

JUL 11 1988

ALJ/AVG/rsr

Decision SS 07 021 JUL 8 1988**ORIGINAL**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application Of )  
 The Southern California Edison )  
 Company (U 338-E) For (1) Authority )  
 To Change Its Energy Cost Adjustment )  
 Billing Factors And Its Electric )  
 Revenue Adjustment Billing Factor )  
 Effective June 1, 1987; (2) Author- )  
 ity, At Some Future Date, To Reduce )  
 Its Energy Cost Adjustment Clause )  
 Rates To Reflect Fuel And Energy )  
 Cost Savings Attributable To Palo )  
 Verde Nuclear Generating Station )  
 Unit 3 And Balsam Meadow, Coincident )  
 With Increases In Base Rates, Re- )  
 spectively; (3) Authority To )  
 Implement Other Modifications To Its )  
 Energy Cost Adjustment Clause And )  
 Its Electric Revenue Adjustment )  
 Mechanism As More Specifically Set )  
 Forth In This Application; (4) )  
 Review Of The Reasonableness Of )  
 Edison's Operations During The )  
 Period From December 1, 1985, )  
 Through November 30, 1986; And (5) )  
 Review Of The Reasonableness Of )  
 Edison Payments To Qualifying )  
 Facilities Under Non-Standard )  
 Contracts During The Period From )  
 December 1, 1984, Through )  
 November 30, 1986. )

Application 87-02-019  
 (Filed February 5, 1987)

(For appearances see Decision 87-11-013.)

### OPINION

#### Summary of Decision

We find Southern California Edison Company's (Edison) operations during the period December 1, 1985 to November 30, 1986 to be reasonable. Specifically, we conclude that:

1. The Stipulation and Agreement between the Division of Ratepayers (DRA) and Edison covering the cost of replacement fuel

and purchased power during an outage at San Onofre Nuclear Generating Station Unit 1 (SONGS-1) should be adopted.

2. Edison is entitled to a \$7,881,737 reward under the Coal Plant Incentive Procedure (CPIP) for operations at the Mohave Generating Station (Mohave) and the Four Corners Generating Station (Four Corners).

3. The CPIP has served its purpose and should be discontinued.

4. The Edison proposed additional Economic Modifier to the Nuclear Unit Incentive Procedure should be adopted.

5. Edison should aggressively pursue steps to achieve concessions from Arizona Public Service Company (APS) with regards to its Cholla-4 contract.

#### Background

On February 5, 1987, Edison filed Application (A.) 87-02-019 requesting, among other things, that the Commission find reasonable Edison's fuel and energy costs recorded in the Energy Cost Adjustment Clause (ECAC) Balancing Account from December 1, 1985 to November 30, 1986 "Record Period". Processing of the application was initially split into three phases: Phase I - a review of the forecast of operations for the period June 1, 1987 through May 31, 1988, Phase II - a review of the reasonableness of operations for the Record Period, and Phase III - a review of the reasonableness of Edison's purchased power expenses under nonstandard Qualified Facilities (QF) contracts for the 1985 and 1986 record period. Based on a request by the parties, the Administrative Law Judge (ALJ) removed the reasonableness review of Edison's nonstandard QF contracts from this proceeding to Edison's pending ECAC proceeding A.88-02-016.

Hearings in Phase I of the proceedings were held before ALJ Barnett. The Commission issued Decision (D.) 87-11-013 in that phase. Hearings in Phase II, the reasonableness phase, were held

before ALJ Garde on January 13, 1988. This decision addresses Phase II issues.

There was substantial agreement among the parties of this proceeding concerning the reasonableness of Edison's operations during the record period. There are, however, five specific issues which require separate discussion. In this decision we will resolve each of these five issues separately and then deal in summary with remaining reasonableness issues. The five separate issues are listed below:

1. SONGS disallowance.
2. CPIP reward.
3. CPIP program reevaluation.
4. Economic Modifier to Nuclear Unit Incentive Procedure.
5. Cholla-4 Contract.

SONGS-1 Outage

In November 1986, SONGS-1 had an eight-day forced outage. Edison was cited and fined \$180,000 by the Nuclear Regulatory Commission for three violations arising from the investigation of the outage. DRA recommended a disallowance of \$798,682 for the cost of replacement fuel and purchased power during the outage. Edison opposed DRA's recommendation for a disallowance on the basis that no generation was lost due to this outage because it had scheduled a refueling outage during that period.

