

Decision 07-09-010 September 6, 2007

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

Application of San Diego Gas and Electric Company (U902-E) for Approval of Power Purchase Agreement with J-Power, USA Development Company, LTD and Wellhead Power Margarita, LLC for Recovery of Costs and for a limited Exemption from the Requirements of Public Utilities Code Section 851.

Application 07-05-023  
(Filed May 11, 2007)

**OPINION APPROVING POWER PURCHASE AND  
LEASE OPTION AGREEMENTS  
ORDERING RECOVERY OF COSTS RELATED TO THOSE AGREEMENTS,  
AND FOR A LIMITED EXEMPTION FROM THE REQUIREMENTS  
OF PUBLIC UTILITIES CODE SECTION 851**

This decision approves power purchase agreements (PPAs) and corresponding leases between: (1) San Diego Gas and Electric Company (SDG&E) and J-Power, USA Development Company, Ltd. (J-Power); and (2) between SDG&E and Wellhead Power Margarita, LLC (Wellhead). For each of these sets of agreements, SDG&E shall grant options to lease its land to a developer (J-Power and Wellhead, respectively), who shall construct gas-powered peaker generators (peakers) on the leased land. The PPAs commit the

output of those peakers to SDG&E for a period of 25 years,<sup>1</sup> after which the leases shall expire and title to the peakers shall transfer to SDG&E at no additional cost.

Because the public interest is served by these arrangements, this decision also finds that these leases of utility land fall within the exceptions to the requirements of Pub. Util. Code § 851 found in Pub. Util. Code § 853(b).<sup>2</sup>

This decision further orders full recovery of costs associated with the PPAs from bundled customers through SDG&E's Energy Resources Recovery Account (ERRA). Any rental revenues in excess of the revenue requirement associated with the land values in rate base will also be recorded to SDG&E's ERRA account, for the benefit of bundled customers.

In total, these agreements will provide approximately 130 megawatts (MW) of power to meet future energy and reliability needs of SDG&E's bundled customers starting in 2008. This proceeding is closed.

## **1. Introduction**

In response to the unusually hot summer of 2006, we ordered Southern California Edison Company to immediately procure up to 250 MW of additional peaking capacity to be placed into service by the summer of 2007, and directed SDG&E and Pacific Gas and Electric Company to file reports addressing the potential need for similar action in their service areas.

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<sup>1</sup> The Wellhead PPA will terminate on December 31 of the year in which the 25<sup>th</sup> anniversary of initial delivery occurs, and so will be in effect for longer than 25 years but less than 26 years.

<sup>2</sup> All further code references are to the Public Utilities Code, unless otherwise stated.

After SDG&E reviewed its long-term procurement plan (LTPP) needs, it identified a need for additional capacity as early as the summer of 2008. SDG&E consulted with its Procurement Review Group (PRG) and with its Independent Evaluator (IE). Subsequent to these meetings, SDG&E issued a Request for Offers (RFO) on October 17, 2006.<sup>3</sup>

### **1.1 J-Power and Wellhead Projects**

SDG&E evaluated the projects offered into the RFO<sup>4</sup> and selected the agreements with J-Power and Wellhead, which are the subject of the present application.<sup>5</sup> Each offer consists of an option agreement to enter into a lease of SDG&E real property for the purpose of constructing peaker generators and a PPA to purchase the output of the new peakers.

Under the J-Power agreements, J-Power would construct two simple gas-fired peaker turbines with a combined capacity of about 86.5 MW, to be constructed on 16.5 acres of SDG&E's 202 acre Pala substation site in northern San Diego County, to which the generators would be connected. The commercial online date will be May 31, 2008, and the delivery term of the PPA is expected to be from May 31, 2008 through May 31, 2033.<sup>6</sup>

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<sup>3</sup> Application, p. 2.

<sup>4</sup> SDG&E's analysis is at the center of the IE's report, Exhibits 1 and C-1, and is also described in Exhibits 4 and C-4 on pp. 1-3.

<sup>5</sup> SDG&E may elect to submit applications at a future date seeking approval of other offered projects it received pursuant to the October 16, 2006 RFO. The present application does not address those offers in any detail and they are not being considered together with these projects.

