs. The allocation of CHP PPA costs is addressed in Section 13 of the Settlement Agreement. Section 6.4 describes the methodology for establishing the GHG Targets for each of the IOUs. Section 6.5 requires each IOU to report its progress toward meeting its GHG Target in its semi-annual CHP Program Reports that are submitted to the

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<sup>20</sup> *Id.*, § 6.3.1.

<sup>21</sup> *Id.*, §6.2.2.1.

<sup>22</sup> *Id.*, §6.2.2.3.

<sup>23</sup> *See also id.*, § 6.3.3.

Commission. Section 6.6 states that the GHG Targets for the Second Program Period are subject to review and revision in the LTPP process.

Section 6.7 provides for revisions to the GHG Targets if CARB modifies its CHP reduction goals and provides for GHG Targets to be adjusted in the LTPP if AB 32 compliance is suspended or delayed. In Section 6.8, the Joint Parties agree to advocate at CARB in support of the Settlement Agreement, subject to certain conditions.

Finally, Section 6.9 sets out the justifications for failing to meet the GHG Targets, including the efficiency of CHP facilities participating in the IOUs' procurement programs, excessive offer prices and a lack of need for CHP resources.

#### **G. Section 7 – GHG Emission Accounting Methodology**

Section 7 establishes the accounting principles for determining the IOUs' progress toward meeting their GHG Targets. This section adopts a Double Benchmark methodology for determining GHG reductions and provides detailed accounting procedures for new, repowered, and existing CHP facilities to determine the amount of GHG emissions reductions that are attributable to these different types of facilities.

#### **H. Section 8 – Commission Jurisdictional Entities' Reporting Requirements**

Section 8 establishes reporting requirements for Commission-jurisdictional LSEs (*i.e.*, the IOUs, ESPs and CCAs). Each LSE must prepare a semi-annual report detailing progress toward meeting its MW Targets and GHG Targets.<sup>24</sup> Sections 8.2 – 8.5 describe the contents of the semi-annual reports, and specify report content for different categories of CHP generation (*e.g.*, new, legacy, terminated).

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<sup>24</sup> *Id.*, § 8.1.1.

## **I. Section 9 – CHP Auditor**

Section 9 provides for a CHP auditor (“CHP Auditor”) who is to act as an advocate for CHP interests regarding the implementation of the QF/CHP Program.<sup>25</sup> The CHP Auditor is used in situations where an IOU provides notice that it does not anticipate meeting the MW Targets during a particular RFO or the GHG Targets. The CHP party or parties requesting a CHP Auditor bear the costs<sup>26</sup> and the CHP Auditor is provided with an opportunity to receive and review confidential IOU information regarding the relevant QF/CHP RFO. Section 9 includes provisions for execution of a non-disclosure agreement by the CHP Auditor (Section 9.1.4), when an IOU notice triggers an audit (Section 9.2), the time period for an audit review (Section 9.3), receipt and review of confidential information (Section 9.4), and the number of CHP Auditors, as well as rules regarding any potential conflicts of interest (Section 9.5).

## **J. Section 10 – SRAC Energy Pricing Structure**

Section 10 establishes methodologies and formulas for SRAC to be used in Transition PPAs, Legacy PPAs, other existing QF PPAs and Optional As-Available PPAs.<sup>27</sup> Section 10.2 includes a methodology for transitioning, by January 1, 2015, SRAC pricing from a formula that is based in part on administratively-determined heat rates to a formula that uses solely market heat rates. Section 10.4 includes a process for addressing market disruptions that may impact the market heat rate to be used in SRAC. Section 10.2 also includes IOU-specific time-of-use (“TOU”) factors to be applied to energy prices to encourage energy deliveries during the times when the energy is most needed by customers. The SRAC formula also includes a locational adjustment based on CAISO nodal prices. Section 10.2 also includes pricing options based on

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<sup>25</sup> *Id.*, § 9.1.2.

<sup>26</sup> *Id.*, § 9.1.3.

<sup>27</sup> Prices for RFO PPAs are based on competitive bids in the RFO process and bilateral PPA prices are based on negotiated prices between the IOU and the CHP party.

whether a cap-and-trade program or other form of GHG regulation is developed in California or nationally.

When such a cap-and-trade program is initially developed that applies to California, Section 10.2 establishes a floor test which compares an energy price developed with a market-based heat rate to an energy price developed with either a negotiated heat rate, or a heat rate from a period prior to the start of a cap and trade program, plus the market price of GHG allowances. The higher of the two energy prices is the one chosen as SRAC.

Section 10.3 requires the Seller under a CHP PPA to provide certain information to the IOU regarding GHG information that it has reported to CARB or another governmental authority, and information concerning the operation of its facility. Finally, Section 10.5 addresses the responsibility for GHG-related costs.

**K. Section 11 – Legacy PPA Matters for Existing QFs**

Under Section 11.1, QFs with existing standard offers or other PPAs (“QF PPAs”) at the time of the Settlement Effective Date<sup>28</sup> will be paid for energy based on the SRAC formula specified in Section 10 (unless the QF PPA specifies a different price) or may elect to amend their standard offer QF PPA to choose one of the energy price options described in the Legacy QF Amendments, are attached as an exhibit to the Settlement Agreement. Unless otherwise specified in the QF PPA, capacity payments for QF PPAs will be based on the capacity price established by the Commission in D. 07-09-040. Section 11.2 provides for the transition from a QF PPA to a new CHP PPA and ensures that delivery from an existing CHP facility continues uninterrupted during that period. The amendments are not available to QFs participating in the Renewable Portfolio Standard program.

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<sup>28</sup> The Settlement Effective Date is described in Section 16 of the Term Sheet.

Section 11.3 provides that the Seller under an existing QF PPA shall make a good faith effort to provide forecasting information to the IOU so that the IOU can more accurately schedule QF generation in the CAISO markets. This section provides specific forecasting submittal procedures.

**L. Section 12 – CAISO Tariff Compliance**

Section 12 provides that all CHP facilities subject to the CAISO Tariff shall comply with CAISO requirements when the facility begins deliveries under a CHP PPA. Section 12 also includes requirements for the installation of metering and telemetry equipment at existing CHP facilities within six (6) months of the execution of a CHP PPA. The Joint Parties also acknowledge that the CAISO may condition, waive or modify certain requirements for QF and CHP facilities.