DRA, Edison, and San Diego Gas and Electric Company (SDG&E) reached agreement on a settlement of DRA's proposed disallowance for the replacement fuel and purchased power expenses related to the eight-day SONGS-1 outage. On January 20, 1988, DRA, Edison, and SDG&E filed a Stipulation and Agreement and a joint motion requesting its adoption. Copies of the Stipulation and Agreement were served on all parties to Edison's and SDG&E's ECAC applications. No party filed comments or objections.

The parties recommend that the Commission adopt a disallowance of \$798,682 (plus interest at the ECAC Balancing

Account rate from June 1, 1986 to the effective date of this decision) to Edison's ECAC Balancing Account and a disallowance of \$226,034 (plus interest at the ECAC Balancing Account rate from June 1, 1986 to the effective date of this decision) to SDG&E's ECAC Balancing Account.

Other provisions of the Stipulation and Agreement are:

1. DRA's and Edison's exhibits previously identified will be admitted into evidence in A.87-02-019 without objection from any Party;
2. Upon approval of the Stipulation and Agreement by the Commission, Edison and SDG&E will adjust their respective ECAC Balancing Account balances according to DRA's proposed disallowances in each ECAC proceeding;
3. Edison and SDG&E will provide notice of this Stipulation and Agreement to their respective ECAC service lists; and
4. The Stipulation and Agreement does not constitute approval of, or precedent regarding, any principle or issue in this proceeding and shall not be used as evidence by DRA or any other party in another proceeding.
5. Edison and SDG&E expressly do not concede that DRA's proposed disallowance is correct, valid, or justified in any way. While agreeing to accept the DRA-recommended disallowance, Edison and SDG&E expressly do not concede that any management imprudence was responsible for the outage period at issue.
6. The Stipulation and Agreement is solely in settlement of DRA's claim for a disallowance of replacement fuel and purchase power expenses occurring during the period from November 21, 1985 through November 30, 1986. The settlement does not cover any potential disallowances for other types of costs associated with the SONGS-1

outage, whenever those costs were incurred, or replacement fuel and purchase power expenses incurred after November 30, 1986.

7. The Stipulation and Agreement is entered into by the parties on the basis that it be adopted in its entirety without modification by the Commission.
8. If the Commission approves this Stipulation and Agreement, but imposes any modifications or conditions thereto, the Stipulation and Agreement shall not become effective as to any party unless the party agrees in writing to accept the modifications or conditions within 30 days of the Commission decision.
9. The Stipulation and Agreement shall become effective when a Commission decision approving it is issued.

#### Discussion

We believe that this Stipulation and Agreement will resolve the issue of the SONGS-1 outage. We also believe that it is a reasonable settlement because it accepts DRA's recommended disallowance and avoids further litigation. Therefore, we will adopt it.

We will address only Edison's share of disallowance in this order. SDG&E's share of disallowance should be addressed in SDG&E's next ECAC proceeding.

#### Reward Under The Coal Plant Incentive Procedure

The CPIP was implemented by D.93363 to provide an incentive to improve the efficiency of Edison's coal plants. It is designed to provide for the possibility of reward or penalty, or neither reward nor penalty, based on the actual performance of the coal plants. The CPIP standard of performance is the gross capacity factor reached by the coal plant over four years. The CPIP procedure established a "null zone" for the gross capacity factor. If the coal plant gross capacity factor is less than the

lower limit of the null zone, Edison is penalized. Edison is entitled to a reward if the coal plant gross capacity factor exceeds the upper limit of the null zone.

In D.86-04-059 Edison was authorized to record the reward earned under the CPIP for the 1984 record period. The decision also ordered a reexamination of the CPIP because the coal plants have regularly exceeded the gross capacity factor standard. Pending receipt of the study, the null zone was expanded from  $\pm 3\%$  to  $\pm 8\%$ .

Edison filed an application for rehearing of D.86-04-059 with respect to the modification of the CPIP null zone for the 1985 record period. D.86-08-035 denied a rehearing of D.86-04-059, however, it did not foreclose Edison from raising this issue in A.86-02-011 or seeking judicial review on that issue. D.87-08-081 also in A.86-02-011 concluded that the expanded null zone of  $\pm 8\%$  should be applied prospectively from the effective date of D.86-04-059.

