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Decision 11-03-010 March 10, 2011

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for Approval of Four Power Purchase Agreements With Westside Qualifying Facilities and Associated Cost Recovery. (U39E)	Application 10-10-005 (Filed October 8, 2010)

DECISION APPROVING FOUR POWER PURCHASE AGREEMENTS WITH EXISTING QUALIFYING FACILITIES

This decision approves four power purchase agreements between Pacific Gas and Electric Company (PG&E) and four existing qualifying facilities, and cost recovery associated with those agreements, contingent on the "Qualifying Facility and Contained Heat and Power Program Settlement Agreement" becoming effective. This proceeding is closed.

1. Background

By this application, Pacific Gas and Electric Company (PG&E) requests Commission approval of four power purchase agreements (PPAs) between PG&E and four existing cogeneration qualifying facilities (QFs): Mid-Set Cogeneration Company (46 megawatts (MW)), Salinas River Cogeneration Company (49.9 MW), Coalinga Cogeneration Company (49.9 MW), and Sargent Canyon Cogeneration Company (48.5 MW) (collectively, "sellers").

Each of these QFs began firm capacity deliveries to PG&E pursuant to 15-year Interim Standard Offer 4 contracts that were executed by PG&E and the sellers' predecessors-in-interest on June 28, 1985. Although the original contracts

have expired, PG&E has continued to purchase electric generation from the sellers under Standard Offer No. 1 as-available capacity contracts that are currently set to expire on December 31, 2011, March 5, 2012, February 28, 2012, and February 21, 2012, respectively. The proposed PPAs will replace the current contracts and provide for deliveries through December 31, 2016.

PG&E filed this application in anticipation of the Commission's approval of the then-pending "Qualifying Facility and Combined Heat and Power Program Settlement Agreement" (QF/CHP Settlement), which resolved numerous outstanding QF-related disputes. PG&E asserts that the power purchase contracts are just and reasonable, in large part, because they are consistent with the QF/CHP Settlement. Alliance for Retail Energy Markets (AReM) filed a protest opposing the application, including the proposed cost recovery provisions, as premature because the QF/CHP Settlement had not been adopted by the Commission. The California Independent System Operator (CAISO) filed a response supporting the application.

On December 3, 2010, the assigned commissioner issued a scoping memo and ruling which identified the issues to be determined and set a schedule for addressing those issues. In particular, the scoping memo determined that the matter should be submitted upon the filing of concurrent opening and reply briefs without the need for evidentiary hearing, set a schedule in anticipation that the Commission would issue a decision on the QF/CHP Settlement on December 16, 2010, and provided an opportunity for parties to file a motion for extension of time or other procedural relief upon a showing that the Commission decision approving the QF/CHP Settlement, if any, substantially deviated from the then-pending proposed decision. The Commission approved the QF/CHP

Settlement in Decision (D.) 10-12-035 on December 16, 2010, whereupon no motions were filed seeking an extension of time or other procedural relief.

PG&E and AReM filed concurrent opening briefs on January 10, 2011, AReM filed its concurrent reply brief on January 20, 2011, and PG&E filed its concurrent reply brief on January 24, 2011, upon which the proceeding was submitted.

2. Scope of Issues

The assigned Commissioner's December 3, 2010, scoping memo and ruling identified the following issues to be determined in the proceeding:

1. Are the PPAs just and reasonable? In deciding this overarching issue, we will consider the following factors:
    a. Will the PPAs reduce customer costs by providing better market value?
    b. Will the PPAs provide operational benefits?
    c. Will the PPAs result in reduced greenhouse gas (GHG) emissions?
    d. Will procurement under the PPAs satisfy the Emissions Performance Standard adopted by D.07-01-039?
    e. Will procurement under the PPAs serve to meet PG&E's MW targets and GHG emissions reductions under the QF/CHP Settlement? This issue encompasses consideration of whether procurement under the PPAs should count toward the MW and GHG emissions reduction targets.
    f. Will procurement under the PPAs serve the Commission's policy preference for the utilities to maintain their current level of QF capacity, as provided in D.07-12-052? This issue encompasses consideration of whether procurement under the PPAs should count toward PG&E's obligation to maintain its current level of QF capacity.

g. Do the PPAs satisfy PG&E's obligations with respect to sellers under Section 3.4.4 of the QF/CHP Settlement Term Sheet?