<sup>6</sup> Application, pp. 3 and 6.

Under the Wellhead agreements, J-Power would construct one simple gas-fired peaker turbine with a capacity of about 44 MW, to be constructed on 1.68 acres of SDG&E's 19 acre Margarita substation site in Orange County, to which the generators would be connected. The commercial online date will be July 1, 2008, and the delivery term of the PPA is expected to be from July 1, 2008 through December 31, 2033.<sup>7</sup>

For both projects, during the duration of the PPA, the developer would own and operate the facility, and SDG&E would have exclusive off-take rights to both energy and ancillary services from units. SDG&E will serve as the scheduling coordinator for the units with the California Independent System Operator Corporation (CAISO). The units would be considered resource adequacy units subject to the dispatch and operational rules under the CAISO tariff.<sup>8</sup>

At the end of each lease, ownership of the peaker generators constructed on that site will transfer to SDG&E without cost.

## **2. Procedural Background**

SDG&E filed the present application on May 11, 2007, seeking approval of the projects offered by J-Power and Wellhead. More specifically, SDG&E sought the following relief: (1) approval of the PPAs and lease option agreements; (2) approval of recovery of costs under the PPAs by inclusion in its ERRA account; (3) rebalancing of its capital structure related to Financial Accounting Standards Board (FASB) Interpretation Number 46(R) (FIN 46(R)); and finding of

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<sup>7</sup> Application, pp. 3-4 and 6. The Wellhead PPA will terminate on December 31 of the year in which the 25<sup>th</sup> anniversary of initial delivery occurs.

<sup>8</sup> Application, pp. 3-4.

a limited exemption for the leases from the requirements of § 851 pursuant to § 853(b).

The Commission's Division of Ratepayer Advocates (DRA) filed a protest on June 21, 2007. Merced Irrigation District and Modesto Irrigation District (Districts) jointly filed a protest on June 21, 2007 directed to stranded cost recovery issues.

Administrative Law Judge (ALJ) Victoria S. Kolakowski issued a ruling on June 26, 2007 scheduling a prehearing conference (PHC) and requesting a joint PHC statement to identify and address issues that were under consideration in other proceedings.

The parties filed a joint PHC statement on July 5, 2007, which contains a stipulation between the Districts and SDG&E regarding the stranded cost recovery issues raised by the Districts.<sup>9</sup> Based upon this agreement, Districts entered requested to change their appearance to "information only" and did not attend the PHC.

The PHC statement also noted several areas of agreement and disagreement between DRA and SDG&E. Areas of agreement included the lack of a need for evidentiary hearings and the ultimate result of approving the PPAs.<sup>10</sup> Areas of disagreement related to the basis for the approval, which shall be discussed in more detail below. The other area of DRA concern was with the language in SDG&E's testimony regarding the treatment of the lease payments

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<sup>9</sup> Joint PHC Statement, pp. 5-6.

<sup>10</sup> Joint PHC Statement, p. 6.

due to SDG&E. In response to DRA's concerns, SDG&E filed an amendment to page 4 of the testimony of Michael M. Schneider on July 23, 2007.<sup>11</sup>

The PHC was held on July 9, 2007. SDG&E and DRA attended the PHC, and offered and moved testimony into the record. The testimony was accepted, as described below.

SDG&E filed additional testimony on July 30, 2007 regarding the CAISO's estimates of transmission costs that were received after the PHC. These transmission costs will be recovered through charges tariffed by the Federal Energy Regulatory Commission (FERC) and will not be included in costs approved in this decision.

### **3. J-Power and Wellhead's PPAs and Lease Option Agreements Should Be Approved**

As discussed below, we determine that the PPAs and lease option agreements with J-Power and Wellhead should be approved.

We have reviewed the confidential analysis provided in Exhibit C-3, and find that it provides adequate demonstration of a need for additional peaking capacity sufficient to justify the purchases under the J-Power and Wellhead PPAs. We also agree with SDG&E and DRA's position that use of the energy auction mechanism adopted in D.06-07-029 to meet this need would likely create greater risk than benefit to SDG&E's bundled customers.<sup>12</sup> Under the best circumstances, SDG&E ratepayers would gain only a small amount, while the risk that they would lose money under such an auction far outweighs the benefits.

