



BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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Application of PACIFIC GAS AND ELECTRIC COMPANY for Review of Entries to the Energy Resources Recovery Account (ERRA) and Compliance Review of Electric Contract Administration, Economic Dispatch of Electric Resources, and Utility Retained Generation Fuel Procurement Activities for the Record Period of January 1 through December 31, 2005. (U 39 E)

A.06-02-016

**OPENING BRIEF
OF THE DIVISION OF RATEPAYER ADVOCATES**

Pursuant to Rule 75 of the Commission's Rules of Practice and Procedure, the Division of Ratepayer Advocates ("DRA") hereby submits its Opening Brief in the above-captioned proceeding. On February 15, 2006, Pacific Gas and Electric Company ("PG&E") filed an application for approval of its contract administration, least cost dispatch, and other procurement activities during the record period January 1, 2005 through December 31, 2005 for the Energy Resource Recovery Account ("ERRA"). In this brief, DRA will discuss the following issues:

1. Whether the Commission should authorize a disallowance on PG&E for not achieving least cost dispatch on December 26, 2005?
2. Whether the Commission should require PG&E to participate in a benchmarking study to establish appropriate operating standards for PG&E's hydro portfolio?
3. Whether the Commission should adopt certain procedures for the future treatment of contract amendment and/or modifications?

4. Whether confidential treatment as proscribed by D.06-06-066 is applicable to PG&E's current application?
5. Whether the 2005 trigger amount is applicable in the current proceeding?

I. THE COMMISSION SHOULD AUTHORIZE A DISALLOWANCE ON PG&E'S RELATED TO ITS FAILURE TO ACHIEVE LEAST COST DISPATCH ON DECEMBER 26, 2005

DRA's Report recommends the Commission authorize a disallowance on PG&E based on its failure to achieve least cost dispatch on December 26, 2005. (Exhibit D, DRA Prepared Testimony, p. 1-2, ln. 23-25.) DRA believes PG&E made an extra conservative decision to defer the sales of its long position to the hour-ahead ("HA") market, thus resulting in additional costs to the ratepayers. For deviating from least cost dispatch requirements, DRA suggests the Commission approve a \$263,000 disallowance.

A. The Potential Curtailment of Diablo Canyon Was Contrary to PG&E's Own Estimate on Availability

PG&E argues it followed least cost dispatch process using professional judgment to supplement the optimization analysis due to the uncertainties cited in trading five days early. (Ex. B, PG&E Rebuttal Testimony, p. 2-5, ln. 1-3.) PG&E indicates that on the onset of day-ahead ("DA") trading, December 21st, Diablo Canyon was curtailed due to weather. (Ex. B, PG&E Rebuttal Testimony, p. 2-5, ln. 8-9.) PG&E decided to defer sales of its long position to the HA market because of potential curtailment of Diablo Canyon due to possible high swells. (Ex. D, DRA Prepared Testimony, p. 5-5, ln. 26-28.) But in fact, Diablo Canyon was assumed fully available for December 26th. (Ex. D, DRA Prepared Testimony, p. 5-5-, ln. 14-15.) In its initial analysis, PG&E determined it could sell a certain amount of MW for the entire 24 hour period. (Ex. B, PG&E Rebuttal Testimony, p. 2-5, ln. 5.) A subsequent run later revealed a recommendation to sell a number of MW for 24 hours, while still assuming that Diablo Canyon was available. (Ex. B, PG&E Rebuttal Testimony, p. 2-5, ln. 5-6.) Despite these analyses, PG&E chose not to sell power in the DA market. (Ex. B, PG&E Rebuttal Testimony, p. 2-5, ln. 9-10.) PG&E then maintains that a short time after trading was concluded, Diablo Canyon was

assumed fully available. (Evidentiary Hearing, Reporter's Transcript, p. 15, ln. 1-12.) Based on this information, DRA disagrees with PG&E that its decision to defer to the HA market was the "optimum recommendation." Accordingly, PG&E faulty judgment resulted in additional costs to the ratepayers.