2. Should PG&E be authorized to recover the costs of the PPAs through the Electric Revenue Recovery Account (ERRA) and allocate stranded costs consistent with Section 13.1 of the QF/CHP Settlement Term Sheet? This issue encompasses consideration of whether PG&E's cost allocation proposal is consistent with the QF/CHP Settlement.

3. The PPAs are Just and Reasonable

3.1. PPA Description

The PPAs will replace the sellers' current contracts and provide for deliveries through December 31, 2016. Under the proposed PPAs, sellers' deliveries are subject to 30-day and day-ahead forecasts and subject to scheduling deviation adjustments. Sellers are required to meet performance an outage standards that exceed those of their current contracts. Sellers are subject to higher operating standards, and more stringent scheduling and forecasting requirements, than those under existing QF PPAs. The sellers must comply with North American Electric Reliability Corporation requirements, as well the requirements of the CAISO tariff. The capacity and energy pricing is consistent with the forms of the PPAs under the QF/CHP Settlement.[1]

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[1] PG&E asserts that the capacity prices under the proposed PPAs are consistent with D.07-09-040, in which the Commission determined that QFs that were operating under current firm capacity contracts at that time would be eligible to execute new firm capacity contracts with a firm capacity price of $91.97 per kilowatt per year. As the sellers were not eligible for those contracts (*see* D.09-04-034, denying petition to modify D.07-09-040 to extend the eligibility to QFs with expired firm capacity contracts), this comparison is not determinative of the reasonableness of the proposed power purchase contracts. However, under the QF/CHP Settlement, QFs with existing standard offers are eligible to enter into Transition PPAs with this same firm capacity price. (*See*

Footnote continued on next page

3.2. Market Value

Under the QF/CHP Settlement, existing CHP QFs with an expiring standard offer contract may convert it to a transition power purchase agreement (Transition PPA) that will expire by no later than July 1, 2015.[2] The utilities will conduct competitive solicitations for CHP resources as a means of achieving their MW and GHG emissions reduction targets.[3] The QF/CHP Settlement also contemplates that the utilities may enter into bilaterally negotiated PPAs for CHP resources.[4]

The PPAs will provide approximately $5 million greater market value than the Transition PPAs that the sellers could receive under the QF/CHP Settlement Agreement, due to PG&E's greater curtailment rights under the proposed power purchase contracts.[5]

3.3. Operational Benefits

The proposed PPAs provide for more detailed and reliable seller forecasts of deliveries, greater curtailment rights, and more structured outages, as

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D.10-12-035, Appendix A, Transition Standard Offer Contract for Existing Qualifying Cogeneration Facilities, Section 1.06.)

[2] D.10-12-035, Appendix A, Term Sheet, § 3.

[3] *Id.*, § 4.2.

[4] *Id.*, § 4.3.

[5] PG&E notes that the proposed PPAs represent a compromise of claims made by the sellers' representative, Cogeneration Association of California, in its petition to modify D.07-09-040, which "made it possible for" the QF/CHP Settlement to include the withdrawal of that petition. As these proposed PPAs were not before the Commission in its consideration of the QF/CHP Settlement, the withdrawal of that petition as part of the settlement is not informative or determinative of the reasonableness of the proposed PPAs.

compared to the sellers' current contracts and the Transition PPAs. The PPAs provide greater clarity regarding the role and responsibility of the scheduling coordinator, and mandate compliance with CAISO tariff and metering requirements consistent with the Commission's policy to better integrate QF resources into the CAISO tariffs and deliverability standards. (*See*, e.g., D.07-09-040 at 210-211.)