The reward for the Record Period is computed by applying a null zone of  $\pm 8\%$  to coal plant performance after the effective date of D.86-04-059. The gross capacity factor for Edison's coal plant exceeded the upper limit of the null zone during the Record Period. Therefore, DRA and Edison agree that Edison should receive a CPIP reward for the Record Period computed as follows:

Mohave Unit 1	\$ -
Mohave Unit 2	717,566
Four Corners Unit 4	2,570,178
Four Corners Unit 5	<u>4,593,993</u>
Total	\$7,881,727

Discussion

We agree with DRA and Edison that a \$7,881,737 reward under the CPIP for the Record Period is reasonable and should be adopted.

Coal Plant Incentive Procedure Reexamination

D.86-04-059 ordered Edison to submit with its 1987 ECAC application a study of the entire CPIP. Accordingly, Edison provided DRA a report prepared by Pickard, Lowe and Garrick, Inc. (PL&G).

According to DRA, a review of the PL&G report shows that most of the improvements at Mohave and Four Corners have been accomplished since implementation of the CPIP. DRA contends that the PL&G report also indicates that the benefit-to-cost ratio of the CPIP to the ratepayer has drastically decreased. DRA believes that this is an indication that the CPIP has achieved its purpose and is no longer required.

DRA has also analyzed the current state of the CPIP and concluded it should be revoked for the following reasons:

- o The objective of improving the efficiency of coal plants has been achieved at both Mohave and Four Corners plants.
- o The price differential between coal and gas/oil has decreased and fuel cost savings through the use of coal will be very low. Since the price of fuel is no longer at issue, it may be economical to burn low cost gas/oil in Edison's generating units, thus saving the ratepayers the additional expense of rewards for Edison.
- o Edison cannot use coal plant generation for base load requirements because it has enough low cost purchased power and hydro power available during off-peak hours.
- o Edison has received large awards under the CPIP.

- o Edison has received awards for Mohave even when the plant did not produce power.

Therefore, DRA recommends that the CPIP be revoked. If the CPIP were to be continued, DRA recommends that it be applied only to Mohave since Four Corners is operated by Arizona Public Service Company (APS) and is not subject to Edison control.

While not in agreement with the bases supporting DRA's recommendation, Edison agrees that the CPIP should be revoked. Edison contends that:

- o An incentive program is unnecessary to provide an incentive to Edison to provide less cost energy to its ratepayers;
- o Consistent with system operating constraints, Edison emphasizes the need for reliability of its coal-fired generating units to minimize cost; and
- o Although the cost differential between average coal and oil and gas has decreased in the last two years, coal generation is less expensive and Edison maximizes coal-produced energy.

Edison also does not agree with DRA's recommendation that if the Commission desires to continue the CPIP, that it apply only to Mohave. According to Edison, although it is not the operator of Four Corners, Edison is represented on the committees which control the operation of the plant. Edison claims that it has a significant influence over plant operation, however, not as direct as its control over Mohave. Edison believes that for purposes of termination or continuation of the CPIP, Mohave and Four Corners should be treated consistently.

#### Discussion

We believe that the CPIP has achieved its main objective of improving the thermal efficiency of the coal plants. Following its introduction in 1981, the CPIP provided a mechanism for risk



and benefit sharing between Edison and its ratepayers from the improved coal plant performance.

We now believe that the current narrowing of the price differential between coal and gas/oil has greatly reduced the benefits of the procedure. Therefore, we will revoke the CPIP for Mohave as well as Four Corners effective immediately.

It should be noted that the CPIP will remain in effect until the effective date of the revocation. Therefore, the performance of Edison's coal plants will remain subject to the provisions of the CPIP from the end of this record period (November 30, 1986) until the effective date of the revocation. This resolution of the issue will apply to all Edison's coal units including Mohave Units 1 and 2 which suffered an outage due to the June 9, 1985 accident. The Commission has instituted an investigation of the accident in I.86-04-002. ✓

Economic Modifier to the  
Nuclear Unit Incentive Procedure ✓

Edison proposes to establish an additional Economic Modifier to its Nuclear Unit Incentive Procedure when it is necessary to change a SONGS Unit's refueling outage schedule to meet the system reliability needs of one or more SONGS Parties. This Economic Modifier would provide for an adjustment to the calculation of the Incentive Period Gross Capacity Factors applicable to the SONGS Units 1, 2, and 3.