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<sup>11</sup> This amendment is identified as Exhibit 5 below.

<sup>12</sup> Joint PHC Statement, p. 7.

Delay in adding peaking resources can adversely affect system reliability, and can cause imbalances in negotiating power for procurement of such resources.<sup>13</sup> While it would otherwise be appropriate to wait until determining the total LTPP needs of SDG&E in R.06-02-013 before reaching a decision on this application, the need to begin the process of construction of the peaker units in time to meet the projected need for the summer of 2008 requires that we make a determination without delay.<sup>14</sup> Given SDG&E's current and unique situation, we are persuaded to approve these commitments prior to a final need determination in the LTPP proceeding, R.06-02-013. However, we note that the conclusions reached here today are based on a unique set of circumstances and should not be assumed to be applicable in a general sense.<sup>15</sup>

One potential concern with approving these projects is that adding gas fired resources such as these peakers could crowd out resources higher in the load order set forth in the Energy Action Plan (EAP). The LTPP process considers issues such as the EAP loading order in a comprehensive manner, to avoid such outcomes. Therefore, we expect that all Investor Owned Utilities (IOUs) will plan for meeting their needs through appropriate implementation of the loading order. Only once an IOU has exhausted all attempts to fill a net short position with preferred loading order resources should it look to traditional fossil generation to meet remaining needs.

SDG&E sought to meet this need through its October 16, 2006 RFO, which was developed in concert with its PRG and IE. Bids were evaluated by

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<sup>13</sup> Exhibit 2, p. 2.

<sup>14</sup> Joint PHC Statement, p. 3-4.

<sup>15</sup> A Commission Decision in R.06-02-013 is currently anticipated later this year.

considering prices, depreciation, debt service, equity charges, federal and state taxes and estimated operation and maintenance expenses.<sup>16</sup> Bids were then compared and the top choices were subjected to a credit analysis to identify the risks of failure to perform over the 25-year term of the projects.<sup>17</sup> The final projects were selected based upon price, creditworthiness, delivery dates and location of the projects.<sup>18</sup> Using these criteria, the J-Power and Wellhead proposals were accepted.

We find that SDG&E used a prudent process for selecting the J-Power and Wellhead projects from the RFO. We have previously directed IOUs to use a least-cost, best fit (LCBF) methodology when evaluating RFO bids.<sup>19</sup> Based upon our review of SDG&E's process, it selected the LCBF proposals that met the reasonable location, delivery and creditworthiness requirements imposed by SDG&E.<sup>20</sup>

Furthermore, these projects meet the environmental tests that we apply to all such projects. The project will be built on SDG&E property, and therefore meets the requirement that IOUs give priority to generation projects on existing (brownfield) sites before using new (greenfield) sites.<sup>21</sup> The peakers have expected capacity factors below the 60% threshold, and therefore they are exempt from meeting the Greenhouse Gas requirements set forth in D.07-01-039

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<sup>16</sup> Exhibit 2, pp. 5-6.

<sup>17</sup> *Id.*, p. 6.

<sup>18</sup> *Id.*, pp. 8-9.

<sup>19</sup> D.04-12-048, Finding of Fact 86 and Ordering Paragraph 26(d).

<sup>20</sup> We do not address whether this methodology would fully meet the LCBF requirements for future RFOs.

<sup>21</sup> *See* D.04-12-048.



and under statute.<sup>22</sup> Local governments and the California Energy Commission (CEC) will ensure compliance with the environmental requirements of the California Environmental Quality Act (CEQA).<sup>23</sup>

We have reviewed the J-Power and Wellhead PPAs, and find that they prudently meet demonstrated need at reasonable costs. Each provides the benefits of peaking capacity, energy and ancillary services; helps meet resource adequacy goals; and provides local reliability benefits.

Both PPAs contain tolling provisions that provide that SDG&E shall provide the natural gas to operate the peakers. We have previously recognized that there are distinct advantages in some circumstances to such an arrangement. In D.02-08-065, we noted that “[t]olling arrangements have the potential to provide benefits to electric consumers through reduced electric price volatility and ensuring plants are available to meet peak demands.”<sup>24</sup> Such concerns are particularly relevant to units such as peakers, which are designed both to meet such peak demand as well as provide “black start” capability to ensure local system restoration in case of blackouts. We find that it is likely that such price and availability benefits will be provided by these PPAs.