B. PG&E Incurred a Cost of Approximately \$265,000 for Deviating From Least Cost Dispatch Requirements

PG&E could have sold a standard light load product during DA trading, but it opted instead to defer to selling any long position in the HA market. (Ex. D, DRA Prepared Testimony, p. 5-5, ln. 18-21.) DRA has calculated a modest disallowance based on PG&E's first estimate of potential day-ahead sales during low load hours for December 26, 2005. (Ex. D, DRA Prepared Testimony, p. 5-6, ln. 5-7.) For its calculation, DRA used only 8 hours out of the 24 hour strip. (Ex. D, DRA Prepared Testimony, p. 5-6, ln. 9-10.) The calculation took the difference between the lower range of day ahead prices recorded on ICE and an estimated average light load HA sale price. (Ex. D, DRA Prepared Testimony, p. 5-6, ln. 8-9.) As a result, DRA arrived at an estimate of a cost to ratepayers of \$263,000 due to PG&E's deviation from least cost dispatch requirements. (Ex. D, DRA Prepared Testimony, p. 5-6, ln. 10-12.) Accordingly, the Commission should authorize a disallowance on PG&E for this cost.

II. UTILITY RETAINED GENERATION: PG&E'S PROPRIETARY HYDRO MODELS.

In its Report on PG&E's 2005 ERRAs activities, DRA staff also recommended that PG&E's in-house hydro models be: (1) benchmarked relative to an industry peer group; or (2) evaluated by an independent auditor. (Ex. D, DRA Prepared Testimony, p. 2-3, lines 11-12; and p. 2-4, lines 19-20.)

DRA staff requests the Commission order PG&E to participate in either activity. Our recommendation is based on the following factors:

A. DRA’s Recommendation is Consistent with the Commission’s Procurement Directives on Investor-Owned Utility Procurement.

In D.03-12-062, the Commission stated its three primary oversight responsibilities in short-term risk management policy: “(1) to specify the interim level of CRT; (2) to make sure each IOU has *accurate and transparent tools* place to measure ratepayer risk exposure; and (3) to review and adopt utility procurement plans.” (D.03-12-062, FOF 12, emphasis added.)

In that decision, the Commission further endorsed the principle of transparency in IOU procurement activities, stating:

While we continue to believe that it is unwise to be overly prescriptive in directing utility risk management practices, we need to balance our preference for an “even-handed” treatment on procurement policy with an emphasis on transparency and consistency in risk management reporting. (D.03-12-062, pp. 13-14.)

DRA’s recommendation is fully consistent with the Commission’s directives on transparency in IOU procurement processes. Logically, the principle of transparency must apply to all aspects of the IOUs procurement process— modeling, risk measurement and reporting, and other practices.

DRA is not opposed per se to the concept of a proprietary or in-house modeling process. However, we wish to ensure that the standards and assumptions on which the models are based are consistent with industry practice and with commercially-developed models. A model audit will provide DRA and Commission staff with a degree of certainty that these standards have been met. Further, it will confirm that dispatch decisions on behalf of PG&E ratepayers are based on a set of assumptions and factors consistent with those executed on behalf of other utility ratepayers. A benchmarking exercise would confirm to DRA and Commission staff that PG&E’s hydro operations are viable, relative to its industry peers. Either mechanism provides DRA staff with the assurance that PG&E is meeting the AB57 standard in its dispatch decisions. As a result, we can reasonably analyze these decisions as part of the ERRA review.

B. Complex Regulatory Requirements Governing Dispatch Decisions May Require More Transparency In Modeling Processes.

The IOUs' resumed responsibility for procurement following California's energy crisis of 2000-01. In the aftermath of this crisis, the Commission established procurement directives consistent with the mandate of AB57. This was to ensure that IOUs follow a "least-cost, best-fit" approach to portfolio risk management. Commission directives regarding the scope and nature of AB57 compliance has been refined over the years. For example, in D.04-07-028 (Interim Opinion on Reliability), the Commission clarified that AB57 includes reliability, among other criteria.¹ DRA believes that changes in the regulatory and market landscape after the crisis have made the dispatch decision – and the mix of elements underlying that decision – more complex. This complexity further underscores the need for more transparency in modeling, to ensure that the IOUs effectively comply with the AB57 mandate.