**M. Section 13 -- IOU Cost Recovery For CHP PPAs**

Section 13 addresses cost allocation if the Commission determines that IOUs should purchase CHP generation on behalf of ESPs and CCAs.<sup>29</sup> In this circumstance, the IOUs are authorized to recover “net capacity costs” from all bundled, direct access (“DA”) and CCA customers on a non-by-passable basis. Net capacity costs are the total costs paid by the IOU under the QF/CHP Program less the value of the energy and ancillary services supplied to the IOU under the program.

Section 13.1.1 recognizes that PPAs under the QF/CHP Program may be greater than ten (10) years and requires that the Commission: (1) affirmatively supersede the ten (10)-year limitation for stranded cost recovery established in D. 04-12-048 and D. 08-09-012 and (2) determine that all above-market or net capacity costs associated with the QF/CHP Program can be recovered for the entire duration of any CHP PPA.

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<sup>29</sup> Term Sheet, § 13.1.2.2.

Section 13.1.2.1 provides that if the Commission determines that ESPs and CCAs are responsible for procuring CHP generation for their customers, any above-market costs associated with the QF/CHP Program can be allocated to future departing load customers who depart for DA or CCA service.

In Sections 13.1.3 and 13.1.4, the Joint Parties agree that they will not advocate the imposition of QF/CHP Program costs on CHP customer generation departing load, and in Section 13.1.5 the Joint Parties agree to advocate that CHP PPAs entered into as a result of the QF/CHP Program not be included in the existing Competition Transition Charge.

Finally, Section 13.2 provides that all payments made by the IOUs under the QF/CHP Program can be recovered in the IOUs' respective Energy Resources Recovery Account.

**N. Section 14 -- Settlement Of Pending And Anticipated Litigation**

Section 14 addresses the settlement of pending, as well as anticipated, claims and litigation. In Section 14.1, the IOUs agree under certain conditions to withdraw with prejudice all SRAC retroactive price adjustment claims. The Joint Parties mutually agree not to raise any new SRAC retroactive adjustment claims as long as the PURPA purchase obligation remains suspended (as described in more detail in Section 15).

In Section 14.2, the Joint Parties agree to release or withdraw a number of pending claims, rehearing applications, or motions including claims and motions at the Commission (Sections 14.2.1 – 14.2.3, 14.2.5 – 14.2.12) and pending appeals at the Court of Appeal (Section 14.2.4). Section 14 does not affect the Joint Parties' rights to advocate their respective position regarding the confidentiality of IOU procurement information.<sup>30</sup>

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<sup>30</sup> *Id.*, § 14.3.2.

**O. Section 15 – FERC 210(m) Application**

Under Section 15, after the Commission approves the Settlement Agreement, the IOUs will submit an application to FERC requesting termination of the IOUs’ PURPA purchase requirement from QFs with net capacity in excess of 20 MW, consistent with Section 210(m) of PURPA. Section 15.1 establishes a process for the CHP representatives to review the IOUs’ FERC application and provides that these parties can intervene and comment on, but not protest, the IOUs’ application. Under Section 15.1.10, the CHP representatives can file at FERC for reinstatement of the PURPA purchase obligation if an IOU “breaches its obligations under the Settlement [Agreement] or the CHP Program adopted in the Settlement [Agreement] is not successfully implemented, based upon the IOU’s failure to meet the targets established by the CPUC pursuant to the Settlement [Agreement], without justification as provided for in the Settlement [Agreement].”

Section 15.2 addresses a circumstance where FERC reinstates the PURPA purchase obligation. In this case, SRAC pricing established under the Settlement Agreement stays in place until changed by the Commission (Section 15.2.1.1), although Joint Parties may advocate for a change to SRAC (Section 15.2.1.3). Joint Parties may also advocate for retroactive adjustments to SRAC pricing (Section 15.2.1.4). If the PURPA purchase obligation is reinstated, the IOUs’ obligations to conduct CHP RFOs or to engage in alternative procurement processes and the MW Targets and GHG Targets are suspended “provided that the CPUC may on grounds other than the Settlement [Agreement] direct the procurement of CHP resources.” (Section 15.2.1.7) Any procurement target to be established by the Commission in the LTPP remains in place unless and until modified by the Commission in a subsequent proceeding. The Joint Parties also agree in Section 15.2.1.8 that for purposes of Section 210(m), designated CHP PPAs constitute “legally enforceable obligations.”

**P. Section 16 – Conditions Precedent and Settlement Effective Date**

Section 16.2 specifies that the Settlement Agreement becomes effective upon satisfaction of the following conditions precedent: (1) a final and non-appealable FERC order approving the IOUs’ application to terminate their PURPA purchase obligation (Section 16.2.1); (2) a final and non-appealable Commission decision approving the Settlement, including a determination that the Settlement supersedes certain portions of existing Commission decisions (Sections 16.2.2 and 16.2.4 – 16.2.6); and (3) CARB support, in written form, for the Settlement (Section 16.2.3).

Section 16.3 provides that after the Settlement Agreement becomes effective, if CARB adopts regulations directly imposing a MW Target or GHG Emissions Target that differs from the Settlement Agreement for the Second Program Period, the IOUs’ obligations to purchase from CHP to meet these targets will remain in place until such time as the Commission is able to consider such change in an LTPP or other pertinent proceeding.

**Q. Section 17 – Glossary**

The section includes a glossary of the defined terms used in the Settlement.

**R. Attachments**

The Settlement Agreement attaches the Term Sheet and Exhibits 1-11 below:

1. Amendment to Legacy QF PPA for PG&E
2. Amendment to Legacy QF PPA for SCE
3. Amendment to Legacy QF PPA for SDG&E
4. Transition PPA for existing Qualifying Cogeneration Facilities
5. CHP RFO Pro Forma PPA for CHP Facilities Participating in Solicitations
6. QF PPA for QFs 20 MW or Less;
7. Optional As-Available PPA for eligible As-Available Facilities;
8. Non-Disclosure Agreement (“NDA”) for CHP Auditor;

9. List of Members of CAC
10. List of Members of CCC
11. List of Members of EPUC

Exhibits 1-7 containing the PPAs are described in more detail below in Section III.A.6. An additional attachment to this Joint Motion, offered for the Commission's information, is the Letter Agreement between the CAISO and the three utilities describing their understanding concerning the utilities' responsibilities concerning CHP/QF compliance with CAISO Tariffs and Protocols under the PPAs attached in Exhibits 4-7.

