

Decision **PROPOSED DECISION OF COMMISSIONER PEEVEY**
(Mailed 9/2/2008)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.

Rulemaking 06-04-009
(Filed April 13, 2006)

**DECISION DENYING PETITION OF
SOUTHERN CALIFORNIA EDISON COMPANY
TO MODIFY DECISION 07-01-039**

1. Summary

This decision addresses a petition filed by Southern California Edison Company (SCE) to modify Decision (D.) 07-01-039. SCE requests that D.07-01-039 be modified to state that financial contribution requirements under preexisting contractual obligations are not subject to the provisions of Senate Bill (SB) 1368. We find the requested modification to be too broad and deny SCE's request. However, we find that our definition of "new ownership investments" in D.07-01-039 was not intended to apply to the capital expenditures requested by SCE in Application (A.) 07-11-011 for Units 4 and 5 of the Four Corners Generation Station. Accordingly, these requested expenditures are not subject to the emissions performance standard under SB 1368 and SCE may seek rate

recovery of these costs in A.07-11-011.¹ This decision also directs SCE to conduct a study on future actions with respect to its ownership interest in Four Corners and to submit a report on its findings to the Commission within six months.

2. Background

Senate Bill (SB) 1368 (Stats. 2006, ch. 598), enacted in September 2006, directed the Commission to establish an interim greenhouse gas (GHG) emission performance standard (EPS) and to adopt rules to enforce this standard. On January 25, 2007, we adopted Interim Rules for Greenhouse Gas Emissions Performance Standard (Interim EPS Rules) in D.07-01-039 (Decision) pursuant to the requirements of SB 1368.² As part of the Decision, we identified those types of generation and financial commitments subject to the EPS (“covered procurements.”) We defined covered procurements to include new ownership investment in retained baseload generation “intended to extend the life of one or more units of an existing baseload powerplant for five years or more, or [that] results in a net increase in the existing rated capacity of that powerplant.”³

In its opening comments to the proposed decision that was ultimately voted out as D.07-01-039, SCE had expressed concern that the definition of “covered procurements” could impair its ability to comply with various agreements relating to its co-ownership in Units 4 and 5 of the Four Corners

¹ Although we find that the requested capital expenditures are not “new ownership investments” for purposes of complying with the EPS, we make no determinations concerning the reasonableness or necessity of the requested expenditures. These determinations shall be made in A.07-11-011.

² The Interim EPS Rules are in Attachment 7 of the Decision.

³ D.07-01-039 at p. 53.

Generation Station (Four Corners).⁴ Specifically, SCE expressed concern that the language, if adopted, could be construed to prevent SCE from making required financial investments under its Agreements to maintain Four Corners for the term of the existing contract, since Four Corners could not satisfy the EPS.⁵ Therefore, it had requested that the Commission “clarify that the EPS does not apply to contracts on existing baseload power plants or to provide an exemption for [load serving entities (LSEs)] that co-own existing generating plants with third parties with whom they have contractual obligations to pay for ongoing expenses.”⁶

The Decision rejected this request. However, it noted “If SCE anticipates that the EPS will prevent it from complying with its contractual obligations at Four Corners, it should file an application for petition for modification, together with adequate supporting information, documentation, and analysis, and request appropriate relief.”⁷

⁴ SCE owns a 48% co-tenancy interest in Units 4 and 5 of Four Corners. SCE’s rights and obligations with respect to its ownership in Four Corners are stated in various agreements (Agreements). The current Agreements between SCE and its co-owners terminate in 2016. Under the Agreements, SCE is obligated to pay its share of expenditures for capital additions, improvements and replacements. (SCE Petition, Exhibit A.) If it fails to do so, SCE states that it would not receive power from Four Corners but would remain liable for unpaid costs. (SCE Petition, Exhibit B.)

⁵ Comments of Southern California Edison Company (U338E) on The Proposed Decision of President Peevey and ALJ Gottstein, filed January 2, 2007, p. 13.

