ALJ/SK/vdl *

Decision 88-03-026 March 9, 1988

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Second application of Pacific Gas and Electric Company for approval of certain standard offers pursuant to Decision 82-01-103 in Order Instituting Rulemaking No. 2.	Application 82-04-44 (Filed April 21, 1982; amended April 28, 1982, July 19, 1982, July 11, 1983, August 2, 1983, and August 21, 1986)
And Related Matters.	Application 82-04-46 Application 82-04-47 Application 82-03-26 Application 82-03-37 Application 82-03-62 Application 82-03-67 Application 82-03-78 Application 82-04-21

THIRD INTERIM OPINION, COMPLIANCE PHASE: STANDARD OFFER UPDATING

Today's decision is devoted entirely to the issue of standard offer updating. This is a key element in fitting the pricing and procurement of qualifying facilities (QFs) within the overall resource planning of California's electric utilities. Updating is particularly important for those utilities with long-run standard offer applications: Pacific Gas & Electric Company (PG&E); San Diego Gas & Electric Company (SDG&E); and Southern California Edison Company (Edison).

these purposes. Dependence on the GRC for capacity price updating is largely responsible for the problems culminating in suspension of Standard Offer 2 and for prolonged uncertainty over the interpretation of an incomplete capacity price schedule adopted in PG&E's test year 1984 GRC (D.83-12-068).

Today's decision does not address the issue of coordinating our biennial resource plan review with the Energy Commission's Electricity Report process. We reserve this issue to the next decision, which will conclude the development of final Standard Offer 4.

II. Annual Updating and the Role of ECAC

Two aspects of Table A are somewhat controversial. First, we had considered, and Edison continues to favor, having a single annual proceeding to update variable QF payments for PG&E, SDG&E, and Edison, instead of assigning this task to the respective Energy Cost Adjustment Clause (ECAC) proceedings. However, the single proceeding would not be orderly or administrable, nor would it properly integrate QF pricing within the regulatory framework. ECAC proceedings develop a marginal cost forecast; marginal costs, in turn, are used in calculating variable QF payments. If we were to require the use of ECAC assumptions in a subsequent single proceeding for QF pricing, QFs would appear in ECACs to litigate those assumptions, and the subsequent proceeding would have little point. If we were to update those assumptions in the later proceedings, we would have essentially a new ECAC proceeding, just for QFs, but involving all three major electric utilities. There is no way to manage such a proceeding. The solution to this problem is not to create a unique proceeding for QFs, but rather to make optimal use of ECAC by setting QF prices at the same time (and from the same assumptions) that we adjust utility rates. Our adopted update procedure accomplishes this.

CORRECTION

THIS DOCUMENT HAS

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I. The Goals of Updating

The suspensions of interim Standard Offer 4 and of Standard Offer 2 illustrate the need for better ways to update the price and other terms of standard offers. Updating has three goals, which in turn shape the updating procedures that we adopt. First, updating must ensure that the fixed and variable prices of currently-available standard offers reflect current utility resource planning assumptions at appropriate intervals. Second, updating must be orderly and periodic, in order to avoid disruption, minimize administrative burdens, and integrate QF pricing and procurement within our overall regulatory structure for the electric utilities. Third, updating must be entirely prospective and without systematic bias; in other words, updating does not serve to recoup perceived over- or underpayments to QFs or to alter existing contracts. Properly implemented updating procedures will result, over time, in each utility holding a diverse portfolio of short-term and long-term QF contracts with payments that, for the portfolio as a whole, track the utility's avoided costs very closely.

We adopt the updating procedures shown in Table A. These procedures should meet our goals. Many of the procedures are already in place. For example, quarterly updating of the price of the marginal fuel has been a feature of the standard offer program from the beginning.