In addition, included as Attachment B to this Joint Motion is a letter agreement between the CAISO and the IOUs regarding implementation of the Settlement Agreement.

### **III. THE SETTLEMENT AGREEMENT IS REASONABLE AND IN THE PUBLIC INTEREST**

The Commission will approve a settlement if it finds the settlement "reasonable in light of the whole record, consistent with law, and in the public interest."<sup>31</sup> The proposed Settlement Agreement readily meets these criteria. The Joint Parties negotiated in good faith, bargained aggressively, compromised, and agreed to the Settlement Agreement as an interrelated package; the resolution of any one issue cannot be assessed discreetly. Due to the divergence of the interests of the Joint Parties that had to be accommodated, the Settlement Agreement with regard to each issue represents compromises by various Parties. The Commission, in evaluating the Settlement Agreement, should evaluate it as a package. Each element of the Settlement Agreement is related to all others, any change to the resolution of any one issue may offset the balance that the entire package strikes and represents.

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<sup>31</sup> Rule 12.1(d); *see also* D.09-10-017 (applying Rule 12.1(d) criteria).

Factors that the Commission has considered in reviewing settlements include: (1) the risk, expense, complexity and likely duration of further litigation, (2) whether the settlement negotiations were at arms-length, (3) whether major issues were addressed, and (4) whether the parties were adequately represented.<sup>32</sup> In this case, the Settlement Agreement resolves complex and contentious litigation on QF and SRAC pricing matters presently before the Commission and the Court of Appeal. The lengthy settlement negotiations were at arms-length and addressed the major issues regarding the development and operation of CHP in California historically and going forward.

**A. The Settlement Agreement Is Reasonable And Consistent With Existing Law**

**1. Consistent With State And Commission Policy, The Settlement Agreement Is Intended To Facilitate CHP Goals and Objectives.**

As set forth in the Settlement Agreement, the policy objectives addressed by the Settlement Agreement include requirements under:

- Section 372(a) of the California Public Utilities Code which states: “it is the policy of the state to encourage and support the development of cogeneration technology as an efficient, environmentally beneficial, competitive energy resource that will enhance the reliability of local generation supply, and promote local business growth.”
- The Energy Action Plan II which states: “The loading order identifies energy efficiency and demand response as the State’s preferred means of meeting growing energy needs. After cost effective efficiency and demand response, we rely on renewable sources of power and distributed generation, such as combined heat and power applications. To the extent efficiency, demand response, renewable resources, and distributed generation are unable to satisfy increasing energy and capacity needs, we support clean and efficient fossil-fired generation.”

According to the Settlement Agreement;

“The purpose of the State CHP Program is to encourage the continued operation of the State’s Existing CHP Facilities, and the development, installation, and interconnection of new, clean and efficient CHP Facilities, in order to increase the diversity, reliability, and environmental benefits of the energy resources available to the State’s electricity

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<sup>32</sup> *Re Pacific Gas & Electric Company*, 30 CPUC 2d 189, 222.

consumers.”

“These policies and purposes will be achieved by a State CHP Program that procures CHP as set forth in this Settlement, retains existing efficient CHP, supports the change in operations of inefficient CHP to provide greater benefits to the State, and replaces CHP that will no longer be under contract with the IOUs with new, efficient CHP.”

**2. Consistent With State And Commission Policy, The Settlement Agreement Is Intended To Facilitate GHG Emissions Reductions From CHP Facilities.**

When it enacted AB 32, the California Legislature declared that global warming caused by GHG emissions posed a serious threat to California.<sup>33</sup> AB 32 was designed to reduce California’s GHG emissions. Since AB 32 was enacted, the Commission has repeatedly indicated that the reduction in GHG emissions is a key policy objective for the utility industry.<sup>34</sup> The Commission, CARB and the CEC have all recognized that efficient and clean CHP can reduce GHG emissions.<sup>35</sup> Indeed, CARB has made CHP one element in its Scoping Plan to implement AB 32 and reduce GHG emissions in California.

As stated in the Settlement Agreement: “In addition, this State CHP Program will secure additional Greenhouse Gas (GHG) emissions reduction benefits, consistent with the reduction targets of Assembly Bill (AB) 32, by adding new, efficient CHP.” Consistent with state law and these policy objectives, the Settlement is intended to facilitate the reduction in GHG emissions in a number of ways.

First, under the Settlement, GHG Targets are set for all Commission-jurisdictional LSEs, including the IOUs, ESPs and CCAs.<sup>36</sup> These targets are intended to facilitate the LSEs meeting

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<sup>33</sup> Cal. Health and Safety Code, § 38501, *et seq.*

<sup>34</sup> See *e.g.*, D.07-12-052 at pp. 2-5, 243; D.08-10-037 at pp. 2-3 (providing general overview of utility industry role in GHG reduction).

<sup>35</sup> D.08-10-037 at pp. 237-238 (Commission discussion of CHP); CARB Scoping Plan at pp. 43-44; 2009 IPER at pp. 97-98.

<sup>36</sup> Term Sheet, § 6.

CARB's CHP goals by December 31, 2020.<sup>37</sup> To the extent CARB modifies its CHP goals, the Settlement provides flexibility to incorporate any modification in the CARB goals.<sup>38</sup>

Second, the Settlement creates incentives for upgrading existing, inefficient CHP facilities, or, alternatively, for facilities that cannot participate or are unsuccessful in the CHP Program, the Settlement Agreement provides an orderly exit strategy. All CHP facilities will be able to participate in the CHP RFOs, and some will be able to participate in other procurement processes and obtain contracts that facilitate the financing, construction and operation of upgraded and/or new facilities. The CHP RFO PPA will explicitly include efficiency performance obligations.<sup>39</sup> The Settlement Agreement recognizes as one of the QF/CHP Program goals upgrading inefficient existing CHP facilities, or allowing them to retire, and encouraging the development of new, clean and efficient CHP.<sup>40</sup>

Third, the Settlement Agreement includes a requirement for all Commission-jurisdictional LSEs to file semi-annual compliance reports that include GHG emissions information.<sup>41</sup> This will allow the Commission and other interested parties to monitor the GHG emissions resulting from the QF/CHP Program and to determine if LSEs are obtaining the GHG benefits expected, and to address any shortfalls in expected GHG emission reduction benefits in a timely manner.

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<sup>37</sup> *Id.*, § 6.1.

<sup>38</sup> *Id.*, § 6.7

<sup>39</sup> *Id.*, § 4.2.9.