C. DRA's Benchmarking Recommendation Will Help To Ensure That PG&E Ratepayers Are Protected From Overall Risk On The Same Basis As Other California Ratepayers.

The Commission debate regarding the need for transparency in IOUs modeling processes is not new. DRA has voiced its concerns that the three IOUs should adhere to the principle of transparency in their procurement activities. Our concerns are not limited to PG&E, nor are our comments limited to the ERRA proceeding. Indeed, in D.03-12-062, SCE proposed that the Commission approve a proprietary model that it had developed. DRA² objected on the basis that at that time, the model was not in its final stage, and therefore not ready for Commission approval or consideration. DRA also stated its concerns that ratepayers should not have to pay for development of this model.

¹ Such as environmental, safety, and cost factors to be incorporated into the dispatch decision.

² Then known as the Office of Ratepayer Advocates (ORA).

The Commission stated its concern that proprietary modeling not compromise ratepayer risk [and concomitant costs]:

We recognize the importance of standardized risk reporting in order to measure ratepayer risk on an “apples-to-apples” basis and to ensure that utility procurement decisions will benefit all IOU ratepayers in an equitable and unbiased manner.
(D.02-12-062, p. 14)

An independent audit or benchmarking study will help to ensure that PG&E ratepayers are protected from market risks to the same extent as other California ratepayers.

D. The Cost of an Audit or Benchmarking Study should be recovered in the GRC.

DRA recommends that the Commission order PG&E to either participate in a benchmarking study or to submit their in-house hydro models for independent audit. (Ex. D, DRA Prepared Testimony, p. 203, ln. 21-22.) The benchmarking study will reassure Commission and DRA staff that PG&E models are viable, relative to its counterparts. The audit will also confirm the PG&E modeling process is viable, relative to commercially available models. Either process provides the Commission and DRA with the transparency needed to ensure that PG&E complies with AB57 and can undergo ERRRA review.

In D.02-12-062, the Commission provided SCE with guidance on how the costs of its model could get ratemaking treatment. In that decision, the Commission conditionally approved the IOUs efforts in developing the model, and directed that rate recovery, for a model that gets an unqualified audit, take place in the General Rate Case (GRC) proceeding. The Commission stated, “An unqualified model certification will serve as the basis for authorizing the model. In the event that the model is not successfully validated, SCE and Energy Division staff will agree on the use of a commercially available risk measurement model. Cost recovery for this validated model shall be sought through the General Rate Case (GRC) process, the same as all procurement administration expenses.” (D.02-12-062, p. 14)

In the instant proceeding, PG&E has already developed its hydro, in-house models. (Ex. B, PG&E Rebuttal Testimony, p. 2-7, ln. 13.) Therefore, the question is the criteria which would qualify the costs of either a model audit or benchmarking study for ratemaking treatment:

The costs of an unqualified model audit should be incorporated into PG&E's General Rate Case proceeding following audit determination. As explained in D.04-12-048, an unqualified certification should not mean that the model be proven infallible. The Commission noted: "We are simply seeking an independent review of the internal validity of the model that all the features of the model work as advertised, that the model is mathematically sound and that the assumptions utilized by the model are reasonable." (D.04-12-048, p. 109, Conclusion of Law 40.) This is the standard the Commission imposed on SCE's in-house model; DRA believes it is appropriate for PG&E's auditing process, as well.