We have also reviewed the lease option agreements, as well as the proposed lease agreements. These agreements provide reasonable protections for SDG&E and its ratepayers.

Therefore, we approve the PPAs and lease option agreements with J-Power and Wellhead. By approving agreements which will eventually lead to

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<sup>22</sup> Exhibit 2, p. 2. SDG&E commits to limiting the operating hours to less than 60%.

<sup>23</sup> Application, p. 7.

<sup>24</sup> D.02-08-065, fn. 3.

increased SDG&E ownership of generation facilities, we do not intend to signal that we are abandoning our commitment to the hybrid wholesale market. As stated above, these agreements are being approved due to unique circumstances, and this decision is not to be considered precedential.

#### **4. Payments Under the J-Power and Wellhead Agreements Treatment in SDG&E's ERRA**

##### **4.1 Recovery of Purchased Power Costs**

The fundamental question that we must decide regarding the recovery of purchased power costs is whether to include these costs in SDG&E's ERRA, which provides recovery from bundled customers, or from all benefiting customers.

The purpose of the IOU ERRA accounts is to provide full recovery of the IOU's energy procurement costs associated with fuel and purchased power, utility retained generation, CAISO-related costs, and costs associated with residual net short procurement requirements to serve the IOU's bundled customers.<sup>25</sup> SDG&E records in its ERRA revenues from its Electric Energy Commodity Cost rate schedule adjusted to exclude California Department of Water Resources purchases and commodity revenues assigned to the Non-Fuel Generating Balancing Account (NGBA).<sup>26</sup>

SDG&E has demonstrated through its testimony that the projects are being proposed for the benefit of meeting bundled customer demand, and not for

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<sup>25</sup> See D.02-10-062 and D.02-12-074.

<sup>26</sup> The NGBA became effective in January 1, 2004 to comply with D.03-12-063. See Exhibit 4, p.3, fn. 1.

providing capacity for other customers.<sup>27</sup> Therefore it is appropriate for SDG&E to recover its purchased power costs through the ERRA.

#### **4.2 Treatment of Lease Revenues**

SDG&E will receive lease payment revenues from J-Power and Wellhead. The treatment of these revenues was one of the sources of discussion between SDG&E and DRA.<sup>28</sup> In order to clarify this treatment, SDG&E filed Exhibit 5, which amended the testimony of Exhibit 4. The amended language reads that:

“SDG&E proposes to record revenues associated with lease payments to the Transition Cost Balancing Account (TCBA) equal to the revenue requirement costs associated with the land values recorded in rate base. The balance in the TCBA is amortized in the Competition Transition Charge (CTC) rate component, which is applicable to both bundled and DA customers. Any revenues associated with lease payments that exceed the revenue requirement associated with the land values in rate base will be recorded to the ERRA account.”<sup>29</sup>

We agree that this is a prudent treatment of these revenues, which will allow any excess payments to offset the costs of bundled customers, while preserving the treatment of the payments below the revenue requirement in the TCBA, which will benefit both bundled and direct access customers.

#### **5. The J-Power and Wellhead Agreements Should be Exempted from the Requirements of § 851**

Section 851 requires that all leases entered into by a public utility must be approved by the Commission. Under the agreements with J-Power and

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<sup>27</sup> See Exhibit 3, pp. 3 and 6, and Exhibit 4, p. 3.

<sup>28</sup> Joint PHC Statement, p. 7.

<sup>29</sup> Exhibit 5, replacing page 4 of Exhibit 4.

Wellhead, SDG&E is granting an option to lease the property, rather than entering into the leases. As a result, § 851 would require a subsequent proceeding to approve the leases. SDG&E has noted that this would add significantly to the time to construct the peakers, and would make it impossible to make the peakers available for the summer of 2008.<sup>30</sup>

Section 853(b) authorizes the Commission to exempt a public utility from the § 851 requirements upon a finding that the application of § 851 is not necessary in the public interest. SDG&E seeks such an exemption on several grounds.