The proposed PPAs give PG&E greater curtailment rights as compared to the sellers' current contracts and the Transition PPAs. Depending on GHG emissions reduction and compliance costs, PG&E may decide to use these greater curtailment rights to reduce GHG emissions from the sellers' facilities. This is consistent with Commission policy encouraging the utilities to consider GHG emissions and costs when making procurement and scheduling decisions. (*See*, e.g., D.07-12-052 at 243-245.)

3.4. Emissions Performance Standard Requirements

Under the Emissions Performance Standard adopted by the Commission in D.07-01-039, long-term (five years or greater) contracts for generating facilities designed and intended to provide electricity at an annualized capacity factor of 60% must provide for a maximum carbon dioxide emissions rate of no more than 1,100 pounds per megawatt-hour (MWh). The proposed PPAs comply with this requirement because their emissions rates are significantly less than 1,100 pounds per MWh.

3.5. Consistency with QF/CHP Settlement and PG&E's MW and GHG Emissions Reduction Targets

The QF/CHP Settlement establishes MW and GHG emissions reduction targets to increase the diversity, reliability, and environmental benefits of the energy resources available to the State's electricity consumers. Section 4.3.1 of

the QF/CHP Settlement provides that bilaterally negotiated and executed CHP PPAs are part of the CHP Program procurement options, and Section 5.2.2 provides that PPAs executed during the stated interval count towards the MW and GHG emissions reduction targets. Accordingly, the proposed PPAs count toward PG&E's MW and GHG emissions reduction targets.

3.6. Consistency with Policy Preference to Maintain Current Level of QF Capacity

In D.07-12-052, as modified by D.08-09-045, the Commission indicated its policy preference for utilities to maintain their current level of QF capacity through new or renewed contracts, subject to the limitations of the Public Utilities Regulatory Policy Act of 1978 (PURPA).[6] One of the expressed purposes of the QF/CHP Settlement, which D.10-12-035 affirmed as consistent with state and Commission policy and law, is to encourage the continued operation of the state's existing CHP facilities. The proposed PPAs allow for the continued operation of four existing CHP QF facilities that have provided reliable energy and capacity to PG&E since the 1980s. This is consistent with the Commission's policy preference that the utilities maintain currently existing QF capacity in their resource mix.

3.7. Consistency with Obligations to Sellers under Section 3.4.4 of the QF/CHP Settlement

PG&E requests that the Commission determine that the proposed PPAs satisfy PG&E's obligations to sellers under Section 3.4.4 of the QF/CHP

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[6] The United States Congress passed PURPA in 1978, as codified in the United States Codes (U.S.C.) at 16 U.S.C. Section 824a-3, and 18 Code of Federal Regulations (CFR) Sections 292.301 *et seq.*

Settlement Term Sheet. Section 3.4.4 provides that certain named QFs, including the sellers, can elect to sign a firm capacity Transition PPA and shall be paid under such PPA as if deliveries started on January 1, 2010. Under the proposed PPAs presented in this application, sellers will likewise be paid a true-up amount for firm capacity for the period starting January 1, 2010 as if deliveries had started at that time. PG&E asserts that the proposed PPAs therefore satisfy its obligations as imposed by Section 3.4.4.

However, PG&E does not have any obligation to sellers under Section 3.4.4. By its terms, Section 3.4.4 imposes the obligation to pay for firm capacity as if deliveries started on January 1, 2010, *if the sellers elect to sign a Transition PPA*. Instead, sellers have elected to sign bilaterally negotiated PPAs which, pursuant to Section 3.1.4, makes the Transition PPA unavailable to them. Therefore, the QF/CHP Settlement does not impose on PG&E the obligation to pay as if deliveries started on January 1, 2010. As PG&E has no such obligation, it is meaningless to attempt to ascertain whether the proposed PPAs meet it.