On February 26, 1987, Edison, SDG&E, the City of Anaheim, and the City of Riverside executed the Second Amended San Onofre Operating Agreement (Operating Agreement) and the San Onofre Refueling Exchange Agreement (Refueling Agreement). The Operating Agreement sets forth the manner in which SONGS Units will be operated for the benefit of all SONGS Parties. The Refueling Agreement governs exchanges of energy and capacity between SONGS Parties when a scheduled refueling outage date is changed by the election of one or more of the SONGS Parties. The effect of the

Refueling Agreement is that the SONGS Parties (and their ratepayers) not participating in the election to change a scheduled refueling outage remain indifferent to the change.

Edison believes that the proposed Economic Modifier should be adopted for the following reasons:

1. It recognizes needed operating flexibility. The modifier permits operation of the SONGS Units for the benefit of all of the SONGS Parties and their ratepayers;
2. The Modifier eliminates or reduces the possibility of an unwarranted Nuclear Incentive Procedure penalty when a refueling outage schedule change is consistent with the above; and
3. Edison has the burden of proof to demonstrate that its ratepayers were not adversely impacted by a SONGS refueling outage schedule change at such time that the proposed Economic Modifier is claimed.

There was no opposition to Edison's proposed modification to the Nuclear Unit Incentive Procedure.

#### Discussion

We believe that the proposed Economic Modifier is necessary to prevent Edison from incurring a penalty under its Nuclear Unit Incentive Procedure by allowing operation of the SONGS Units for the benefit of other SONGS Parties pursuant to the Operating Agreement or the Refueling Agreement. Currently, the two existing Economic Modifiers explicitly address only the impacts on Edison's system and result in changes to the operation of a SONGS unit. The existing Economic Modifiers do not address conditions requiring a refueling outage schedule change for system reliability purposes on another SONGS Party's system. Therefore, we will adopt the Economic Modifier proposed by Edison.

#### The Cholla-4 Contract

DRA recommends that the Commission order Edison to renegotiate or terminate the Cholla-4 contract. DRA does not

recommend any disallowance related to the Cholla-4 contract. Edison opposes DRA's recommendation.

In February 1980 Edison agreed to purchase electricity from APS under the Cholla-4 contract. The contract had a termination date of May 31, 1989 with provisions for extension. The Cholla-4 contract is a dedicated unit contract which committed APS to build Unit 4 at its coal-fired steam electric Cholla Plant and Edison to pay fixed charges to cover the ownership and operating costs of the unit during the life of the contract. The energy price is based on the contract price of coal charged to APS. Energy deliveries began in June 1984 at 123 megawatts (MW) and rose to the contract capacity of 350 MW in June 1985. The fixed contract charges are based on the operating and maintenance expenses, working capital, ad valorem taxes and the rate of return on the rate base allowed by the Federal Energy Regulatory Commission for this unit. The relevant rate base is normally reduced each year; however, it can be increased to account for capital improvements elected by APS.

In October 1983 the termination date of the Cholla-4 contract was amended to May 31, 1990.

DRA contends that during the Record Period the payments for energy under the Cholla-4 contract exceed Edison's avoided cost of the same quantity of energy by approximately \$33.8 million. DRA asserts that its calculations of excess payments are conservative. According to DRA, gas prices are expected to remain reasonably stable through the life of Cholla-4 contract and so these excess payments are likely to continue. DRA maintains that Cholla-4 is Edison's highest priced firm energy inter-utility contract. ✓

Edison contends that it has demonstrated that the Cholla-4 contract was reasonable when executed and amended based upon facts known when executed and that it is unlikely that renegotiation or termination of the contract would benefit the ratepayers.

Edison maintains that under the terms of the Cholla-4 contract, it can schedule the energy deliveries and has the right to modify deliveries on an hourly basis to accommodate its system operating conditions. Edison can also coordinate the annual maintenance schedule of Cholla-4 with APS to assure optimal availability of the unit.

Edison contends that it entered into the Cholla-4 contract based upon an identified need to supply a portion of the expected demands for capacity and associated energy on its system for the years 1984 through 1989. According to Edison, at the time of entering the contract, forecasted Cholla-4 capacity and energy expense was less than forecasts of available alternatives over the term of the contract. Edison argues that the appropriate standard of reasonableness requires that its actions be reviewed based upon what was known by its management at the time the contract was executed. Edison points out that DRA made no evaluation of the reasonableness of the Cholla-4 contract or its amendments at the time of execution. In fact, Edison asserts that for the purpose of its recommendation, DRA is not concerned with the reasonableness of the contract.