First, SDG&E cites D.01-06-006, which granted SDG&E an exemption to construct generation units during the Energy Crisis of 2000-01.<sup>31</sup> SDG&E contends that these facilities are needed due to similar compelling need for the period beginning in the summer of 2008, as well as the statements made in the Assigned Commissioner Ruling (ACR) in R.06-02-013 ordering SCE to procure additional peaking capacity. DRA did not agree that SDG&E should rely on the ACR in R.06-02-013. DRA contends that the need was demonstrated in Exhibits 3 and C-3, which interpret portions of SDG&E's 2007-2016 LTPP filing in R.06-02-013, as well as projections of SDG&E and the CEC.<sup>32</sup>

Second, SDG&E states that the operation of the peakers will not interfere with SDG&E's provision of utility service, and as noted above, the CEC and local

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<sup>30</sup> Application, p. 8.

<sup>31</sup> Application, p. 5.

<sup>32</sup> Joint PHC Statement, p. 6.

governments would ensure compliance with the environmental requirements of the California Environmental Quality Act (CEQA).<sup>33</sup>

Third, SDG&E notes that the generation will provide power, reliability, resource adequacy and least cost/best fit procurement benefits.

Exemplary copies of the leases that SDG&E seeks to exempt from further review under § 851 are included as an attachment to the agreements.<sup>34</sup> If these leases were presented to us for approval as part of the present application, they would receive such approval. As a general policy, with regard to approval under § 851, we have found that “[t]he public interest is served when utility property is used for other productive purposes without interfering with the utility’s operation or affecting service to utility customers.”<sup>35</sup> That test is fully met by the proposed leases. The land in question will be used for a very productive purpose directly related to that of the utility’s service obligations – to meet the reliability and power needs of its customers.

We do not have the final leases before us for approval, but it would be redundant to seek further approval for the leases as long as they are the same as presented in the record of this proceeding. It is not in the public interest to delay execution of these leases pending a further proceeding, and therefore the requirements of § 853(b) are satisfied.<sup>36</sup>

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<sup>33</sup> Application, p. 7.

<sup>34</sup> See Exhibits C-2, Attachments 3 and 4.

<sup>35</sup> D.00-07-010, pp. 6-7, 2000 Cal.PUC LEXIS 576 \*9.

<sup>36</sup> SDG&E may not have needed to seek a waiver under § 853(b), as their application may have contained sufficient information to seek direct approval of the proposed leases. In general, we do not favor parties seeking waiver of the requirements under § 851. However, due to the urgency of the present application and since no party has

*Footnote continued on next page*

There is therefore no need to rely upon our prior decision D.01-06-006 or upon the ACR in R.06-02-013. DRA is correct that the showings in Exhibits 3 and C-3 are independently sufficient to justify waiver of the § 851 requirements for these specific projects.

## **6. Testimony and Exhibits**

As discussed above, SDG&E offered several exhibits into the record, which were received by the ALJ. On July 23, 2007, SDG&E served an additional exhibit, which amended the testimony of Exhibits 4 and C-4. This exhibit was identified as Exhibit 5. Finally, on July 30, 2007, SDG&E served a late-filed exhibit into the record, with both confidential and public (redacted) versions. These exhibits are identified as Exhibit 5 (public) and Exhibit C-5 (confidential).

SDG&E's testimony is identified as follows and is received into evidence:

Exhibit 1 – Report of the Independent Evaluator on the 2008 Local Peaking Capacity RFO of SDG&E (Public Version)

Exhibit 2 – Direct Testimony of Mike McClenahan of SDG&E (Public Version)

Exhibit 3 – Direct Testimony of Robert B. Anderson of SDG&E (Public Version)

Exhibit 4 – Direct Testimony of Michael M. Schneider of SDG&E (Public Version)

Exhibit 5 – Amendment to Direct Testimony of Michael M. Schneider of SDG&E

Exhibit 6 – Late-Filed Exhibit of SDG&E (Public Version)

Exhibit C-1 - Report of the Independent Evaluator on the 2008 Local Peaking Capacity RFO of SDG&E (Confidential Version)

Exhibit C-2 – Direct Testimony of Mike McClenahan of SDG&E (Confidential Version)

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addressed whether SDG&E's filing was adequate to support approval under § 851, we shall not make any finding regarding this question, and this decision should not be considered precedential.