The costs of a "successful" benchmarking study should be incorporated into PG&E's General Rate Case proceeding following completion of that study. "Successful" means that PG&E will perform on par with or better than its industry peers in the majority of the comparators indicated in the study. The scope and comparators of the study may vary, depending on the consultant contracted and the peer industry group.³ DRA should receive a copy of the study's prospectus or outline for review and approval, interim or progress reports of the study, as well as a copy of the final report, with results and recommendations.

III. THE COMMISSION SHOULD FIND THE PROCUREMENT TRANSACTION QUARTERLY COMPLIANCE REPORT FILING IS THE NOT PROPER FORUM FOR REVIEW OF CONTRACT AMENDMENTS AND MODIFICATIONS

In its application, PG&E reported it executed Power Purchase Agreement ("PPA") modifications and amendments to six QF contracts. (Ex. A, PG&E Prepared Testimony,

³ DRA staff recommended the HJA methodology, but may agree to other consulting methodologies, as and when proposed by PG&E.

p. 5-6, ln. 6.) However, PG&E indicated it is not requesting approval of the five modifications/amendments agreements in the ERRA application, since these agreements were submitted for approval in the Procurement Transaction Quarterly Compliance Report filed with the Commission. (Ex. D, DRA Prepared Testimony, p. 3-4, ln. 12-13.)

DRA's Report found PG&E's administration and management of QF contracts and its related costs reasonable. (Ex. D and 3, DRA Prepared Testimony, p. 3-8, ln. 12-13.) However, DRA recommends any future contract amendments and/or modifications be reviewed either through the ERRA application, a separate application, or advice letter process—not through the Procurement Transaction Quarterly Compliance Reports. (Ex. D, DRA Prepared Testimony, p. 3-8, ln. 13-17.) DRA describes its reasoning below:

[T]he the procurement quarterly compliance filing through Advice Letter is not the proper forum for the review and approval of contract amendments and modifications. The Commission indicated the Procurement Transaction Quarterly Advice Letter process is used mainly for tracking purposes; its objective is limited to procurement plan compliance: “The Commission’s Energy Division should review the transactions to ensure the prices, terms, types of products, and quantities of each product conform to the approved plan.”⁴ Moreover, the Commission concluded, “Consistent with AB 57, any transaction submitted by advice letter that is found to not comport with the adopted procurement plan *may be subject to further review*.”⁵ Based on the following, DRA recommends any future contract amendments/modifications be reviewed through the ERRA, through an exclusive application or exclusive advice letter process, rather than pursue approval through the established Procurement Transaction Quarterly Compliance Reports that PG&E filed as an Advice Letter.” (Ex. D, DRA Prepared Testimony, p. 3-5, ln. 17 to 3-6, ln. 6.)

DRA does not recommend an “alternative process” for the review of QF contract amendments and modifications. (Ex. B, PG&E Rebuttal Testimony, p. 1-6, ln. 5.)

⁴ D.02-10-062, p. 73; Conclusion of Law 7.

⁵ *Id* (emphasis added).

Rather, DRA proposes the Commission prohibit PG&E from requesting approval of its contract amendments and/or modifications through the Procurement Transaction Quarterly Compliance Reports—all other methods of requesting approval (whether through the annual ERRA compliance application, a separate application, or advice letter process) are available at PG&E’s discretion. It is a customary IOU practice to seek approval of its activities through an application or advice letter as appropriately required by the Commission. Accordingly, DRA’s recommendation does not constitute an after-the-fact reasonableness review of contract terms, as prohibited by Section 454.5(d)(2).

PG&E’s Rebuttal Testimony further states, “PG&E has over 300 QF contracts, and contract amendments / contract modifications happen frequently. It would be inefficient to hold these for review and approval until the annual compliance application.” (Ex. B, PG&E Rebuttal Testimony, p. 1-6, ln. 29-30.) Given that PG&E is not limited to seek approval through the ERRA compliance review application, and has only *five* contract amendments and modifications during the current record period, DRA believes its recommendation is not burdensome to the utility.