Edison disagrees with DRA's recommendation that the Cholla-4 contract should be renegotiated or terminated simply because Edison's payments during the Record Period were more than DRA's estimate of Edison's avoided cost. Edison argues that DRA's approach applies a new standard each year to a long-term contract, does not consider the cost of renegotiation or termination, and makes no attempt to analyze the contract based on conditions at the time of execution. Thus, DRA failed to apply the appropriate standard of reasonableness to its examination of the Cholla-4 contract.

Edison recognizes the fact that Cholla-4 energy is more expensive than its other inter-utility long-term purchase power

agreements. Edison claims that in accordance with prior Commission statements, it has attempted to achieve some concessions from APS.

DRA believes that Edison opposes its recommendation regarding the Cholla-4 contract largely because it misunderstands the recommendation. DRA agrees with Edison's contention that prudence of a contract must be judged by the facts the utility knew or could have known when it entered onto the contract. That is why, DRA maintains that it is not recommending a disallowance; it is merely recommending contract renegotiation or termination.

DRA also points out that its recommendation does not require Edison to renegotiate or terminate the contract if it is uneconomic to do so.

#### Discussion

It is clear from the record that for the Record Period payments for energy under the Cholla-4 contract exceed Edison's avoided cost of the same quantity of energy by \$33.8 million. Therefore, purchases of energy from Cholla-4 were not cost-effective during the Record Period. We recognize that the energy purchases from Cholla-4 have been cost-effective in the past, but the future cost-effectiveness of the Cholla-4 contract is dependent on the price of fossil fuel and cannot be predicted with certainty at this time. ✓

We note that Edison has met with APS on three separate occasions in 1986 to renegotiate the contract with APS. The exact nature of Edison's attempt to renegotiate the contract is not clear. However, we do know that APS declined to discuss renegotiation of the contract.

We share DRA's concern about the high cost of energy from Cholla-4 and reiterate our position that for long-term contracts a utility has the duty to monitor and assess the value of the contract from year to year throughout its remaining term and to take every reasonable step to protect the interests of the ratepayers. In keeping with our policy regarding long-term

contracts, we require Edison to assess the cost of terminating the Cholla-4 contract and, with its next ECAC filing, provide a complete description of its efforts to renegotiate the contract and a report on the cost of such a termination. Edison's report should contain its analysis of the economic benefits to the ratepayers supporting whatever decision it makes regarding the Cholla-4 contract.

Summary of The Remaining Reasonableness Phase Issues

A summary of DRA's position regarding the remaining reasonableness phase issues is as follows:

1. Hydroelectric Generation

According to DRA's analysis, Edison's hydroelectric generation expenses during the Record Period were reasonable.

2. Coal Generation

DRA found that Edison's expenses for coal and gas burned at Mohave and at Four Corners during the Record Period were reasonable.

3. Nuclear Generation and Price

DRA found nuclear generation and costs during the Record Period to be reasonable except for replacement energy expenses for an eight-day period for SONGS Unit 1 discussed earlier.

DRA also recommended that the reasonableness of uranium ore costs be subject to the Commission's decision in Order Instituting Investigation (I.) 85-05-002. D.87-10-042 in that proceeding found Edison's purchases of uranium ore to be reasonable.

In addition, DRA recommends that no final judgment be made on the reasonableness of any replacement fuel costs for SONGS Units 2 and 3 until the reasonableness review of SONGS Units 2 and 3 post commercial operating date costs have been completed.

4. Purchased Power

DRA found that Edison's expenses for economy energy purchases for the Record Period were reasonable. For firm purchased power expenses, DRA does not recommend any disallowance. However, DRA recommends that the Commission order Edison to renegotiate or terminate the Cholla-4 contract as discussed earlier.

5. Cogeneration

As stated previously, review of Edison's purchases from cogenerators for the 1985 and 1986 Record Periods has been deferred to be held in Edison's pending ECAC proceeding A.88-02-016.

6. Fossil Fuel Generation and Heat Rate

DRA found Edison fossil plant outages for the Record Period to be reasonable.

The Commission indicated an interest in the heat rate performance of Edison's fossil fuel units and in D.86-04-059 recommended that Edison adopt a heat rate deviation method similar to that adopted for Pacific Gas and Electric Company (PG&E). In order to evaluate heat rate performance, Edison proposed an Efficiency Deviation Method. This method serves as a performance standard and provides a measurement of the improvements in heat rate efficiency.