Exhibit C-3 - Direct Testimony of Robert B. Anderson of SDG&E (Confidential Version)

Exhibit C-4 - Direct Testimony of Michael M. Schneider of SDG&E (Confidential Version)

Exhibit C-6 - Late-Filed Exhibit of SDG&E (Confidential Version)

## **7. Confidential Information**

SDG&E has provided declarations along with each of its confidential exhibits regarding the confidentiality of data provided in prepared testimony in support of its application request. The declarations identify information subject to requested confidential treatment, the appropriate reference to the Matrix Category in Appendix A of D.06-06-066 regarding confidential treatment of investor owned utility data, and the assertion that the detailed information is required for the application and cannot be aggregated, summarized, redacted, masked or otherwise protected in a way that allows partial disclosure.

Upon review of the contents of the exhibits and their associated declarations, Exhibits C-1, C-2, C-3, C-4 and C-6 are received into evidence under seal.

## **8. Categorization and Need for Hearings**

In Resolution ALJ 176-3192 dated May 24, 2007, the Commission preliminarily categorized this application as ratesetting, and preliminarily determined that hearings were not necessary. At the prehearing conference, it was determined that the parties agreed that no evidentiary hearings were needed, and therefore it is not necessary to alter the preliminary determinations made in Resolution ALJ 176-3192.

## **9. Comments on Proposed Decision**

The parties agreed at the prehearing conference to a shortened comment period for this proposed decision. Accordingly, comments were due on

Monday, August 27, 2007 and reply comments were due on Tuesday, September 4, 2007. The only comments were received from the Districts, who recommended changes to clarify the sections describing their participation.

#### **10. Assignment of Proceeding**

Michael R. Peevey is the assigned Commissioner and Victoria S. Kolakowski is the assigned ALJ.

#### **Findings of Fact**

1. SDG&E has entered into a PPA and lease option agreement with J-Power to develop approximately 86.5 MW of gas-fired peaking generation on 16.5 acres of SDG&E's 202 acre Pala substation in northern San Diego County, to which the generators will be connected. The commercial online date will be May 31, 2008, and the delivery term of the PPA is expected to be from May 31, 2008 through May 31, 2033.

2. SDG&E has entered into a PPA and lease option agreement with Wellhead to develop approximately 44 MW of gas-fired peaking generation on 1.68 acres of SDG&E's 19 acre Margarita substation in Orange County, to which the generators will be connected. The commercial online date will be July 1, 2008, and the delivery term of the PPA is expected to be from July 1, 2008 through December 31, 2033.

3. For both the J-Power and Wellhead projects, during the duration of the PPA, the developer would own and operate the facility, and SDG&E would have exclusive off-take rights to both energy and ancillary services from units. SDG&E will serve as the scheduling coordinator for the units with the CAISO. SDG&E would provide natural gas to fuel the generators. The units would be considered resource adequacy units subject to the dispatch and operational rules under the CAISO tariff.



4. At the end of each lease, ownership of the peaker generators constructed on that site will transfer to SDG&E without cost.

5. The parties have agreed to defer discussions of the capital structure issues arising from this application to A07-05-007.

6. SDG&E has demonstrated a need for additional peaking capacity to meet the needs of its bundled customers that exceeds the generation capacity of the projects proposed by J-Power and Wellhead.

7. Purchasing power to meet the demonstrated need in an energy auction poses greater cost risks to SDG&E bundled ratepayers than the likely benefits of using such an auction.

8. Delay in approval of peaking generation could result in shortfalls as early as the summer of 2008.

9. SDG&E used a prudent process for selecting the J-Power and Wellhead projects from among competing projects offered into its October 16, 2007 RFO. The process selected the best fit and least cost proposals that fully met the location, delivery and creditworthiness requirements imposed by SDG&E.

10. The J-Power and Wellhead PPAs prudently meet demonstrated need at reasonable costs. Each provides benefits of peaking capacity, energy and ancillary services and helps meet resource adequacy and local reliability goals.

11. The use of tolling agreements for gas for the peakers should provide reduced electric price volatility, and will help ensure the peakers are available to meet peak demands and black start capability.