<sup>40</sup> *Id.*, §§ 1.2.2.3 – 1.2.2.5; *see also* § 7.3 (GHG accounting methodology which takes into account GHG benefits from new facilities and retirement of inefficient existing CHP facilities).

<sup>41</sup> *Id.*, § 8.

### **3. The QF/CHP Program Procurement Process Is Consistent With The Commission's Preference For Competitive Procurement.**

The Commission has repeatedly stated a policy preference for competitive wholesale energy markets and competitive solicitations to procure new resources in those markets.<sup>42</sup> Currently, CHP QF contracting is not conducted through a competitive solicitation process. The Commission's early QF Program involved the issuance of standard offer contracts that a QF of any technology could sign. In recent years, the CHP QF Program has primarily been sustained by extensions of existing contracts and the availability of short-term contracting options. In D.07-09-040, however, the Commission ordered the IOUs to offer QFs five (5) year as-available and ten (10) year firm PPAs. Despite considerable efforts, those contracts have never been finalized or made available to QFs.

Under the Settlement Agreement, a new, competitive procurement process will be adopted in lieu of the Commission ordered contracts. In particular, the Settlement Agreement creates a CHP RFO process that allows the IOUs to run competitive, transparent RFOs for CHP resources.<sup>43</sup> This is a significant change in CHP procurement and puts CHP resources into a process similar to the one currently used for conventional and Renewable Portfolio Standard ("RPS") procurement. This process will result in competitive prices that are ultimately subject to Commission approval.

In addition, the Commission has also provided for other methods for utility procurement, such as bilateral contracting.<sup>44</sup> The Settlement Agreement provides similar additional flexibility to the IOUs in the CHP procurement process by including not only RFOs, but also other processes such as bilateral contracting, AB 1613 feed-in tariffs, a PURPA Program for QFs

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<sup>42</sup> D.04-01-050 at p. 63 (discussing competitive solicitations); D.07-12-052 at p. 205 (discussing development of functional competitive energy market); D.08-11-008 at p. 20 (same).

<sup>43</sup> Term Sheet, § 4.2.

<sup>44</sup> See e.g. D.03-12-062 at pp. 38-40 (approving bilateral contracting under certain conditions).

under 20 MW, utility-ownership, and other procurement options.<sup>45</sup> The Settlement Agreement also includes a regulatory approval process for CHP PPAs that result from these procurement options.<sup>46</sup> In short, the Settlement Agreement adopts a procurement process for QF and CHP resources that is competitive, flexible, and allows for sufficient regulatory oversight to ensure that the IOUs are able to minimize costs and select appropriate resources for California customers.

#### **4. The Energy And Capacity Prices Are Reasonable And Consistent With Recent Commission Decisions.**

There are several different pricing and contracting options in the Settlement. First, CHP PPA prices will be set on a contract-specific basis through a competitive RFO process subject to Commission approval.<sup>47</sup> Allowing CHP developers to bid into the RFO will allow them to propose prices that are sufficient to finance and develop their facilities, while at the same time allowing the IOUs to pick the best offers based on a number of criteria, including price. An RFO procurement process, similar to the processes currently used for conventional and Renewable Portfolio Standard (“RPS”) contracts, will result in competitive prices that are ultimately subject to Commission approval. In addition, to the extent that RFO prices are excessive, the Settlement Agreement expressly provides that an IOU may use excessive prices as a justification for failing to meet the MW Targets and GHG Targets.<sup>48</sup>

Second, the Settlement Agreement establishes SRAC prices for the Transition PPAs, Legacy PPAs, QF contracts that are still available under PURPA for facilities less than 20 MW,

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<sup>45</sup> Term Sheet, §§ 4.3 – 4.9.

<sup>46</sup> *Id.*, § 4.10.

<sup>47</sup> Bilaterally negotiated PPAs will set contract-specific prices subject to Commission regulatory approval.

<sup>48</sup> Term Sheet, § 5.4 and § 5.4.1 (addressing failure to meet the MW Target); § 6.9 (addressing failure to meet the GHG Targets).

and the Optional As-Available PPAs.<sup>49</sup> The SRAC included in the Settlement Agreement is based on the current Commission-approved SRAC pricing formula<sup>50</sup> and achieves the Commission goal of ultimately transitioning to a market heat rate to determine SRAC by January 1, 2015.<sup>51</sup> There is a long history of setting SRAC prices through settlements. The Settlement Agreement resolves this very contentious issue through an arms-length negotiation among adverse parties. As a result, the established SRAC prices are reasonable and in the public interest.

Finally, the Settlement Agreement includes capacity prices that have already been approved by the Commission in D.07-09-040 or are already incorporated in existing contracts.<sup>52</sup>

### **5. The QF/CHP Targets Are Appropriate.**

The Settlement establishes MW Targets for each IOU.<sup>53</sup> These MW Targets are the result of heated and protracted negotiations among parties with divergent interests. The CPUC has recognized that a settlement of contested issues among parties with divergent interests is reasonable and in the public interest. In addition, the Settlement Agreement establishes a GHG Target for all Commission-jurisdictional LSEs. These targets are consistent with the CHP targets included in CARB's Scoping Plan, but can also be adjusted to reflect changes by CARB in CHP targets for GHG emissions reductions and if there is a lack of need is asserted by an IOU and determined by the Commission.<sup>54</sup>

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<sup>49</sup> *Id.*, § 10.1.

<sup>50</sup> D.07-09-040 at p. 67; Resolution E-4246 (issued July 10, 2009) (adopting Market Index Formula).

<sup>51</sup> D.07-09-040 at p. 68 (indicating intent to transition from administrative heat rates to market heat rates).

<sup>52</sup> *See e.g.*, Term Sheet, § 3.2.1 (capacity pricing for Transition PPAs); § 4.6.2.2 (capacity pricing for Optional As-Available PPA); and § 11.1 (capacity prices for existing Legacy PPAs).

<sup>53</sup> Term Sheet, § 5.

<sup>54</sup> *Id.*, §§ 6.7 (addressing changes to CARB CHP targets); 6.9.3 (lack of need as a justification for not meeting the GHG Targets).