The Efficiency Deviation Method is based on changes from historic performance utilizing individual unit hourly operating information to establish theoretical fuel consumption. This theoretical fuel use is then compared against actual fuel consumption to determine deviation from theoretical.

DRA agreed that the Efficiency Deviation Method is a reasonable approach; however, DRA believes that heat rate improvement should be measured in BTU/kWh and not by the percentage method used by Edison.

Edison and DRA subsequently agreed to use the 1984 and 1985 recorded system heat rate data, including Redondo Units 7 and 8, as the base for the Efficiency Deviation Method. Edison provided tables which reflect both the percentage and BTU/KWh deviations from the recorded 1984 through 1985 base heat rate standard.

7. Natural Gas Expenses

DRA agreed that Edison's natural gas expense was reasonable.

8. Fuel Oil Expense

In D.87-06-021, the Commission ordered a disallowance of 10 percent of the Chevron Option Agreement Demand charges which were \$520,000 for the Record Period. DRA agreed that Edison's August 1986 Low Sulfur Fuel Oil burn of 993,000 barrels was reasonable and that Edison's fuel oil carrying charges were reasonable.

Discussion

As this summary indicates, there is agreement that Edison's operations during the Record Period, except as discussed earlier, were reasonable. We concur with Edison's showing and the DRA's analysis.

Comments on the Proposed Decision

Edison and DRA have filed comments on the ALJ's proposed decision. They have also filed responses to each other's comments. Based on our review, we believe that the following modifications to the decision, other than correction of typographical errors, should be made:

1. Effective Dates for Revocation of the  
CPIP and Adoption of the Economic  
Modifier to the Nuclear Unit  
Incentive Procedure

The proposed decision revokes the CPIP on the effective date of the order. The proposed decision also adopts an Economic Modifier to the Nuclear Unit Incentive Procedure.



Edison points out that since the CPIP and the Nuclear Incentive Procedure are included in its tariffs, it will need to file advice letters to remove the CPIP and add the Economic Modifier to the Nuclear Unit Incentive Procedure. Therefore, Edison requests that the ordering paragraphs be modified to allow it five days after the effective date of the order to file the advice letters. Edison also requests that any reward or penalty under the existing CPIP and the Nuclear Unit Incentive Procedure should be calculated using the existing procedures until the advice letters are filed.

We agree with Edison's request and accordingly will modify Ordering Paragraph 1 as follows:

- "1. The Coal Plant Incentive Procedure (CPIP) for Southern California Edison Company's (Edison) Mohave Generating Station and Four Corners Generating Station shall be revoked. Edison shall file revised tariffs implementing this order within five days of the effective date of this decision. The revocation of the CPIP shall be effective upon filing of the revised tariffs."

We will also add the following ordering paragraph to adopt the Economic Modifier to the Nuclear Unit Incentive Procedure:

"Edison's Nuclear Unit Incentive Procedure shall be modified to establish an additional economic Modifier when it is necessary to change a SONGS Unit's refueling outage schedule to meet the system reliability needs of one or more SONGS parties. Edison shall file revised tariffs implementing this order within five days of the effective date of this decision. The modification of the Nuclear Unit Incentive Procedure shall be effective upon filing of the revised tariffs."

#### The Cholla 4 Contract

DRA recommends that with respect to the Cholla-4 contract, the decision should add the following language:

"Any decision to revise or terminate the Cholla-4 contract, or to continue it unchanged, shall be in the economic interest of Edison's ratepayers."

DRA believes that this message is strongly implied by the proposed decision. However, DRA requests that it be made explicit.

We agree with DRA and accordingly add the following language to the first paragraph on page 14:

"Edison's report should contain its analysis of the economic benefits to the ratepayers supporting whatever decision it makes regarding the Cholla-4 contract."

The proposed decision orders Edison to file a report on the cost of terminating the Cholla-4 contract with its next ECAC filing. Edison requests that this information be held in confidence otherwise it would adversely affect Edison's ability to obtain concessions from APS in further discussions regarding the Cholla-4 contract.

We believe that Edison's request, if appropriate, is premature. Therefore, we will not grant it.