12. The J-Power and Wellhead lease-option agreements provide reasonable protections for SDG&E and its ratepayers.

13. SDG&E will record revenues associated with lease payments to the TCBA equal to the revenue requirement costs associated with the land values recorded

in rate base. The balance in the TCBA is amortized in the CTC rate component, which is applicable to both bundled and direct access customers.

14. Any revenues associated with lease payments that exceed the revenue requirement associated with the land values in rate base will be recorded to the ERRRA account.

15. Operation of the peakers constructed under the option agreements will not interfere with SDG&E's provision of utility service to its customers.

16. Operation of the peakers is a productive purpose for the use of the substation land covered by the agreements.

17. SDG&E' public (redacted) Exhibits 1 through 6 and confidential (unredacted) Confidential Exhibits C-1, C-2, C-3, C-4 and C-6 are identified herein and have been offered by SDG&E as testimony.

18. SDG&E has provided declarations with each of its confidential exhibits that meet the requirements of D.06-06-066. The contents of those exhibits qualify them for confidential treatment pursuant to D.06-06-066.

### **Conclusions of Law**

1. SDG&E's PPA with J-Power and its associated lease option agreement should be approved, as they prudently meet demonstrated need at reasonable costs.

2. SDG&E's PPA with Wellhead and its associated lease option agreement should be approved, as they prudently meet demonstrated need at reasonable costs.

3. SDG&E should be allowed to recover in power purchase costs through its ERRRA, as the purchases are for the benefit of its bundled customers.

4. SDG&E should record revenues associated with lease payments to the TCBA equal to the revenue requirement costs associated with the land values recorded in rate base.

5. SDG&E should record to its ERRRA account any revenues associated with lease payments that exceed the revenue requirement associated with the land values in rate base.

6. SDG&E's agreements to lease substation land provide useful purposes for the land without interfering with SDG&E's provision of utility services, and therefore meets the requirements under § 853(b) of a waiver of the § 851 requirements for the limited purposes of constructing peaker units pursuant to these agreements, provided that they are the same as those attached to the lease option agreements..

7. SDG&E' public (redacted) Exhibits 1 through 6 and confidential (unredacted) Confidential Exhibits C-1, C-2, C-3, C-4 and C-6 should be entered into the record of this proceeding.

8. SDG&E has met the requirements of D.06-06-066 for Confidential Exhibits C-1, C-2, C-3, C-4 and C-6, and those exhibits should be filed under seal.

## **O R D E R**

### **IT IS ORDERED** that:

1. San Diego Gas and Electric Company's (SDG&E) power procurement agreement (PPA) and lease option agreement of May 9, 2007 with J-Power, USA Development Company, Ltd. is approved.

2. SDG&E's PPA and lease option agreement of May 1, 2007 with Wellhead Power Margarita, LLC is approved.

3. SDG&E is authorized to recover payments made pursuant to the PPA by means of entries into its Energy Resources Recover Account (ERRA), subject to annual review of those payments.

4. SDG&E shall record to the Transition Cost Balancing Account any revenues associated with payments made under any lease executed pursuant to the lease option agreements, up to the revenue requirement costs associated with the land values recorded in rate base.

5. SDG&E shall record any revenues associated with lease payments that exceed the revenue requirement associated with the land values in rate base to the ERRA account.

6. Any leases executed pursuant to the lease option agreements approved herein are exempt from the requirement of Commission approval found in Pub. Util. Code § 851 pursuant to Pub. Util. Code § 853(b), provided that they are the same as those attached to the lease option agreements.

7. SDG&E' public (redacted) Exhibits 1 through 6 and confidential (unredacted) Confidential Exhibits C-1, C-2, C-3, C-4 and C-6, as described herein, are entered into the record of this proceeding.

8. Confidential Exhibits C-1, C-2, C-3, C-4 and C-6 are filed under seal pursuant to D.06-06-066 and shall remain sealed for a period of three years from the effective date of this decision.

9. Application 07-05-023 is closed.

This order is effective today.

Dated September 6, 2007, at San Francisco, California.

MICHAEL R. PEEVEY  
President  
DIAN M. GRUENEICH

JOHN A. BOHN  
RACHELLE B. CHONG  
TIMOTHY ALAN SIMON  
Commissioners