Table A also has some changes and innovations, but these will generally come as no surprise to parties that have followed the consolidated standard offer proceeding. For example, Decision (D.) 86-05-024 (at mimeo. pp. 15-16) has strong criticism of the general rate case (GRC) as a forum for updating. We have decided to no longer use the GRC for standard offer updating purposes. The GRC (now on a three-year cycle for PG&E, SDG&E, and Edison) is too infrequent and too crowded with other issues to be suitable for

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The second controversy concerns incremental energy rate (IER) updating for PG&E. PG&E supports the use of ECAC for updating variable QF payments, with one major reservation.[1] Specifically, PG&E would also adjust the IER each quarter, based on a narrower review of input assumptions than that performed in ECAC. The quarterly IER update would be done through preliminary and final filings (the same process used now for updating the price of the marginal fuel), and would be based exclusively on changes in hydro conditions, fuel prices, and nuclear plant refueling schedules. According to PG&E witness Hindley, the between-ECAC update would use the same energy balance determined from system simulation in PG&E's most recent ECAC decision; to compute the new IER for the coming quarter, the system would be modeled with all parameters _except_ hydro and nuclear availability and fuel price held constant. (See transcript pages 7967-69.)

We do not adopt PG&E's recommendation at this time. There are basically two reasons for our decision. First, selective updating, even where the assumptions to be updated are specified in advance, seems very susceptible to "gaming" by the parties. Also, there is often a legitimate question whether the selected assumptions can fairly or reasonably be changed without re-examining all other inputs, particularly where there is a marked shift from prior assumptions. The process envisioned by PG&E is not at all suited to any but the most straightforward adjustments. We suspect that the quarterly IER updates would draw many protests that would result in a miniature ECAC and create an intolerable burden on us and the parties.

1 PG&E also points out that standard offer methodological issues must not be introduced into ECAC. We agree. As indicated in Table A, methodological issues are reserved to our biennial resource plan review, where (unlike ECAC) statewide planning issues will be addressed.

Second, even if the process of selective updating were worked out satisfactorily, it is not clear that such updating is the optimal solution to the problem that PG&E is trying to address. That problem, as we see it, is to ensure that PG&E is able to dispatch its system so as to take full advantage of greater-than-forecast availability of energy from low-cost resources.[2] We have considered three strategies to address this problem, which is particularly significant for PG&E because of its relatively large dependence on as-available resources such as hydro. These strategies, in addition to more frequent IER updating, are real-time pricing and contractual performance features ("adders") such as curtailment and full dispatchability.

We have already approved curtailment adders in the context of negotiated contract amendments (see D.87-01-049) and in connection with development of final Standard Offer 4. We have also authorized PG&E, in consultation with interested QFs and others, to experiment with a voluntary real-time pricing program. (See D.86-12-091.) At this point, more work is necessary before we can choose definitively among these strategies, and it is possible that some combination of the strategies will be necessary in order to maximize net benefits.

Our present strong preference is for annual IER updating (which is a vast improvement over our historical practice of using the GRC for this purpose) and curtailment adders, with work continuing on real-time pricing. We are willing to reconsider PG&E's proposal for between-ECAC updating, provided that PG&E can

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2 Note that QFs themselves are paid on the basis of forecast conditions and thus provide the purchasing utility with price protection in case the actual availability of low-cost energy is <u>less</u> than the forecast. Note also that the problem is <u>not</u> over- or underpayments to QFs: assuming unbiased forecasts, QF payments over time will closely follow avoided costs, although the price signal to QFs does not instantaneously track the purchasing utility's marginal costs.

work out the substantial problems that we fear such updating would entail.[3] PG&E, if it wishes to pursue this, should do so in consultation with QFs. A procedure developed with the parties most directly affected would go far to allay our concerns.

III. Revision Date for Variable QF Payments

As a result of using ECACs to update utility capacity values and IERs, QFs will have different annual revision dates, depending on which utility purchases their output. This makes sense: a given QF project sells to only one utility, and there is no reason why all QF prices should change simultaneously throughout the state.

QF energy prices actually change every quarter (on February 1, May 1, August 1, and November 1), due to the quarterly update of the price of the marginal fuel. We have adhered strictly to our policy of not changing QF prices at any time other than these four dates, in order to give QFs some stability for planning their own operations. We will continue this policy and therefore adopt the following schedule for the annual revision dates for the new capacity value and IER calculated from assumptions adopted in the purchasing utility's current ECAC. If the effective date of the ECAC decision is at least 45 days from the next quarterly price revision date, then the new capacity value and IER will be included in that quarterly revision; if the effective date is less than 45 days from the next quarterly price revision date, then the new capacity value and IER will be included in the second quarterly

3 For QFs receiving variable energy payments, the frequency of IER updating is not fixed by contract. Thus, our decision to stick with annual IER updating for PG&E at this time can be changed later without that change constituting a retroactive amendment of the power purchase agreement. The forum for such reconsideration would be the biennial resource plan review.