⁶ *Id.*

⁷ D.07-01-039, at p. 46.

On January 28, 2008, SCE filed *Petition for Modification of Decision 07-01-039 of Southern California Edison Company* (SCE Petition).⁸ SCE states that as part of its General Rate Case Application for Test Year 2009, A.07-11-011, it has requested authorization to recover \$178,593,000 to cover its share of capital expenditures at Four Corners. SCE states that, as written, the Decision's language concerning new ownership investment in retained baseload power could be applied in a manner that would prevent it from fulfilling this financial obligation. Consequently, it requests that the Decision be modified "to find that financial contributions required under preexisting contractual obligations for generating units owned jointly with third parties are not 'covered procurements' under the EPS."⁹

Responses to SCE's Petition were filed by the Division of Ratepayer Advocates, the Western Power Trading Forum (WPTF) the Independent Energy Producers Association (IEP) and jointly by the Natural Resources Defense Council, Union of Concerned Scientists, The Utility Reform Network, Environmental Defense Fund, Center for Energy Efficiency and Renewable Technologies and Western Resource Advocates. Although parties filing responses disagreed on whether investments in Four Corners should be exempt from the EPS, they all agreed that SCE's requested modification was too broad and should be rejected. In its reply to the responses, SCE clarified that it was not

⁸ SCE filed an amended Petition on February 13, 2008. This amended Petition corrected some minor errors, but did not modify the substance of its request.

⁹ SCE Petition, p. 5.

proposing generic relief, but rather wanted the Decision to specifically state that Four Corners is not subject to the EPS during its current contractual term.

3. Discussion

3.1. SCE's Request

SCE asserts that although the language in the Decision could be construed to apply to SCE's requested expenditures in Four Corners, the Commission did not intend to have the EPS apply to pre-existing co-ownership agreements such as Four Corners. First, SCE maintains that D.07-01-039 states that applying the EPS to required financial investments in existing facilities would "subject the millions of dollars SCE has already spent on preparing Four Corners to serve SCE's customers throughout its current term to a standard intended to affect future investment decisions."¹⁰ Additionally, SCE asserts that the Decision only intended for the EPS to be triggered by investments that would fundamentally alter the way in which an existing powerplant operates, not every required capital investment in a plant. Finally, SCE argues that under the Decision, covered procurements subject to the EPS include investments over which the LSE would have discretion and choice. As such, it contends that the EPS should not apply to its ownership in Four Corners since SCE is a minority owner and has no say over its financial obligations.¹¹ Based on these arguments, SCE requests that the definition of "covered procurement" in Attachment 7 of the Decision be modified to state:

¹⁰ SCE Petition, p. 7.

¹¹ SCE Petition, pp. 7-8.

Except for financial contributions required by existing contractual agreements (effective prior to January 25, 2007), new investments in the LSE's own existing non-Combined-cycle Gas Turbine (CCGT) baseload power plants that are: (1) intended to extend the life of one or more units by five years or more, (2) result in a new increase in the rated capacity of the powerplant, or (3) intended to convert a non-baseload plant to a baseload plant . . .¹²

All parties responding to the Petition maintain that SCE's proposed modification is too generic and would result in a blanket exemption from the EPS for all future spending required under existing contractual agreements. We agree. SCE's proposed modification is overly broad and there is a risk that if we granted the SCE Petition, other LSEs with existing contractual agreements would assert that their agreements were not "covered procurements" in order to avoid complying with the EPS. Therefore, we decline to modify D.07-01-039 as requested by SCE. However, for the reasons discussed below, we find that under the Interim EPS Rules, our definition of "new ownership investments" was not intended to apply to the situation presented in A.07-11-011. Therefore, the requested capital expenditures in Four Corners are not subject to the EPS.

Pub. Util. Code § 8341(b)(3) authorizes the Commission to "adopt rules to enforce the requirements of [Section 8341], for load-serving entities." In the Interim EPS Rules, we determined that under Section 8341(a), (b)(1), and (b)(2), "the EPS shall apply to all baseload generation in the event that the compliance requirement is triggered by a 'long-term financial commitment' as defined in § 8340(j)."¹³ Pursuant to § 8340(j), "[l]ong-term financial commitment means

¹² SCE Petition, pp. 8-9, as amended [proposed modification underlined].