**6. The Semi-Annual Reports And CHP Auditor Process Are Consistent With Commission Policies Supporting Greater Public Information And Transparency.**

The Commission has encouraged transparency in RFO and procurement processes.<sup>55</sup> The Settlement Agreement includes several provisions that promote transparency. First, Commission-jurisdictional LSEs are required to submit semi-annual reports concerning their progress toward achieving the MW Targets and GHG Targets.<sup>56</sup> The Settlement Agreement contains detailed requirements for the type of information to be included in the semi-annual reports. This will provide the Commission and interested parties with information concerning the progress of the QF/CHP Program, and will provide this information with sufficient frequency that the Commission will have an opportunity to address issues and concerns as they arise, rather than waiting until the end of the program to address these issues.

Second, the Settlement Agreement provides for a CHP Auditor to be used for the CHP RFOs if an IOU does not or anticipates that it will not meet its MW Targets or GHG Targets.<sup>57</sup> The CHP Auditor provisions provide the auditor with access to confidential IOU information, to review the CHP RFO process, while including appropriate safeguards to prevent the disclosure of confidential information. The CHP Auditor can review the results of the IOU CHP RFOs, and raise any concerns about the RFOs to the Commission or the Energy Division. This provides an additional level of transparency in the implementation of the QF/CHP Program.

**7. The *Pro Forma* PPAs and Legacy QF PPA Amendment.**

The Commission has previously approved the use of *Pro Forma* PPAs for QFs, as well as for use in RFOs for conventional and RPS resources. The Settlement Agreement includes the

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<sup>55</sup> See e.g. D.07-12-052 at pp. 148-151 (discussing transparency in RFO process).

<sup>56</sup> Term Sheet, § 8.

<sup>57</sup> *Id.*, § 9.

following four *Pro Forma* PPAs that were developed for specific circumstances and a *Pro Forma* Legacy QF PPA Amendment for each IOU:

- Legacy QF PPA Amendment -- These *Pro Forma* Amendments offer QFs under unexpired Legacy QF PPAs as of the Settlement Effective Date (“Legacy QFs”) the option of amending the energy payment terms of their QF PPAs by selecting one of several payment options and executing the Legacy Amendment within 180 days of the Settlement Effective Date.
- Transition PPA – This *Pro Forma* PPA offers an existing CHP facility whose existing QF PPA or extension thereof is scheduled to expire prior to 2015 the option to continue existing deliveries until July 1, 2015.
- CHP RFO PPA – This *Pro Forma* PPA will be issued in the CHP RFOs to procure deliveries from CHP and other eligible generators larger than five (5) MW.
- Optional As-Available CHP PPA – This *Pro Forma* PPA offers gas-fired CHP facilities with nameplates greater than 20 MW, but annual average deliveries less than 131,400 MWh, the option to make as-available deliveries to meet criteria specified in the Settlement Agreement.
- PPA for QFs of 20 MW or Less – This *Pro Forma* PPA offers QFs of 20 MW or less, including small power producers and renewable energy resources, the option to make firm or as-available sales to the IOUs.

a. **Legacy QF PPA Amendments.**

The Legacy PPA Amendments allow a QF under a currently effective PPA, excluding those executed in the Renewable Portfolio Standard (“RPS”) program, to amend the energy price formula by selecting one of the defined energy pricing options within 180 days of the effective date of the Settlement Agreement. Each of the energy price options is generally based on the SRAC energy pricing structure established by the Settlement (“Settlement SRAC”), as described in Section II.J, above. The energy pricing options differ in terms of the negotiated heat rates and the risk assumed by Seller for the recovery of GHG costs:

- **Option A:** Option A is identical to the Settlement SRAC pricing structure described in Section II.J, above.

- **Option B:** Option B employs the same formula for calculating the energy price as used for Option A. However, the negotiated heat rate is higher than Option A until it becomes market-based in 2015 and GHG compliance costs are the responsibility of the Seller.
- **Option C1:** The Seller's selection of Option C1 triggers a 90-day negotiating period, following the Amendment Effective Date, where parties may agree to a tolling agreement pursuant to which Seller will cause the generating facility to be dispatchable, and Buyer will purchase dispatchable electricity. If Option C1 is selected, the Seller must check a fallback option which shall apply in the absence of a Tolling Agreement.
- **Option C2:** In addition to making energy payments to the Seller based on a negotiated heat rate that is 265 Btu/kWh lower than in Option B, in the event of a cap-and-trade GHG control program is established, the Buyer will make payments of \$20 per metric ton ("MT") to Seller based on a fixed emission rate for GHG compliance costs. In exchange, the Seller is solely responsible for all GHG compliance costs.
- **Option C3:** The energy pricing terms of C3 are identical to those of C2, except that GHG costs are based on facility-specific emissions, capped at Base Year emissions, and an allowance price capped at \$12.50/MT. Annual heat rates are identical to those in Option C2.

The availability of the Legacy QF PPA Amendments is subject to the Commission Approval of the Settlement Agreement and FERC approval of the California IOUs' request to waive the PURPA must-take procurement obligation. This *Pro Forma* amendment incorporates the Joint Parties' settlement of the SRAC pricing issues and offers QFs flexibility to manage the risk of GHG compliance cost.

#### b. **Transition PPA.**

The Transition PPA is available to CHP facilities currently selling to an IOU under a Legacy PPA or an extension thereof that is due to expire during the Transition Period. A CHP facility may only enter into a Transition PPA with the same IOU that it currently delivers electricity to under a Legacy PPA or an extension thereof. The term of the Transition PPA begins upon the expiration of the CHP facility's existing PPA and may be terminated upon 180 days' notice when a CHP facility has executed a PPA resulting from either a solicitation or

bilateral negotiation. The Seller may provide firm, as-available, or both forms of capacity. The Transition PPA provides firm capacity payment at the rate of \$91.97/kW-yr and as-available capacity payment at \$41.22/kW-yr escalating annually. Energy is priced at the Settlement SRAC.

The Transition PPA requires a delivery schedule, the installation of a CAISO-approved meter within 180 days of contract execution, and agreements to curtail power production upon notification of CAISO or transmission owner instruction.

Although deliveries are generally limited to historic levels under the Legacy PPA, both capacity and energy levels may be modified, provided that any CHP facility modification does not increase the Buyer's GHG costs. Certain CHP facilities with unique operational constraints may negotiate an amendment to the Transition PPA to deliver a standard additional capacity product that meets Commission and /or CAISO requirements for resource adequacy and CAISO protocols.