revision following the ECAC. This is necessary to ensure that utilities have time to complete the preliminary and final price filings that we require in revising variable QF payments.[4]

IV. Fourth Time-of-Delivery Costing Period

We have previously approved a fourth costing period (super off-peak) in conjunction with QF payments. This is now in place for PG&E (see D.86-12-091, mimeo., p. 101), and we have directed SDG&E and Edison to develop a super off-peak on the same principles. (See D.87-05-060, mimeo., pp. 33-34.) SDG&E and Edison shall file their proposed costing periods 30 days after the effective date of today's decision. The new costing periods will take effect at the quarterly revision date at least 30 days following the initial filing. Consistent with Table A, the designation of costing periods will remain in effect until the next biennial resource plan review, at which time they are subject to possible revision.

V. Response to Comments on ALJ's Proposed Decision

Pursuant to Public Utilities Code § 311 and to our Rules of Practice and Procedure, the Proposed Decision of ALJ Kotz was issued before today's decision. Four parties (the Division of Ratepayer Advocates (DRA), PG&E, Edison, and Cogenerators of Southern California (CSC)) filed comments on the proposed decision,

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4 We are presently considering possible changes to the time schedules for the Rate Case Plan and fuel offset proceedings. (R.87-11-012.) These time schedules are likely to affect whether the new capacity value and IER are adopted in time for inclusion in the next quarterly QF price revision or in the second quarterly QF price revision following the ECAC.

and we have made a few modifications as a result of DRA's comments. We have also corrected typographical errors and added a cross-reference to our proceeding to revise our schedule for ECACs.

CSC apparently accepts the recommendation of the proposed decision that variable energy and variable capacity prices be updated annually in the purchasing utility's ECAC. However, CSC argues that, in the case of Edison, these prices should not be updated until the 1989 ECAC. CSC justifies this on the ground that these prices were recently updated in Edison's last GRC. (See D.87-12-066.) We reject CSC's argument. The infrequency of GRC updating has been the chief cause, if not the only one, of our having to suspend some of the standard offers. The transition to ECAC updating should be made at the first opportunity. This means that Edison's variable energy and capacity prices should both be updated in Edison's 1988 ECAC, even though the consequence is that the GRC prices for QFs will be in effect somewhat less than a full year;[5] the alternative (skipping the current ECAC) would keep the GRC prices for QFs in effect for <u>more</u> than a full year.

<u>Findings of Fact</u>

1. Standard offers must be updated regularly in order to ensure consistency with current resource planning assumptions, allow orderly development of the QF industry, minimize administrative burdens, and create a balanced and diverse portfolio of power purchase agreements.

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5 CSC claims that our Third Interim Opinion in this proceeding postponed the update of Edison's variable capacity prices to Edison's <u>1989</u> ECAC. CSC misreads that opinion, which contains nothing inconsistent with today's decision. We stress again our intention to update variable energy and capacity payments to QFs once each calendar year, in the ECAC proceedings of the respective utilities. Cf. Section II.B of the Third Interim Opinion ("We will update variable capacity payments each year").

2. The updating procedures summarized in Table A will meet the goals stated in Finding of Fact 1.

3. Limiting QF price changes to specific quarterly revision dates (February 1, May 1, August 1, and November 1) allows QFs to plan their operations with some certainty, consistent with the utilities' need for prompt and accurate updating.

4. A super off-peak costing period is in place for PG&E and is ripe for implementation at this time by SDG&E and Edison.

Conclusions of Law

1. The updating procedures summarized in Table A should be adopted.

2. The policy of limiting QF price changes to specific quarterly revision dates should continue.

3. SDG&E and Edison should implement a super off-peak costing period, to continue in effect unless revised in the next biennial resource plan review.

4. This order should take effect immediately in order to remove uncertainties on standard offer updating.

THIRD INTERIM ORDER - COMPLIANCE PHASE

IT IS ORDERED that:

1. The standard offer updating procedures summarized in Table A are adopted. Revision of these procedures will be considered only in the biennial resource plan review.

2. Changes to prices paid under standard offers shall go into effect only on the following quarterly revision dates: February 1, May 1, August 1, or November 1.