4. Cost Recovery

Section 13.1.2 of the QF/CHP Settlement provides that the Commission shall select one of two specified methods for allocation of CHP procurement costs to all electric service providers and community choice aggregators. In approving the QF/CHP Settlement, D.10-12-035 approved the allocation method set forth in Section 13.1.2.2 of the settlement, which provides that net capacity costs and all resource adequacy benefits associated with PPAs entered into pursuant to the settlement shall be proportionately allocated annually to all bundled, electric service provider, community choice aggregator and departing load customers (as defined in Section 17 of the settlement) on a non-bypassable basis.

Section 13.2.1 of the QF/CHP Settlement provides that the utilities shall recover the cost of all payments made pursuant to PPAs entered into pursuant to the settlement in their respective Energy Resources Recovery Accounts, subject only to their reasonable administration.

The proposed PPAs at issue here are consistent with, and entered into pursuant to, the QF/CHP Settlement. Accordingly, PG&E should allocate net capacity costs and all resource adequacy benefits associated with them pursuant to Section 13.1.2.2 of the settlement, and recover the cost of all payments made under them pursuant to Section 13.2.1 of the settlement.

5. Proposed Contingencies

Pursuant to Section 16.2 of the QF/CHP Settlement, it is not effective until and unless certain conditions precedent have been met, including approval by the FERC of a waiver of the utilities' obligations under Section 210(m) of PURPA. As of this time, those conditions have not been met, and D.10-12-035 approving the QF/CHP Settlement is the subject of three pending applications for rehearing.

In its opening brief, AReM requests that the Commission make approval of the PPAs subject to any changes that may be made to the QF/CHP Settlement as the result of the Commission's resolution of the pending applications for rehearing D.10-12-035 or the FERC's ruling on PG&E's request for waiver of its PURPA obligations, as well as any changes that may occur to the CHP Program as the result of potential future petitions to modify D.10-12-035 or future proceedings regarding the utilities' long term procurement planning. In its reply brief, AReM additionally requests that the Commission make approval of the PPAs contingent on resolution of the pending applications for rehearing of

D.10-12-035 and a FERC ruling approving PG&E's application for waiver from PURPA requirements.

It is inappropriate to make approval of this application contingent on the resolution of pending applications for rehearing of D.10-12-035. D.10-12-035 was made effective immediately upon its issuance and, therefore, the applications for rehearing do not suspend it. (*See* Rules of Practice and Procedure [Title 20, Division 1, of the California Code of Regulations], Rule 16.1(b).)

It is likewise inappropriate to make approval of this application subject to potential future changes to the QF/CHP Settlement, D.10-12-035, or the CHP Program, as it is entirely speculative whether future changes will be made or that, even if they are, any such changes would directly impact the issues addressed in this proceeding. If such changes are made in the future, the proper procedural approach would be for AReM to file a petition to modify this decision approving the PPAs.

It is, however, appropriate to make approval of this application contingent on the QF/CHP Settlement becoming effective. The reasonableness of the proposed PPAs is premised, in large part, on their value relative to the Transition PPAs that the sellers could receive under the QF/CHP Settlement, and the appropriateness of PG&E's proposed recovery of costs is premised on it having entered into the PPAs pursuant to the QF/CHP Settlement. If the QF/CHP Settlement does not become effective, consistency with the settlement will not be determinative of the reasonableness of the PPAs and appropriateness of PG&E's recovery of their costs.

We approve the PPAs and PG&E's recovery of their costs contingent on the QF/CHP Settlement becoming effective. In its reply comments on the proposed decision, PG&E attached a binding agreement between PG&E and all

parties to the PPAs that the PPAs are not effective until and unless the QF/CHP Settlement becomes effective. Accordingly, this proceeding should be closed.

Comments on the Proposed Decision

The proposed decision of Administrative Law Judge (ALJ) Yacknin 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 February 28, 2011, by PG&E and the CAISO, and reply comments were filed on March 3, 2011, by PG&E.

Assignment of Proceeding

Michael R. Peevey is the assigned Commissioner, and Hallie Yacknin is the assigned ALJ in this proceeding.