**c. CHP RFO PPA.**

The CHP RFO PPA is used to solicit competitive offers from certain CHP generators. Within 90 days of the Settlement Effective Date, each IOU will initiate a CHP RFO and issue this CHP RFO PPA to establish the terms and conditions by which existing, new or expanded CHP facilities located within California may offer to sell firm or as-available capacity to the IOU.<sup>58</sup> To be eligible to participate in the CHP RFO, the CHP facility must, among other things, be larger than five (5) MW, must meet the definition of "cogeneration" under Cal. Pub. Util. Code §216.6, must satisfy the Emissions Performance Standard established by Cal. Pub. Util. Code §8341, and must satisfy the definition of "cogeneration facility" under 18 CFR §292.205. Utility Prescheduled Facilities are also eligible to bid into the CHP RFO

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<sup>58</sup> The same CHP RFO PPA will be used in subsequent CHP solicitations as well.

Under the CHP RFO PPA, the delivery term for existing facilities and expanded facilities that elect not to satisfy the credit and collateral requirements of the RFO is up to seven (7) years; for new, repowered or expanded facilities that elect to meet the credit and collateral requirements in the RFO, the term is up to 12 years. Terms in the CHP RFO PPA may be modified on a bilateral basis during negotiations for a particular CHP PPA. If the Seller's offer is accepted, the offer will establish the terms of the PPA.

**d. Optional As-Available CHP PPA.**

The As-Available CHP PPA is one of several commercial alternatives available to new, existing, or repowered gas-fired CHP facilities with nameplates greater than 20 MW that meet certain requirements, including the following: the CHP facility's average annual deliveries may not exceed 131,400 MWh; the project host(s) must consume at least 75% of the total electricity generated by a Topping Cycle CHP Facility or at least 25% of the total electricity generated by a Bottoming Cycle CHP Facility; and for Topping Cycle or Bottoming Cycle with supplemental firing, the facility must meet a 60% efficiency standard.<sup>59</sup>

Seller will be paid an as-available capacity price set forth in Exhibit D, Section 3, and a time of delivery ("TOD") energy price set forth in Exhibit D, Section 2. If the generating facility is a new CHP facility, it must maintain Development Security and Performance Assurance in accordance with scheduled amounts or as negotiated between Seller and Buyer. Seller may terminate the Agreement if Seller's facility is selected in a competitive solicitation.

As-available capacity payments will be paid for deliveries of up to 20 MW in any hour. The Seller is required to schedule all deliveries with the IOU on a day-ahead basis sufficiently in advance to allow the IOU to schedule energy into the CAISO day-ahead market. Energy scheduled on a day-ahead basis and delivered up to 20 MW per hour will be priced at Settlement

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<sup>59</sup> There is no efficiency requirement for a Bottoming Cycle CHP Facility with no supplemental firing.

SRAC. Energy scheduled on a day-ahead basis and delivered at a rate in excess of 20 MW per hour will be priced at the MRTU Day-Ahead market PNode energy price. Unscheduled energy incremental to scheduled energy will be purchased by the IOU at the MRTU real time PNode price, while the Seller will bear CAISO charges and receive all CAISO revenues for such deliveries. The Seller may designate a delivery term of up to seven (7) years.

**e. PPA for QFs of 20 MW or Less.**

The PPA for QFs of 20 MW or Less will be available to QFs with firm or as-available capacity of 20 MW or less under the Commission's continuing PURPA program, regardless of whether the QF has submitted an offer in the CHP RFO or seeks alternative contracting options. The PPA for QFs of 20 MW or Less contains standard terms and conditions and incorporates the capacity prices established in D. 07-09-040, and employs the Settlement SRAC price for energy. There are few terms subject to negotiation. New or repowered facilities must post project development security and performance assurance.

**8. The Cost Recovery Proposal Is Reasonable And Consistent With California Law.**

The Commission has repeatedly determined that where DA and CCA customers benefit from procurement, these customers should pay their share of the procurement costs. For example, the Commission authorized the allocation of new generation resource costs to DA and CCA customers because these customers benefitted from the system reliability provided by the new generation resources.<sup>60</sup> The Commission also allocated GHG compliance costs and certain locational costs associated with CHP facilities developed under AB 1613 to DA and CCA customers because these customers benefitted from the AB 1613 program.<sup>61</sup>

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<sup>60</sup> D.06-07-029 at p. 7.

<sup>61</sup> D.09-12-042 at pp. 21-25, *aff'd*, D.10-04-055 at pp. 11-18.

Here, one of the purposes of the Settlement Agreement is to develop a QF/CHP Program that can facilitate meeting CARB’s CHP goal as specified in its Scoping Plan. The CARB CHP goal is not limited to the IOUs, but applies to all LSEs in California. Section 365.1(c)(1) of the Public Utilities Code, enacted as part of Senate Bill 695 (2009), requires this Commission to “ensure” that ESPs and CCAs “are subject to the same requirements that are applicable to the state's three largest electrical corporations under any programs or rules adopted by the commission to implement . . . the requirements for the electricity sector adopted by the State Air Resources Board.” Under the Settlement Agreement, the CARB CHP goal is equitably allocated among Commission-jurisdictional LSEs based on their respective percentage of total retail sales.<sup>62</sup> This allocation is used to establish GHG Targets for all LSEs, including the IOUs, ESPs and CCA.

As part of its decision on this Settlement Agreement, and based upon input from the parties, including ESPs and CCAs, the Commission will decide whether these entities will be required to meet their portion of the GHG Target by procuring CHP resources, which is the approach the Joint Parties prefer.<sup>63</sup> However, if the Commission determines that ESPs or CCAs are unable or unwilling to meet their portion of the GHG Targets by contracting with CHP facilities, the IOUs have agreed under the terms of the Settlement Agreement to procure CHP resources on behalf of these entities. In this case, however, ESP and CCA customers will be responsible for the costs of CHP resources procured on their behalf by the IOUs.<sup>64</sup> This is consistent with the Commission’s recent decisions on cost allocation when ESP and CCA customers benefit from IOU procurement on their behalf.

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<sup>62</sup> Term Sheet, §§ 6.2 – 6.3.

<sup>63</sup> *Id.*, § 6.3.2.

<sup>64</sup> *Id.*, § 13.1.2.2.