¹³ D.07-01-039, at p. 42.

either a new ownership investment in baseload generation or a new or renewed contract with a term of five or more years, which includes procurement of baseload generation.” As part of determining what would be considered a long-term financial commitment, we needed to define the term “new ownership investments.”

In implementing the Interim EPS Rules, we defined “new ownership investments” as:

any investment that is intended to extend the life of one or more units of an existing baseload powerplant for five years or more, or results in a net increase in the existing rated capacity of that plant.¹⁴

As explained below, our definition of “new ownership investments” was not intended to apply to the capital expenditures requested in this instance. Further, we find that strictly applying this definition in this instance would result in an outcome that is inconsistent with our objectives in D.07-01-039. Therefore, as discussed below, we do not find SCE’s requested expenditures for Four Corners to fall within the definition of “new ownership investments.”

In defining “new ownership investments,” we noted that “we are looking for the best and most workable approach to identifying changes in an existing powerplant that would increase the expected level of GHG emissions from the facility over the long-term.”¹⁵ Thus, our definition of “new ownership investments” was intended to cover major refurbishments, such as those for repowering an existing powerplant, but not

¹⁴ D.07-01-039, at p. 53.

¹⁵ D.07-01-039, at p. 52.

every replacement of equipment or addition of pollution control equipment . . . Even after such changes, the plant and its operation may remain essentially unchanged. More importantly, this approach could reduce reliability as old parts are repaired rather than replaced.¹⁶

In this instance, SCE's requested expenditures are to ensure that Four Corners will continue to provide reliable power through the term of the Agreements. SCE's testimony in A.07-11-011, which was attached as Exhibit C of the Petition, explains why the replacements are necessary to ensure continued reliability of Units 4 and 5. This testimony also states that absent the requested replacements and refurbishments, Units 4 and 5 would be subject to lengthy service outages and present safety concerns.

Further, our implementation of the EPS is to ensure "that an LSE does not enter into long-term financial commitments with high-emitting baseload resources in the first place."¹⁷ This can only happen if the LSE is making a financial commitment. Here, due to the particular terms of the Four Corners Agreements, SCE would be contractually committed to paying for capital expenditures to Four Corners if the expenditures are approved by the Engineering and Operating Committee.¹⁸ Moreover, SCE points out that if it does not meet its financial obligations to cover its share of capital expenditures, SCE would not receive its share of power from Four Corners, yet still remain

¹⁶ *Id.*

¹⁷ D.07-01-039, at p. 32.

¹⁸ SCE Petition, Exhibit A, ¶ 15.2 & Exhibit C, p. 9.

liable for these costs.¹⁹ SCE states that its share of power from Four Corners is approximately 720 megawatts (MW) and estimates that the potential loss of energy and capacity from Four Corners could cost SCE customers approximately \$220 million per year.²⁰ Consequently, considering the requested capital expenditures as “new ownership investments” would impose additional costs on SCE ratepayers even though the amount of GHG emissions from Four Corners would likely remain unchanged.

As explained above, we had intended that our definition of “new ownership investments” serve as a workable approach to identifying changes made by an LSE to an existing powerplant that would increase the expected level of GHG emissions over the long-term, not every capital expenditure. Further, the overall objective of establishing the EPS in D.07-01-039 is to focus on

new long-term financial commitments to electrical generating resources that will have major impacts on GHG emissions for many years to come. This enables us to prevent major LSE procurement ‘backsliding’ that will make future GHG reductions more difficult.²¹

Strictly applying our definition of “new ownership investments” in this instance would be inconsistent with the objectives of D.07-01-039, since the requested capital expenditures in Four Corners are necessary for continued reliability for the duration of SCE’s Agreements and SCE’s financial commitment is contractually required under the terms of its Agreements. Accordingly, we find

¹⁹ SCE Petition, Exhibit B, ¶ 20.5.