Findings of Fact

1. The PPAs will provide approximately $5 million greater market value than the Transition PPAs that the sellers could receive under the QF/CHP Settlement, due to PG&E's greater curtailment rights.

2. The PPAs provide greater operational benefits than the sellers' current contracts and the Transition PPAs that the sellers could receive under the QF/CHP Settlement.

3. The PPAs may result in reduced GHG emissions as compared to GHG emissions under the sellers' current contracts and the Transition PPAs that the sellers could receive under the QF/CHP Settlement.

4. Procurement under the PPAs will satisfy the Emissions Performance Standard adopted by D.07-01-039.

5. Procurement under the PPAs qualifies to meet PG&E's MW targets and GHG emissions reductions under the QF/CHP Settlement.

6. Procurement under the proposed PPAs will serve the Commission's policy preference for the utilities to maintain their current level of QF capacity, as provided in D.07-12-052.

7. Section 3.4.4 of the QF/CHP Settlement Term Sheet does not impose any obligation on PG&E to pay for deliveries under the proposed PPAs as if they started on January 1, 2010.

Conclusions of Law

1. Contingent on the QF/CHP Settlement becoming effective, the PPAs are just and reasonable and should be approved.

2. Contingent on the QF/CHP Settlement becoming effective, procurement under the PPAs should count toward PG&E's MW and GHG emissions reduction targets.

3. Contingent on the QF/CHP Settlement becoming effective, PG&E should proportionately allocate annually the PPAs' net capacity costs and all resource adequacy benefits associated with them to all bundled, electric service provider, community choice aggregator and departing load customers on a non-bypassable basis pursuant to Section 13.2.1 of the QF/CHP Settlement, and recover the bundled customer costs associated with them in its Energy Resources Recovery Account.

4. As D.10-12-035 is not suspended by virtue of the pending applications for rehearing the decision, it is inappropriate to make this decision approving the PPAs contingent on the resolution of those applications.

5. The proper vehicle for seeking to apply future potential changes to the QF/CHP Settlement, D.10-12-035, or the CHP Program to the PPAs and/or PG&E's recovery of costs incurred under them is by petition to modify this decision approving the PPAs.

6. As the PPAs are contingent on the QF/CHP Settlement taking effect, it is unnecessary to condition approval of the PPAs on such event.

7. This proceeding should be closed.

8. This order should be effective immediately.

O R D E R

IT IS ORDERED that:

1. Pacific Gas and Electric Company's power purchase agreements with Mid-Set Cogeneration Company, Salinas River Cogeneration Company, Coalinga Cogeneration Company, and Sargent Canyon Cogeneration Company are approved, contingent on the Qualifying Facility and Combined Heat and Power Program Settlement Agreement becoming effective.

2. Procurement under Pacific Gas and Electric Company's power purchase agreements with Mid-Set Cogeneration Company, Salinas River Cogeneration Company, Coalinga Cogeneration Company, and Sargent Canyon Cogeneration Company shall count toward Pacific Gas & Electric Company's megawatt and greenhouse gas emissions reduction targets, contingent on the Qualifying Facility and Combined Heat and Power Program Settlement Agreement becoming effective.

3. Pacific Gas and Electric Company shall proportionately allocate annually the net capacity costs of its power purchase agreements with Mid-Set Cogeneration Company, Salinas River Cogeneration Company, Coalinga Cogeneration Company, and Sargent Canyon Cogeneration Company, and all resource adequacy benefits associated with them, to all bundled, electric service provider, community choice aggregator and departing load customers on a non-bypassable basis, and shall recover the bundled customer costs of the power

purchase agreements in its Energy Resources Recovery Account, contingent on the Qualifying Facility and Combined Heat and Power Program Settlement Agreement becoming effective.

4. Application 10-10-005 is closed.

This order is effective today.

Dated March 10, 2011, at San Francisco, California.

MICHAEL R. PEEVEY
President
TIMOTHY ALAN SIMON
CATHERINE J.K. SANDOVAL
Commissioners

I abstain.

/s/ MICHEL PETER FLORIO
Commissioner