Decision **ALTERNATE PROPOSED DECISION OF COMMISSIONER BOHN**
(Mailed 11/2/2010)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for Approval of 2008 Long-Term Request for Offer Results and for Adoption of Cost Recovery and Ratemaking Mechanisms (U 39 E).	Application 09-09-021 (Filed September 30, 2009)

DECISION AUTHORIZING PACIFIC GAS AND ELECTRIC COMPANY TO ENTER INTO A PURCHASE AND SALE AGREEMENT WITH CONTRA COSTA GENERATING STATION LLC

1. Summary

In Decision (D.) 10-07-045 we granted, in part, the application of Pacific Gas and Electric Company (PG&E) for approval of its 2008 Long-Term Request for Offer results and adopted a cost recovery and ratemaking mechanism related thereto. In particular, we approved PG&E's Marsh Landing, Contra Costa 6 & 7, and Midway Sunset procurement agreements. D.10-07-045 also approved a multi-party settlement agreement providing for recovery of the costs associated with the above procurement. However, D.10-07-045 did not approve a purchase and sale agreement for the Contra Costa Generating Station in Oakley, California, (Oakley Project) a new natural gas-fired combined cycle facility that

was expected to produce 586 megawatts of generation at July peak conditions beginning June 4, 2014.[1]

On August 23, 2010, PG&E filed a Petition for Modification (PFM) of D.10-07-045 that sought to modify D.10-07-045 to approve the Oakley Project. This decision denies PG&E's PFM of D.10-07-045, finding a PFM to be an improper procedural vehicle for this request. However, due to the unique opportunity presented by an Oakley Project that can come on-line in 2016, the Commission has sua sponte considered PG&E's filing as an application for approval of the project.

2. Procedural Background

In Decision (D.) 07-12-052, the Commission approved the three investor-owned utilities' (IOU) long-term procurement plans for the term 2006 through 2015 and authorized Pacific Gas and Electric Company (PG&E) to procure 800 – 1,200 megawatts (MW)[2] of new capacity by 2015. PG&E was authorized to issue requests for offers (RFOs) to obtain and execute long-term power purchase agreements (PPAs) for this new capacity.[3] This number was subsequently increased to 928 – 1,328 MW to adjust for previously approved projects that were to be cancelled after D.07-12-052.

In Application (A.) 09-09-021, PG&E sought approval of its 2008 Long-Term Request for Offer (LTRFO) results and adoption of a cost recovery and ratemaking mechanism related thereto. In particular, PG&E sought approval of: (1) a PPA with Mirant Marsh Landing for the net output of the Marsh Landing Generating Station, a new natural gas-fired combustion turbine

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[1] The Oakley Project was to be developed by Contra Costa LLC and purchased and operated by PG&E after the plant became operational and passed performance tests.

[2] MW values are expressed in July peak operating conditions.

[3] *See* D.07-12-052, Ordering Paragraph (OP) 4 at 300.

facility that is expected to produce 719 MW beginning May 1, 2013; (2) a PPA with Mirant Delta LLC for 18 months contingent on the closure of the Contra Costa units 6 and 7, which rely on once-through cooling technologies, at the conclusion of the PPA term;[4] (3) a purchase and sale agreement (PSA) with Contra Costa Generating Station LLC for the Oakley Project, a new state-of-the-art natural gas-fired combined cycle facility that was expected to produce 586 MW of generation beginning June 4, 2014; and (4) a PPA with Midway Sunset Cogeneration Company (Sunset) for the partial output of an existing natural gas-fired cogeneration plant that will deliver 129 MW of Qualifying Facility generation under peak July conditions for five years beginning at Commission approval, and 61 MW through September 30, 2016, when the contract expires. D.10-07-045 approved all but the Oakley Project. In denying the Oakley Project, D.10-07-045 concluded that the project was not needed at the time.[5] In a separate proceeding, PG&E sought Commission approval of power purchase agreements with GWF Energy LLC, for the Tracy Transaction (Tracy) and Calpine Corporation, for the Los Esteros Critical Energy Facility Transaction (Los Esteros) that were originally solicited through PG&E's LTRFO process.[6] These new PPAs would result in PG&E procuring 254 MW of additional new capacity. In D.10-07-042, we conditionally approved these transactions. As set forth in OP 2 of D.10-07-042:

> If the Commission rejects the proposed Marsh Landing Project and/or the Oakley Project in Application (A.) 09-09-021, Pacific Gas and Electric Company shall proceed immediately

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[4] The PPA with Mirant Delta LLC is an 18-month tolling agreement that allows PG&E to dispatch the facility as needed.