#### Findings of Fact

1. DRA finds Edison's expenses for coal and gas burned during the Record Period at Mohave and Four Corners to be reasonable.
2. DRA recommends that for the Record Period, Edison be granted a reward of \$7,881,737 under the CPIP .
3. DRA recommends that the CPIP be revoked until such time that conditions warrant reinstitution of this incentive program. In the alternative, DRA recommends that the CPIP apply only to Mohave.
4. Edison agrees with DRA that the CPIP be revoked for both Mohave and Four Corners.
5. The CPIP has achieved its objective of improving coal plant performances.

6. DRA and Edison have filed a Stipulation and Agreement which settles DRA-recommended disallowance for replacement energy during a SONGS-1 outage in November, 1986.

7. The Stipulation and Agreement recommends that the Commission adopt a disallowance of \$798,682 (plus interest at the ECAC Balancing Account rate from June 1, 1986 to the effective date of this order) to Edison's ECAC Balancing Account.

8. The Stipulation and Agreement is a reasonable settlement of the SONGS-1 outage issue and is fair to Edison's ratepayers.

9. There is no opposition to the Stipulation and Agreement regarding the SONGS-1 outage.

10. DRA and Edison have agreed to use the 1984 and 1985 recorded system heat rate data, including Redondo Units 7 and 8, as the base for the Efficiency Deviation Method.

11. DRA agrees that the Edison proposed Efficiency Deviation Method to evaluate the heat rate performance of Edison's fossil fuel generating units is reasonable.

12. Edison proposes to establish an additional Economic Modifier to the Nuclear Unit Incentive Procedure when a SONGS Unit's refueling outage schedule is changed to meet the system reliability needs of one or more SONGS Parties.

13. Adoption of the proposed Economic Modifier to the Nuclear Unit Incentive Procedure will not have adverse impact on Edison's ratepayers.

14. There is no opposition to Edison's proposed modification to the Nuclear Unit Incentive Procedure.

15. DRA recommends that Edison be ordered to renegotiate or terminate Cholla-4 contract with APS mainly because the cost of energy from Cholla-4 exceeds Edison's current avoided costs.

16. Edison disagrees with DRA's recommendation regarding the Cholla-4 contract.

17. The Cholla-4 contract was reasonable when executed and amended.

18. Edison has attempted to renegotiate the Cholla-4 contract.

19. Other than the issues discussed in the preceding findings of fact, DRA finds Edison's operations during the Record Period to be reasonable.

Conclusions of Law

1. The CPIP for Edison's Mohave and Four Corner plants should be revoked.

2. Edison should be awarded a reward of \$7,881,737 under the CPIP.

3. The Stipulation and Agreement filed by DRA and Edison should be adopted.

4. Edison's ECAC Balancing Account should be reduced by \$798,682 (plus interest at the ECAC Balancing Account rate from June 1, 1986 to the effective date of this order) to account for the replacement energy during SONGS-1 outage.

5. Edison should continue to try to achieve concessions from APS regarding the Cholla-4 contract and should file a report describing in detail its efforts to do this. Edison should also file a report on the cost of terminating the Cholla-4 contract with its next ECAC filing.

6. Subject to the observations made by the Commission as set forth here, Edison's operations during the period December 1, 1985 to November 30, 1986 were reasonable.

ORDER

IT IS ORDERED that:

1. The Coal Plant Incentive Procedure for Southern California Edison Company's (Edison) Mohave Generating Station and Four Corners Generating Station shall be revoked. Edison shall file revised tariffs implementing this order within five days of

the effective date of this decision. The revocation of the CPIP shall be effective upon filing of the revised tariffs.

2. Edison's ECAC Balancing Account shall be reduced by \$798,682 plus interest at the ECAC Balancing Account rate from June 1, 1986 to the effective date of this order.

3. Edison shall be awarded a reward of \$7,881,737 under the Coal Plant Incentive Procedure and its ECAC balancing account shall be adjusted accordingly. ✓

4. Edison shall continue to try to achieve concessions from APS regarding the Cholla-4 contract and shall file a report in its next ECAC proceeding describing in detail its efforts to do this. Edison shall also file a report on the cost of terminating the Cholla-4 contract with its next ECAC filing.

5. Edison's Nuclear Unit Incentive Procedure shall be modified to establish an additional Economic Modifier when it is necessary to change a SONGS Unit's refueling outage schedule to meet the system reliability needs of one or more SONGS parties. Edison shall file revised tariffs implementing this order within five days of the effective date of this decision. The modification of the Nuclear Unit Incentive Procedure shall be effective upon filing of the revised tariffs.