As an alternative to the allocation of costs for CHP resources procured on behalf of ESP and CCA customers, if these entities are required to procure their own CHP resources, then the Settlement Agreement provides for the allocation of any stranded CHP costs to future DA and CCA departing load customers.<sup>65</sup> This allocation of costs is consistent with the Commission's recent departing load cost allocation decisions.<sup>66</sup> However, because PPAs under the Settlement Agreement can have up to a 12-year duration, a condition precedent of the Settlement Agreement becoming effective is that the Commission affirmatively supersede the 10-year limitation in D.08-09-012<sup>67</sup> and determine that PPA above-market costs can be recovered from departing load customers for the entire 12-year term.<sup>68</sup>

### **9. The Settlement Resolves Numerous Pending And Anticipated Disputes.**

The Commission has a long-standing policy of supporting settlements.<sup>69</sup> “The Commission favors settlements because they generally support worthwhile goals, including reducing the expense of litigation, conserving scarce Commission resources, and allowing parties to reduce the risk that litigation will produce unacceptable results.”<sup>70</sup> In this case, rather than resolving a single dispute, the Settlement Agreement resolves numerous disputes pending at both the Commission and in the California Court of Appeal.<sup>71</sup> These disputes involve QF pricing, QF SOC terms and conditions, the amount of QF/CHP capacity included in long-term planning, retroactive SRAC price adjustments dating back to 2000, and numerous other disputes

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<sup>65</sup> *Id.*, § 13.1.1.

<sup>66</sup> *See e.g.* D.04-12-048 at pp. 56-58; D.08-09-012 at p. 37 (allocating new QF contract costs to DA and CCA departing load customers).

<sup>67</sup> D.08-09-012 at pp. 52-55 (discussing 10-year limitation).

<sup>68</sup> Term Sheet, § 16.2.5.

<sup>69</sup> D.05-03-022 at pp. 7-8; D.10-06-031 at p. 12.

<sup>70</sup> D.10-06-031 at p. 12.

<sup>71</sup> Term Sheet, § 14.

concerning the implementation of the Commission's current QF Program. The Settlement Agreement effectively resolves pending disputes by requiring the Joint Parties to either withdraw pending motions and applications, or release certain claims. In addition, the Settlement Agreement precludes the Joint Parties from raising new retroactive SRAC adjustment claims as long as certain conditions are met.<sup>72</sup> Thus, the Settlement not only resolves past disputes, but it also limits potential future disputes regarding SRAC energy prices.

The Settlement Agreement also resolves future potential disputes at FERC concerning an application by the IOUs for waiver of the PURPA purchase obligation by clearly defining what type of application the IOUs will file, and the type of disputes or filings that can be made by the CHP Representatives.<sup>73</sup> But for the Settlement Agreement, the Joint Parties would likely have expended considerable time and resources litigating at FERC the waiver of the PURPA purchase obligation.

#### **10. The Settlement Agreement Provides For Operationally Flexible Resources.**

Recognizing the amount of intermittent, renewable resources that will be added in California as a result of the RPS requirements, the Commission has recently encouraged the development of operationally flexible conventional resources to assist with renewables integration.<sup>74</sup> One of the challenges for CHP facilities is that these facilities are often operated as baseload facilities and/or need to operate consistent with the needs of a thermal host such that these facilities lack significant operational flexibility. Under the Settlement Agreement, the IOUs can contract with a limited group of existing CHP facilities that convert from a QF facility

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<sup>72</sup> *Id.*, § 14.1.1.

<sup>73</sup> *Id.*, § 15.1.

<sup>74</sup> *See e.g.* D.07-12-052 at pp. 106, 111-112, 115.

to a dispatchable generation facility.<sup>75</sup> The dispatchable generating facility is referred to in the Settlement Agreement as a “Utility Prescheduled Facility.” This aspect of the Settlement Agreement has several benefits.

First, if an existing CHP facility converts to a dispatchable facility, it gives the IOU the ability to dispatch the resource when it is needed, rather than the facility providing baseload generation or operating based on a thermal host’s needs. This is similar to the contracts the IOUs have with peaking and other existing conventional generation facilities.

Second, conversion to a dispatchable facility may ultimately result in GHG emission reductions. If an existing CHP facility operates as a baseload facility, and is not efficient, its GHG emissions may be higher than a new conventional facility or other resource options. By giving the IOU the flexibility to dispatch a facility, the utility can optimize its GHG emissions reductions by choosing to operate facilities with the lowest total GHG emissions.

#### **B. The Settlement Agreement Is In The Public Interest**

The Settlement Agreement is clearly in the public interest for a number of reasons. First, the Settlement Agreement resolves numerous pending disputes, motions and applications and will likely limit disputes in the future. As explained above, settlements of disputes benefit the public by reducing the costs and expense of litigation and conserving Commission resources. In addition, because there are pending disputes at the California Court of Appeal and likely will be disputes at FERC, the Settlement Agreement also preserves the resources of the courts and FERC.

Second, the Settlement Agreement creates a framework for a QF/CHP Program going forward that is much more closely aligned with other Commission-approved procurement processes. For example, under the Settlement Agreement, the IOUs will initiate a CHP RFO

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<sup>75</sup> Term Sheet, § 4.8.

process, which is similar to how conventional and RPS resources are now procured. The Settlement Agreement also includes *Pro Forma* PPAs, which will allow CHP developers and the IOUs to reduce transaction costs and resources, which they would otherwise be expended in the time-consuming process of negotiating individual PPAs.

Third, the Settlement Agreement will encourage the continued operation of the State's existing CHP facilities, and the development, installation and interconnection of new, clean and efficient CHP facilities in order to increase the diversity, reliability and environmental benefits of the CHP energy resources available to the State's electricity consumers.

Fourth, the Settlement Agreement creates a framework for achieving CARB's current CHP goals for the reduction of GHG emissions. GHG emissions pose a serious threat to the California economy, environment and the health and welfare of California's citizens. By providing a framework for the implementation of one aspect of the CARB Scoping Plan, the Settlement Agreement will facilitate efforts for California to meet its ambitious AB 32 goals. The Settlement Agreement encourages the retirement of existing, inefficient CHP facilities or repowering existing CHP facilities to make them more clean and efficient, and the development of new, clean and efficient CHP.

Fifth, the Settlement Agreement adopts a methodology for determining SRAC energy prices that is consistent with Commission decisions. The Settlement Agreement also provides for CHP PPA energy prices that are determined as a part of a competitive process, so that the prices accurately reflect a market price. Customers will benefit from clearly established SRAC prices, or prices determined through a competitive process. In addition, the capacity prices adopted in the Settlement Agreement have already been approved by the Commission.

Sixth, the Settlement Agreement creates a transparent procurement process. The Commission, interested parties and the public all benefit from a transparent procurement process with appropriate protections for confidential IOU information.