[5] D.10-07-045, at 53, Finding of Fact Number 18.

[6] *See* A.09-10-022 and A.09-10-034, filed October 16, 2009 and October 22, 2009, respectively.

> with both the Tracy Transaction described in A.09-10-022 and the Los Esteros Critical Energy Facility Transaction described in A.09-10-034.

Consistent with the language above, on August 4, 2010, PG&E filed a Tier-1 Advice Letter (AL). Copies of the executed contracts comprising the Tracy and the Los Esteros Transactions were included in PG&E's advice letter filing.

On August 23, 2010, PG&E filed a Petition for Modification (PFM) of D.10-07-045 seeking to modify D.10-07-045 to approve a revised Oakley Project. On August 24, 2010, the Division of Ratepayer Advocates (DRA) filed a protest to PG&E's AL. DRA's AL protest asked the Commission to either reject PG&E's advice letter without prejudice or suspend it and hold it in abeyance until PG&E's PFM in this proceeding is resolved. The Commission's Energy Division responded to DRA's protest on September 1, 2010. Energy Division noted that General Order (GO) 96-B, Section 7.6.1 allows it to approve an advice letter that has been protested if the protest is not made on proper grounds as set forth in General Rule 7.4.2 of GO 96-B. Energy Division denied DRA's protest on claims that the protest was improper because PG&E's advice letter was filed in compliance with OP 2 of D.10-07-042.[7]

3. Parties' Positions

3.1. PG&E's PFM

PG&E's PFM states that changed circumstances support modifying the decision to approve a revised Oakley Project. According to PG&E, the utility and Contra Costa have re-negotiated the project PSA to extend the guaranteed commercial availability date from June 1, 2014 to June 1, 2016. PG&E asserts that this amendment, which postpones for two years PG&E's obligation to take

[7] As stated in a September 1, 2010 letter from Energy Division: "Rejecting the advice letter would require Energy Division to treat rejection of the Oakley Project in D.10-07-045 as if it was invalid, in contravention of a CPUC decision."

ownership of the power plant under the PSA, represents a significant change and is consistent with suggestions made by several Commissioners at the time D.10-07-045 was issued.

3.2. Opposition to the PFM

On September 22, 2010, The Utility Reform Network (TURN), DRA, and Western Power Trading Forum (WPTF) and Alliance of Retail Energy Markets (AReM) (collectively, "opposing parties") filed comments in opposition to PG&E's PFM. Each of these parties argues that PG&E has not employed the correct procedural vehicle for bringing the Oakley Project back for Commission consideration. They rely in particular on OP 4 of D.10-07-045 which provided that:

> Pacific Gas and Electric Company may resubmit this project, via application, for Commission consideration if any of the conditions detailed in Section 3.5.6…are met.

The opposing parties argue that the PFM is an improper procedural vehicle and that none of the conditions referenced above have been met. These parties also argue that the only factual change PG&E claims in support of its PFM is misleading and at best de minimis, and should be afforded no weight by the Commission.

TURN further notes that PG&E's filing raises new factual issues and, unlike an application, a PFM deprives it and other parties of due process in the form of full discovery, presentation of testimony, evidentiary hearings, and legal briefing.

DRA argues that a PFM cannot legally modify D.10-07-045 to approve the Oakley Project because, by the terms of D.10-07-042, the denial of the Oakley Project created a vested right in two other projects, and governmental entities may not interfere with vested contractual rights. DRA further notes that the PFM seeks to relitigate PG&E's approved need as determined in D.07-12-052 and

D.10-07-045. According to DRA, the additional 586 MW associated with the Oakley Project would exceed the procurement authority granted PG&E in D.07-12-052 and OP 5 of D.10-07-045. Moreover, DRA asserts that there is no evidence in the record that the Oakley Project is needed in 2016.

For their part, WPTF and AReM add that all of PG&E's authorized need has been met with other projects that have been approved by the Commission and the Oakley Project is not needed to meet PG&E's projected bundled customer demand. WPTF and AReM further assert that any reconsideration of the Oakley Project should take place in the context of its next Long-Term Procurement Plan (LTPP) proceeding, when and if there is a determination that new resources are needed.