²⁰ SCE Petition, pp. 6 & 9.

²¹ D.07-01-039, at p. 35.

that the capital expenditures requested in A.07-11-011 to refurbish and replace equipment in Units 4 and 5 of Four Corners are not new ownership investments subject to the EPS. SCE may seek rate recovery of these costs in A.07-11-011.

While we find that these capital expenditures are not new ownership investments, we note that SCE has indicated that additional expenses will likely be required after 2011 to maintain the safety and reliability of Four Corners.²² However, regulations adopted by the California Air Resources Board (CARB) pertaining to GHG emission limits and emission reduction measures will be operative on January 1, 2012.²³ Therefore, SCE's continued ownership interest in Four Corners after that date could subject SCE's ratepayers to potential financial risk for GHG-compliance costs. Consequently, we believe it would be appropriate for SCE to conduct a study on the feasibility of continuing to maintain its interest in Four Corners after 2011. This study would include consideration of the following:

1. Estimated costs of future investments in Four Corners if SCE maintains its interest in Four Corners. This would include estimated costs to bring Four Corners into compliance with the EPS.
2. Costs of GHG allowances or other GHG compliance costs beginning January 1, 2012, and thereafter, if SCE maintains its interest in Four Corners.
3. Cost impacts of selling SCE's interest in Four Corners either by December 31, 2011, or in 2016 (the end of its current operating agreement).

²² SCE Petition, p. 4.

²³ Health & Safety Code § 38526.

SCE shall submit a report on its findings and a proposed course of action with respect to Four Corners to the Commission within six months after this decision is issued. The Commission would then have sufficient time to consider the best course of action to take before any additional capital expenditures would need to be made in Four Corners. Finally, since we will be considering whether it would be in the ratepayers' best interest for SCE to maintain its interest in Four Corners, SCE shall not extend any of its existing Agreements or enter into any new Agreements without first obtaining Commission approval.

3.2. Timeliness of SCE's Petition

Rule 16.4(d) requires that a petition for modification be

filed and served within one year of the effective date of the decision proposed to be modified. If more than one year has elapsed, the petition must also explain why the petition could not have been presented within one year of the effective date of the decision. If the Commission determines that the late submission has not been justified, it may on that ground issue a summary denial of the petition.²⁴

SCE's Petition was filed on January 29, 2008, more than a year after the effective date of the D.07-01-039. On February 13, 2008, SCE filed an Amended Petition. In the Amended Petition, SCE notes that it had erroneously identified the effective date of D.07-01-039 as January 29, 2007, rather than January 25, 2007.

²⁴ Cal. Code Regs., Tit. 20, § 16.4, subd. (d).

It explained that its error arose as a result of the different rules concerning applications for rehearing and petitions for modification.²⁵

We find that SCE has sufficiently justified why its Petition was filed more than one year after D.07-01-039 was effective. It appears that SCE now realizes that petitions for modification should be filed within one year of the *effective* date, not the *mail* date, of a decision and we trust that SCE will not make this error again. Finally, we find that SCE's error was harmless, especially since it explained the error shortly afterwards through the filing of an Amended Petition.

4. Comments on Proposed Decision

The proposed decision of the Commissioner 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 September 22, 2008 by SCE, the Natural Resources Defense Council and jointly by WPTF and IEP. Reply comments were filed on September 29, 2008 by SCE, WPTF and NRDC. No changes were made in response to comments.