Seventh, the Settlement Agreement establishes clear rules for pricing and treatment of existing QF PPAs. For example, under the Settlement, QFs with existing PPAs are encouraged to provide forecasting information to the IOUs so that the IOUs can more accurately forecast QF generation. QFs also have greater certainty as the SRAC formula is clearly established rather than being subject to continued and ongoing disputes.

Finally, the Settlement Agreement provides for the equitable allocation of costs associated with the QF/CHP program to all Commission-jurisdictional LSEs.

#### **IV. THE JOINT PARTIES HAVE COMPLIED WITH THE REQUIREMENTS OF RULE 12.1(B)**

Commission Rule 12.1(b) requires parties to provide a notice of a settlement conference at least seven (7) days before a settlement is signed. On September 24, 2010, the Joint Parties notified all of the parties on the service list in these proceedings of a settlement conference and subsequently convened the settlement conference on October 7, 2010 to describe and discuss the terms of the proposed Settlement Agreement. Representatives of the Joint Parties participated in the settlement conference. After the settlement conference was concluded, the Settlement Agreement was finalized and executed on October 8, 2010.

#### **V. HEARINGS ARE NOT REQUIRED**

The Joint Parties respectfully request that the Commission approve the Settlement Agreement without evidentiary hearings as there are no disputed issues of material fact related to the Settlement Agreement that require hearings. In addition, hearings would prevent the expeditious approval of the Settlement Agreement. Should evidentiary hearings be deemed

necessary, the Joint Parties request that such hearings be held at the earliest opportunity, and concluded in a speedy and efficient manner.

**VI. TIMING FOR REVIEW OF THE SETTLEMENT AGREEMENT AND CONDITIONS PRECEDENT FOR THE SETTLEMENT AGREEMENT TO BECOME EFFECTIVE**

In a separate Motion for Expedited Consideration, which is being filed concurrently with this Motion, the Joint Parties have requested the Commission expeditiously review and approve the Settlement Agreement. Expeditious review and approval of the Settlement Agreement will allow the IOUs to proceed with filing of the FERC application described in Section 15 of the Settlement Agreement and to obtain written support from CARB. FERC approval of an application for termination of the PURPA purchase obligation and CARB written support are conditions precedent to the Settlement Agreement becoming effective. However, because the IOUs cannot file an application at FERC until after the Commission approves the Settlement Agreement,<sup>76</sup> expeditious review of the Settlement Agreement by the Commission is a necessary first step in satisfying all of the conditions precedent.

One of the conditions precedent for the Settlement Agreement to become effective is a Commission decision approving the Settlement Agreement “as submitted for approval without revisions unacceptable to any Party or in an alternative form that is acceptable to all Parties.”<sup>77</sup> The Joint Parties strongly urge the Commission to adopt the Settlement Agreement as is, without modification, and to select one of the two identified options for participation by ESPs and CCAs and their customers. If a Commission decision proposes modifications to the Settlement Agreement, the Joint Parties will then need to review and agree to the modifications before the condition precedent of Commission approval is satisfied. Given that it has taken the Joint Parties

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<sup>76</sup> Term Sheet, § 15.1.6.

<sup>77</sup> *Id.* at § 16.2.2.

more than a year and a half to negotiate the Settlement, and the Settlement Agreement involves a complex series of compromises and agreements, a Commission modification of the Settlement Agreement is likely to result in months of additional delay and may ultimately result in the Joint Parties being unable to agree to the modifications and the Settlement Agreement terminating. In light of the substantial benefits of the Settlement Agreement, the Commission should approve the Settlement Agreement as is, without modification, to avoid further delay negotiating the modifications or, potentially, termination of the Settlement Agreement as a result of the proposed modifications being unacceptable to the Joint Parties.

The Joint Parties are proposing in their Motion for Expedited Consideration the following schedule for consideration of the Settlement Agreement:

<b>Event</b>	<b>Dates Per The Commission's Rules</b>	<b>Proposed Dates</b>
Motion for Approval of Settlement Agreement		Filed October 8, 2010
Comments on Motion for Approval of Settlement Agreement (Rule 12.2.)	November 8, 2010	October 25, 2010
Reply Comments on Motion for Approval of Settlement Agreement (Rule 12.2.)	November 23, 2010	November 1, 2010
ALJ's Proposed Decision (Rule 14.2.)		November 16, 2010
Comments on Proposed Decision (Rule 14.3(a).)	20 days after Proposed Decision	December 6, 2010
Reply comments on Proposed Decision (Rule 14.3(d).)	5 days after opening comments on Proposed Decision	December 13, 2010
Commission vote on Proposed Decision		December 16, 2010

## VII. CONCLUSION

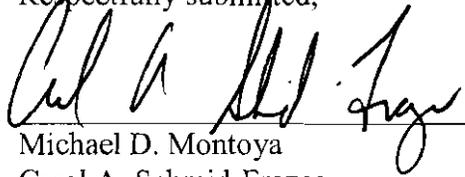
As demonstrated above, the Settlement Agreement is reasonable in light of the whole record, consistent with law, and in the public interest. Thus, the Joint Parties respectfully request that the Commission: (1) approve the Settlement Agreement without modification; (2) approve the *Pro Forma* PPAs attached to the Settlement Agreement without modification; and (3) determine that the decision approving the Settlement Agreement supersedes certain existing Commission decisions identified in Sections 16.2.4, 16.2.5 and 16.2.6 of the Settlement Agreement.

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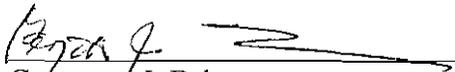
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Respectfully submitted,



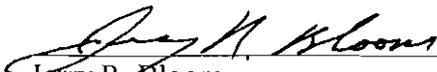
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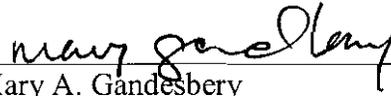
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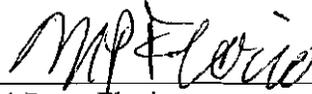
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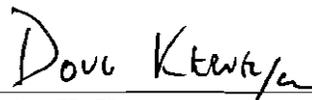
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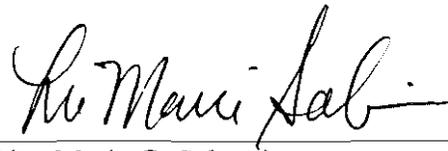
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October 8, 2010