IV. THE COMMISSION SHOULD IMPLEMENT THE PROCEDURES FOR CONFIDENTIAL TREATMENT AS OUTLINED IN DECISION 06-06-066

On March 3, 2006, the *Administrative Law Judge Ruling on Motions for Leave to File Under Seal and Approval of a Protective Order* (“March 3 Ruling”) granted PG&E’s motion for leave to file under seal certain information pertaining to its current 2006 ERRA compliance review application.⁶ The March 3 Ruling indicated such information includes PG&E’s use of utility retained generation resources, energy under PG&E contracts, Department of Water Resources contracts allocated to PG&E, management of

⁶ Public Utility Code Section 454.5(g) requires the Commission to ensure the confidentiality of any market sensitive information submitted in procurement plans and related submissions. The statute requires confidential treatment of “an electrical corporation’s proposed procurement plan or resulting from or related to its approved procurement plan, including, but not limited to, proposed or executed power purchase agreements, data request responses, or consultant reports, or any combination.” Pub. Util. Code § 454.5(g).

surplus energy, acquisition of power to meet the residual net short positions, and hedging activities. (March 3 Ruling, p. 1.)

Since the issuance of the March 3 Ruling, the Commission has addressed the protection of confidential information, as proscribed D.06-06-066, the *Interim Opinion Implementing Senate Bill No. 1488, Relating To Confidentiality Of Electric Procurement Data Submitted To The Commission*. This decision, with its attached “Matrix of Allowed Confidential Treatment,” is applicable in the current proceeding. In D.06-06-066, the Commission explains the new procedure: “Because IOUs must show that information they seek to keep confidential could have a material impact on their market price for electricity, only data in the Matrix that meet this definition may be held in confidence.” (D.06-06-066, p. 43.) Accordingly,

When a party seeks protection for data already contained in the Matrix, its burden should be to prove that the data match the Matrix category, that the information is not already public and that it cannot produce the data in masked or aggregated form. Once it does so, it is entitled to the protection the Matrix provides for that category. (D.06-06-066, COL #6, p. 77.)

Decision 06-06-066 and its accompanying Matrix also describes the applicable window of confidentiality afforded for market sensitive information. (D.06-06-066, p. 43; Appendix 1.)

V. 2005 TRIGGER AMOUNT

During the Evidentiary Hearing conducted on July 17, 2006, ALJ Michael J. Galvin requested the parties identify the 2005 trigger amount applicable. Section 454.5(d)(3) identifies the “trigger amount” as any overcollection or undercollection in the power procurement balancing account that does not exceed 5 percent of the electrical corporation’s actual recorded generation revenues for the prior calendar year excluding revenues collected for the DWR. DRA understands the 2005 trigger amount (if applicable) is addressed in a separate advice letter or application filed by PG&E, and no information regarding this amount has been provided in the current proceeding.

VI. CONCLUSION

WHEREFORE, DRA respectfully requests the Commission to:

(1) authorize a disallowance on PG&E for \$263,000 for deviations from least cost dispatch requirements on December 26, 2005,

(2) order PG&E's in-house hydro models be benchmarked relative to an industry peer group, or evaluated by an independent auditor;

(3) hold future contract amendments and/or modifications be reviewed through the ERRR application, or through an application or advice letter process other than the Procurement Transaction Quarterly Compliance Reports; and

(4) find Decision 06-06-066, with its attached "Matrix of Allowed Confidential Treatment," is applicable in the current proceeding.

Respectfully submitted,

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August 25, 2006

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the foregoing document “**OPENING BRIEF OF THE DIVISION OF RATEPAYER ADVOCATES**” in **A.06-02-016.**”

A copy was served as follows:

BY E-MAIL: I sent a true copy via e-mail to all known parties of record who have provided e-mail addresses.

BY MAIL: I sent a true copy via first-class mail to all known parties of record.

A hard-copy has been provided to Administrative Law Judge Galvin.

Executed in San Francisco, California, on the 25TH day of August 2006.

/s/ ANGELITA MARINDA
Angelita Marinda

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