3.3. Support for the PFM

On September 22, 2010, the Coalition of California Utility Employees and California Unions for Reliable Energy (CUE/CURE) filed comments supporting the PFM. The comments filed by CUE/CURE provide three arguments in support of granting the PFM: (1) that the Oakley Project is economically superior to most projects bid into PG&E's 2008 RFO;[8] (2) that "the Commissioners ruled against Oakley, indicating that the Oakley Project could be approved if PG&E modified the contract to allow for a later availability date, greater flexibility, and newer technology"; (3) "PG&E has also made the showing of changed circumstances required by Rule 16.4."[9]

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[8] CUE/CURE relies on exhibits submitted by it (Exh. 300 - CUE/CURE/Marcus at 2:9-17, 13:1-9) and PG&E (Exh. 67 - PG&E Answer 2) as support for this claim.

[9] Response to PFM filed by CUE/CURE, September 22, 2010, at 1.

4. Discussion

4.1. PG&E's PFM is Rejected Because it is an Improper Procedural Vehicle to Seek Project Approval

PG&E claims to have negotiated a modification to the PSA that extends the guaranteed commercial availability date of the Oakley Project by two years, from June 1, 2014 to June 1, 2016. This two-year extension of the PSA constitutes the "changed circumstances" upon which PG&E relies in support of its PFM.

PG&E asserts that, "the modification of the Oakley Project guaranteed commercial availability date in the amendment constitutes a significant change in circumstances."[10] In contrast, opposing parties argue that the amendment to the Oakley PSA's guaranteed delivery date does not constitute a changed fact or circumstance sufficient to justify the PFM.[11] In response to this criticism, PG&E asserts that "the change in the PSA guaranteed commercial availability date is material."[12] According to PG&E "[t]his is indisputably a change in facts and circumstances because the PSA that was before the Commission in A.09-09-021, and on which the Commission based D.10-07-045, has subsequently been amended."[13] Consistent with this argument, PG&E notes that "under the original PSA, …the Oakley Project would have been on-line no later than June 1, 2014,"[14] while under the amended PSA the Oakley Project would be on-line no later than June 1, 2016.

Rule 16.4(b) requires that allegations of fact must be supported by evidence that is in the record or that is judicially noticeable and that new or

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[10] PG&E PFM at 3.

[11] TURN Comments on PFM at 3-4; DRA Comments on PFM at 6-7.

[12] PG&E Reply to Opposition at 3-4.

[13] *Id*.

[14] *Id*. at 4.

changed facts be supported by a declaration or affidavit. Providing the source for existing facts and documentation for new facts as required by Rule 16.4(b) is necessary to allow these facts to be weighed and considered when reviewing a PFM. PG&E filed the Declaration of Marino Monardi in support of the PFM. Mr. Monardi's Declaration, at 1, paragraph 3, sets forth that the on-line date was changed from no later than June 1, 2014 to no later than June 1, 2016.

Although we agree with PG&E's claim that the change in on-line date is a changed material fact that could arguably support a PFM, the PFM is denied because it is an improper vehicle to seek approval of the revised Oakley PSA. In D.10-07-045, the Commission specifically instructed PG&E that, if the Oakley Project came back before us, it should return as an application. Nevertheless, due to the opportunities and benefits associated with the project that are discussed below, the Commission has sua sponte considered PG&E's filing as an application.

4.2. Consideration of the Revised Oakley PSA

The revised Oakley Project represents a significant new opportunity that merits the Commission's consideration at this time. Many of the operational attributes of this plant were litigated in reaching D.10-07-045, as supplemented by the instant proceeding. In particular, it has been established that:

1) Oakley is a highly viable if the Commission acts today. It is expected that the financing available for this project will no longer be available if the project is not approved in 2010.
2) Oakley is highly efficient (it has a very low heat rate) and will enable California to meet increasingly stringent greenhouse gas (GHG) reduction goals. Oakley would allow for the retirement of peaking resources with high heat rates.
3) Oakley would allow for renewable integration by providing load following capabilities. The combination of

this generation attribute with a low heat rate is uncommon in the current generation fleet.

4) Oakley reduces risk that California will have an insufficient supply of generating resources due to lack of available financing for capital projects and regulatory lag.

5) Generation investment is, by its nature, not well suited to the acquisition of small incremental assets. Instead, investments are often for larger discrete units. As a result, the Commission has in the past approved projects that exceed, in their first couple of years of operation, the Commission's projections of the number of MW needed for reliability. At some point, it is likely that California will need to bring additional projects such as Oakley on-line. In the Commission's judgment, in this instance it is worth the risk of short-term over procurement to ensure that resources such as Oakley are available in the longer-term. Thus, it is reasonable to act now so that Oakley will be operational by 2016.