3. San Diego Gas & Electric Company and Southern California Edison shall file proposed costing periods, incorporating a super off-peak period pursuant to Decision 87-05-060, within 30 days of the effective date of today's decision. The new costing periods will take effect at the quarterly revision date that is at least 30 days following the filing of the proposed costing periods.

This order is effective today.

Dated March 9, 1988, at San Francisco, California.

STANLEY W. HULETT
President
DONALD VIAL
FREDERICK R. DUDA
G. MITCHELL WILK
JOHN B. OHANIAN
Commissioners

I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY.

Victor Weisser, Executive Director

Table A

Page 1

Standard Offer Updating

	Variable Capacity Payments***	Variable Energy Payments***
Offers affected:	S.O. 1, 3, final S.O. 4 (Period 1)	All except interim S.O. 4 (Some options)**
How often updated?	Annually	Quarterly (marginal or avoided plant fuel price) Annually (marginal efficiency)
Methodology:	Cost of combustion turbine, adjusted by EUE-based ERI (SDG&E, Edison), Target Reserve Margin (PG&E)*	Fuel price: Published data Marginal efficiency: IER calculated per CPUC decisions
Where updated?	ECAC	Fuel price: Utility energy price filings (similar to advice letters - no CPUC decision necessary unless protested) Marginal efficiency: ECAC

* The implementation of Target Reserve Margin for PG&E is subject to further comment.

** Interim S.O. 4 QFs generally have some or all of their energy payments fixed in their contracts for the first 10 years, after which they receive variable energy payments.

*** The payments for the increment of QFs being valued are calculated using QFs-in/QFs-out.

Table A

Page 2

Standard Offer Updating

	Fixed Capacity Payments***	Avoidable Resources
Offers affected:	S.O. 2	Final S.O. 4
How often updated?	Biennially	Biennially
Methodology:	Levelized cost of combustion turbine, adjusted by EUE-based ERI (SDG&E, Edison), Target Reserve Margin (PG&E)*; block pricing	Simplified Generation Resource Plan, Second-price Auction
Where updated?	Biennial review of utility resource plans.	Biennial review of utility resource plans.

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Table A

Page 3

Standard Offer Updating

	Non-price Terms; Methodology	Costing Periods for Time-Differentiated Prices
Offers affected:	All	All
How often updated?	Proposals to change standard offer methodology, or to prospectively revise non-price terms in new contracts, may be made by any party in the biennial review	Biennially
Methodology:	CPUC encourages consultation between utilities and QFs to develop joint recommendations wherever possible	Production cost modeling groups hours of similar cost
Where updated?	Biennial review of utility resource plans.	Biennial review of utility resource plans.

Table A

Page 4

Standard Offer Updating

Cost of Combustion Turbine

Offers affected:	S.O. 1, 2, 3, final S.O. 4 (Period 1)
How often updated?	Biennially****
Methodology:	See D.82-12-120
Where updated?	Biennial review of utility resource plans.

**** For rate design purposes, general rate cases also calculate the utility's cost of a combustion turbine.

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revision following the ECAC. This is necessary to ensure that utilities have time to complete the preliminary and final price filings that we require in revising variable QF payments.[4]

IV. Fourth Time-of-Delivery Costing Period

We have previously approved a fourth costing period (super off-peak) in conjunction with QF payments. This is now in place for PG&E (see D.86-12-091, mimeo., p. 101), and we have directed SDG&E and Edison to develop a super off-peak on the same principles. (See D.87-05-060, mimeo., pp. 33-34.) SDG&E and Edison shall file their proposed costing periods 30 days after the effective date of today's decision. The new costing periods will take effect at the quarterly revision date at least 30 days following the initial filing. Consistent with Table A, the designation of costing periods will remain in effect until the next biennial resource plan review, at which time they are subject to possible revision.

Findings of Fact

1. Standard offers must be updated regularly in order to ensure consistency with current resource planning assumptions, allow orderly development of the QF industry, minimize administrative burdens, and create a balanced and diverse portfolio of power purchase agreements.

2. The updating procedures summarized in Table A will meet the goals stated in Finding of Fact 1.

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4 It is conceivable that this revision date schedule could result in an as-available capacity price and IER being in effect for three quarters, or for five quarters, rather than exactly one year. This seems preferable to having to compress the utility price filings within a very short time span, which is likely to produce errors and unfairness.