WPTF and IEP maintain that our determination that SCE's requested expenditures in Four Corners do not fall within our definition of "new ownership investments" is a violation of Pub. Util. Code § 8341. They assert that § 8341 does not allow the Commission to draw exceptions to the rules we

²⁵ Pursuant to Rule 16.1(a), an application for rehearing is due 30 days after the date the Commission mails an order or decision. D.07-01-039 was effective on January 25, 2007, but mailed on January 29, 2007.

adopted in D.07-01-039.²⁶ WPTF and IEP are mistaken. It is within our authority to interpret our own rules, and our determination that SCE's requested expenditures for Four Corners do not fall under our definition of "new ownership investment" is consistent with both SB 1368 and the objectives of D.07-01-039. As such, our determination would be granted deference by a reviewing court.²⁷

SCE requests that the deadline to submit a report on its proposed course of action with respect to Four Corners be extended from six months after the decision is issued to one year after the decision is issued. It argues that the additional six months is needed due to the complexity of issues and to allow for a more thorough assessment and consideration of possible outcomes and costs. However, as SCE acknowledges, even if it had a year to study these issues, it would still not be able to provide definitive answer on many of the cost issues.²⁸ Further, a six-month delay in submitting such a report would shorten the amount of time available to SCE to implement any actions ordered by the Commission to be taken prior to 2012. Accordingly, we decline to extend the deadline, as requested by SCE.

5. Assignment of Proceeding

Michael R. Peevey is the assigned Commissioner and Amy C. Yip-Kikugawa is the assigned Administrative Law Judge in this proceeding.

²⁶ WPTF/IEP Comments on Proposed Decision, pp. 6-7.

²⁷ *Simi Corp. v. Garimendi* (2003) 109 Cal. App. 4th 1496, 1504-1505.

²⁸ SCE Comments on Proposed Decision, p. 3, fn. 1.

Findings of Fact

1. SCE owns a 48% co-tenancy interest in Four Corners and its rights and obligations with respect to Four Corners are stated in various agreements.
2. SCE has requested authorization to recover \$178,593,000 to cover its share of capital expenditures at Four Corners as part of its General Rate Case Application for Test Year 2009 (A.07-11-011).
3. SCE states that it cannot comply with its co-tenancy agreements unless Four Corners is granted an exemption from complying with the EPS.
4. If SCE does not fulfill its financial obligations under the terms of the co-tenancy agreements, it would lose its rights to its share of power from Four Corners.
5. Four Corners makes up approximately 720 MW of SCE's resource portfolio.
6. The Commission's definition of "new ownership investments" was not meant to include every replacement of equipment.
7. The EPS Rules can only prevent backsliding if an LSE has discretion and control over the long-term financial commitments it makes.
8. CARB regulations pertaining to GHG emission limits and emission reductions measures will be operative on January 1, 2012.

Conclusions of Law

1. SCE's proposed modification is too broad and should be denied.
2. Pub. Util. Code § 8341(b)(3) authorizes the Commission to adopt rules to implement the provisions of SB 1368.
3. SCE's requested capital expenditures in Four Corners do not fall under the Commission's definition of "new ownership investments."

4. After January 1, 2012, SCE's ratepayers would be exposed to potential financial risks to bring Four Corners into compliance with the pollution control requirements established by CARB.

5. It would be unreasonable to allow SCE to make any further capital investments in Four Corners without first determining whether SCE should continue to maintain its interest in Four Corners after 2011.

6. Rule 16.4(d) specifies the timeframe for filing a petition for modification.

7. SCE Petition has met the requirements of Rule 16.4(d).

O R D E R

IT IS ORDERED that:

1. Southern California Edison Company's (SCE) petition to modify Decision 07-01-039 is denied.

2. SCE's requested capital expenditures are not subject to the emission performance standard. Therefore, SCE may seek rate recovery of these expenditures in Application 07-11-011.

3. SCE shall conduct a study on whether it should continue to maintain its interest in Four Corners Generation Station (Four Corners) after December 1, 2011. SCE shall file a report on its findings and a proposed course of action with respect to Four Corners with the Commission's Energy Division within six months after this decision is issued. This report shall also be served on the service list in this proceeding.

4. SCE shall not extend any of its existing Agreements or enter into any new Agreements concerning its ownership in Four Corners without first obtaining Commission approval.

5. Rulemaking 06-04-009 remains open.

This order is effective today.

Dated _____, at San Francisco, California.