4.3. Oakley is an Exceptional Project, is Highly Viable, and Must Be Approved Now in Order to Be Built

The Commission's decision to deny Oakley in D.10-07-045 was in no way based on the attributes of the project. Oakley Project represents a highly viable, highly efficient and low polluting project. The Commission recognized that the Oakley Project is uniquely viable because it has nearly completed the permitting process. It is anticipated that the opportunity to bring this project to fruition will be lost, due to financing concerns, if this project is not approved in 2010.

As D.10-07-045 notes, "we understand that developing and building a power plant in California is a long process, fraught with pitfalls."[15] The turbulent economy in which we are currently situated has threatened or doomed the viability of many large capital projects that have been in the planning process for years. Power plant projects are no exception. It is very unusual for this

[15] D.10-07-045 at 40.

Commission to be presented with a viable project, which could become operational, with the same commercial terms, two years later than originally planned during project development. The merits of the operational characteristics, viability and the costs and benefits of this power plant have already been thoroughly litigated before this Commission. The Commission must act now to guarantee its construction.

4.4. Oakley's Unique Operating Characteristics Will Allow California to Meet its GHG Reduction Goals

The Commission must consider the implications of continuing to rely on resources with high heat rates to provide California with an ability to meet peak demand and to integrate renewable energy. Approving the Oakley Project will provide California with much more efficient way to meet peak demand and integrate renewable generation than much of the current generation fleet. Furthermore, the Oakley project provides load following, a highly desirable integration attribute uncommon to peaking facilities.

While arguments for and against the Oakley Project have focused on capacity need issues, there are other features of this project which make it a uniquely valuable addition to PG&E's resource mix. As noted by Commissioner Bohn,[16] the Oakley plant "has many beneficial features, including a very high efficiency and low air emission rates, and utilizes the most up to date technology from General Electric." These are exactly the type of attributes the state of California will need to help with renewable integration. In this instance, it is our view that denying approval of the amended Oakley PSA would be acting contrary to the Commission's stated goal, in D.07-12-052, of integrating renewable resources through LTPP.

[16] See Concurrence of Commissioner John A. Bohn, filed as part of D.10-07-045.

4.5. Oakley is a Hedge Against Risks Caused By Regulatory Lag

Following the Commission's approval of the IOU's long-term procurement plans in D.07-12-052, the Commission opened the 2008 long-term procurement proceeding, Rulemaking (R.) 08-02-007, for the years 2008-2018. That proceeding did not approve any new long-term procurement plans for the IOUs, but instead focused on procurement policy development and integration of renewables into the IOUs' resource portfolios. The Assigned Commissioner's Ruling and Scoping Memo, dated August 28, 2008 for R.08-02-007 stated: "to the extent the LTPP lens is focused on the seven year and greater timeframe for new plants to be built, this proceeding in some cases must infer policy objectives that have not been articulated to a level of detail required for making procurement decisions."[17] This acknowledgement of the conservative time period of seven years to build a plant is important because the procurement authority granted by the Commission in D.07-12-052 assumed that the 2010 LTPP cycle,[18] which will cover the 2011-2020 planning period, would begin in early 2009.[19] This cycle substantively commenced in December 2010, much later than anticipated. It is unlikely that any new plant to address need determined in that proceeding would come on-line before 2018. Indeed, it is reasonably likely–and therefore of concern to the Commission–that any new projects approved in the 2010 LTPP cycle might be delayed well beyond 2018.

Thus the amended Oakley Project is uniquely situated to be in place to fill this critical gap. We previously concluded that the cost of this additional insurance outweighed the benefits, if, as PG&E originally proposed, such costs

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[17] Page 5.

[18] Need determinations have not been made since D.07-12-052. The 2008 LTPP cycle did not conduct a needs determination.

[19] R.08-02-007, July 1, 2009, at 6.

were imposed upon ratepayers in 2014. On balance, however, at present we are convinced there are numerous grounds to consider approving the amended Oakley contract, with a 2016 commencement date in lieu of the original 2014 commencement date. For these reasons, we will approve the revised Oakley Project despite the fact that this authorization will result in PG&E's procurement of new generation capacity in excess of the range of need established by the Commission in D.07-12-052. This decision does not modify our determination in D.07-12-052, or reflect any determination that PG&E's immediate need for new capacity has changed.