3. Limiting QF price changes to specific quarterly revision dates (February 1, May 1, August 1, and November 1) allows QFs to plan their operations with some certainty, consistent with the utilities' need for prompt and accurate updating.

4. A super off-peak costing period is in place for PG&E and is ripe for implementation at this time by SDG&E and Edison.

Conclusions of Law

1. The updating procedures summarized in Table A should be adopted.

2. The policy of limiting QF price changes to specific quarterly revision dates should continue.

3. SDG&E and Edison should implement a super off-peak costing period, to continue in effect unless revised in the next biennial resource plan review.

4. This order should take effect immediately in order to remove uncertainties on standard offer updating.

FOURTH INTERIM ORDER - COMPLIANCE PHASE

IT IS ORDERED that:

1. The standard offer updating procedures summarized in Table A are adopted. Revision of these procedures will be considered only in the biennial resource plan review.

2. Changes to prices paid under standard offers shall go into effect only on the following quarterly revision dates: February 1, May 1, August 1, or November 1.

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FOURTH INTERIM ORDER - COMPLIANCE PHASE

IT IS ORDERED that:

1. The standard offer updating procedures summarized in Table A are adopted. Revision of these procedures will be considered only in the biennial resource plan review.

2. Changes to prices paid under standard offers shall go into effect only on the following quarterly revision dates: February 1, May 1, August 1, or November 1.

3. San Diego Gas & Electric Company and Southern California Edison shall file proposed costing periods, incorporating a super off-peak period pursuant to Decision 87-05-060, within 30 days of the effective date of today's decision. The new costing periods will take effect at the quarterly revision date that is at least 30 days following the filing of the proposed costing periods.

This order is effective today.

Dated ________________, at San Francisco, California.

Table A

Page 1

Standard Offer Updating

	Variable Capacity Payments***	Variable Energy Payments***
Offers affected:	S.O. 1, 3, final S.O. 4 (Period 1)	All except interim S.O. 4 (Some options)**
How often updated?	Annually	Quarterly (marginal or avoided plant fuel price) Annually (marginal efficiency)
Methodology:	Cost of combustion turbine, adjusted by EUE-based ERI (SDG&E, Edison), Target Capacity Factor (PG&E)*	Fuel price: Published data Marginal efficiency: IER calculated per CPUC decisions
Where updated?	ECAC	Fuel price: Utility energy price filings (similar to advice letters - no CPUC decision necessary unless protested) Marginal efficiency: ECAC

* The implementation of Target Capacity Factor for PG&E is subject to further comment.

** Interim S.O. 4 QFs generally have some or all of their energy payments fixed in their contracts for the first 10 years, after which they receive variable energy payments.

*** The payments for the increment of QFs being valued are calculated using QFs-in/QFs-out.

Table A

Page 2

Standard Offer Updating

	Fixed Capacity Payments***	Avoidable Resources
Offers affected:	S.O. 2	Final S.O. 4
How often updated?	Biennially	Biennially
Methodology:	Levelized cost of combustion turbine, adjusted by EUE-based ERI (SDG&E, Edison), Target Capacity Factor (PG&E)*; block pricing	Simplified Generation Resource Plan, Second-price Auction
Where updated?	Biennial review of utility resource plans.	Biennial review of utility resource plans.

*** The payments for the increment of QFs being valued are calculated using QFs-in/QFs-out.

Table A

Page 3

Standard Offer Updating

	Non-price Terms; Methodology	Costing Periods for Time-Differentiated Prices
Offers affected:	All	All
How often updated?	Proposals to change standard offer methodology, or to prospectively revise non-price terms in new contracts, be made by any party in the biennial review	Biennially
Methodology:	CPUC encourages consultation between utilities and QFs to develop joint recommendations wherever possible	Production cost modeling groups hours of similar cost
Where updated?	Biennial review of utility resource plans.	Biennial review of utility resource plans.

Table A

Page 4

Standard Offer Updating

Cost of Combustion Turbine

Offers affected:	S.O. 1, 2, 3, final S.O. 4 (Period 1)
How often updated?	Biennially****
Methodology:	See D.82-12-120
Where updated?	Biennial review of utility resource plans.

**** For rate design purposes, general rate cases also calculate the utility's cost of a combustion turbine.