We recognize, however, that to date it has been three years since the Commission has made a needs determination. As noted above, the 2010 LTPP is currently behind schedule. Although the Commission and its staff are working diligently to make up ground on that proceeding, it may be another year or even two before the Commission makes another new capacity needs determination for PG&E with respect to its generation resources. As a result, we are concerned there could be a gap as long as five years between need determinations. A time lapse of that duration creates substantial risk for capacity shortfalls. The Commission has, before it now, a proposed resource that would be able to come on-line precisely during the gap created by the time lapses between needs determination. It would not be prudent for Commission to turn a blind eye at an excellent opportunity to hedge the risk of any capacity shortfall by declining to consider the revised Oakley contract.

4.6. Conclusion

When the considerations discussed herein are viewed in total, in particular the benefits associated with the amended Oakley Project with the delayed on-line date, it is prudent to allow PG&E to procure the new capacity provided by the project even though this would cause PG&E to exceed the highest range of need

established by the Commission in D.07-12-052. The revised Oakley Project represents a highly viable, highly efficient and low polluting project that will effectively hedge the risks of capacity shortfalls created by the time lapse between needs determinations in the LTPP. Therefore, the project should be approved.

5. Additional Ratepayer Protection

To further protect ratepayers, the Commission will impose an additional condition on this approval: PG&E may not take ownership of the plant under the PSA prior to January 1 of 2016; or, alternatively, PG&E may take ownership only on the condition that its shareholders absorb the associated revenue requirements from the date of purchase until January 1 of 2016.

6. Comments on Alternate Proposed Decision

The alternate proposed decision of Commissioner John A. Bohn in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on _____, by and reply comments were filed on _____ by _____. The alternate proposed decision was revised to address the Parties' comments and while not required, is being reissued for additional comment by the parties. Any party wishing to submit further comment should do so by December 14, 2010.

7. Assignment of Proceeding

Michael R. Peevey is the assigned Commissioner and Darwin E. Farrar is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. PG&E and Contra Costa negotiated a modification to the Oakley Project PSA, extending the delivery date of the project from June 2014 to June 2016.

2. In D.10-07-045, the Commission directed PG&E to submit an application if future consideration and approval of the Oakley project was desired.

3. Oakley is a highly viable project if the Commission acts today. Financing for this project may no longer be available if the project is not approved in 2010.

4. Oakley is highly efficient (it has a very low heat rate) and will enable California to meet increasingly stringent GHG reduction goals.

5. Oakley would allow for the retirement of peaking resources with high heat rates.

6. Oakley would allow for renewable integration by providing load following capabilities. The combination of this generation attribute with a low heat rate is uncommon in the current generation fleet.

7. Oakley reduces risk that California will have an insufficient supply of generating resources due to lack of available financing for capital projects and regulatory lag.

8. The Commission has in the past approved projects that exceed, in their first couple of years of operation, the Commission's projections of the number of MW needed for reliability.

9. There has been no LTPP needs determination since D.07-12-052, creating a risk of capacity shortfall in 2016 and beyond.

10. The revised Oakley Project would help mitigate the risk of any capacity shortfall in 2016 and beyond that has been created by the time lapse between LTPP needs determinations.

Conclusions of Law

1. Rule 16.4(b) requires that allegations of fact be supported by evidence that is in the record or that is judicially noticeable, and that new or changed facts are supported by a declaration or affidavit.

2. Providing the source for existing facts and documentation for new facts as required by Rule 16.4(b) is necessary to allow these facts to be appropriately weighed and considered when reviewing the PFM.

3. PG&E complied with the Rule 16.4(b) requirements for a PFM through the filing of the Declaration of Marino Monardi in support of the PFM.

4. Establishing different guaranteed delivery date criteria for the Oakley Project is a unique opportunity.

5. PG&E's PFM should be denied because it is an improper procedural vehicle for the Commission to consider approval of the Oakley Project.

6. On the Commission's own motion, it may consider the request for approval of the Oakley Project as an application.

O R D E R

IT IS ORDERED that:

1. The petition of the Pacific Gas and Electric Company for modification of Decision 10-07-045 is denied.

2. Pacific Gas and Electric Company's Purchase and Sales Agreement with Contra Costa Generating Station LLC for the Oakley Project is approved subject to the condition that Pacific Gas and Electric Company may not take ownership of the plant under the Purchase and Sales Agreement prior to January 1 of 2016; or, alternatively, Pacific Gas and Electric Company may take ownership only on the condition that its shareholders absorb the associated revenue requirements from the date of purchase until January 1 of 2016.

3. Application 09-09-021 is closed.

This order is effective today.

Dated _____, at San Francisco, California.