6. This proceeding is concluded.  
This order is effective today.

Dated July 8 1988, at San Francisco, California.

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

Commissioner Frederick R. Duda,  
being necessarily absent, did not  
participate.

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

*Victor Weiss*  
Victor Weiss, Executive Director

lower limit of the null zone, Edison is penalized. Edison is entitled to a reward if the coal plant gross capacity factor exceeds the upper limit of the null zone.

In D.86-04-059 Edison was authorized to record the reward earned under the CPIP for the 1984 record period. The decision also ordered a reexamination of the CPIP because the coal plants have regularly exceeded the gross capacity factor standard. Pending receipt of the study, the null zone was expanded from  $\pm 3\%$  to  $\pm 8\%$ .

Edison filed an application for rehearing of D.86-04-059 with respect to the modification of the CPIP null zone for the 1985 record period. D.86-08-035 denied a rehearing of D.86-04-059, however, it did not foreclose Edison from raising this issue in A.86-02-011 or seeking judicial review on that issue. D.87-08-081 also in A.86-02-011 concluded that the expanded null zone of  $\pm 8\%$  should be applied prospectively from the effective date of D.86-04-059.

The reward for the Record Period is computed by applying a null zone of  $\pm 8\%$  to coal plant performance after the effective date of D.86-04-059. The gross capacity factor for Edison's coal plant exceeded the upper limit of the null zone during the Record Period. Therefore, DRA and Edison agree that Edison should receive a CPIP reward for the Record Period computed as follows:

Mohave Unit 1	\$ -0-
Mohave Unit 2	7717.566
Four Corners Unit 4	2,570,178
Four Corners Unit 5	<u>4,593,993</u>
Total	\$ 7,881,737

and benefit sharing between Edison and its ratepayers from the improved coal plant performance.

We now believe that the current narrowing of the price differential between coal and gas/oil has greatly reduced the benefits of the procedure. Therefore, we will revoke the CPIP for Mohave as well as Four Corners effective immediately.

It should be noted that the CPIP will remain in effect until the effective date of this order. Therefore, the performance of Edison's coal plants will remain subject to the provisions of the CPIP from the end of this record period (November 30, 1986) until the effective date of this order. This resolution of the issue will apply to all Edison's coal units including Mohave Units 1 and 2 which suffered an outage due to the June 9, 1985 accident. The Commission has instituted an investigation of the accident in I.86-04-002.

Economic Modifier to the  
Nuclear Unit Incentive Procedure

Edison proposes to establish an additional Economic Modifier to its Nuclear Unit Incentive Procedure when it is necessary to change a SONGS Unit's refueling outage schedule to meet the system reliability needs of one or more SONGS Parties. This Economic Modifier would provide for an adjustment to the calculation of the Incentive Period Gross Capacity Factors applicable to the SONGS Units 1, 2, and 3.

On February 26, 1987, Edison, SDG&E, the City of Anaheim, and the City of Riverside executed the Second Amended San Onofre Operating Agreement (Operating Agreement) and the San Onofre Refueling Exchange Agreement (Refueling Agreement). The Operating Agreement sets forth the manner in which SONGS Units will be operated for the benefit of all SONGS Parties. The Refueling Agreement governs exchanges of energy and capacity between SONGS Parties when a scheduled refueling outage date is changed by the election of one or more of the SONGS Parties. The effect of the

recommend any disallowance related to the Cholla-4 contract. Edison opposes DRA's recommendation.

In February 1980 Edison agreed to purchase electricity from APS under the Cholla-4 contract. The contract had a termination date of May 31, 1989 with provisions for extension. The Cholla-4 contract is a dedicated unit contract which committed APS to build Unit 4 at its coal-fired steam electric Cholla Plant and Edison to pay fixed charges to cover the ownership and operating costs of the unit during the life of the contract. The energy price is based on the contract price of coal charged to APS. Energy deliveries began in June 1984 at 123 megawatts (MW) and rose to the contract capacity of 350 MW in June 1985. The fixed contract charges are based on the operating and maintenance expenses, working capital, ad valorem taxes and the rate of return on the rate base allowed by the Federal Energy Regulatory Commission for this unit. The relevant rate base is normally reduced each year; however, it can be increased to account for capital improvements elected by APS.

In October 1983 the termination date of the Cholla-4 contract was amended to May 31, 1990.

DRA contends that during the Record Period the payments for energy under the Cholla-4 contract exceed Edison's avoided cost of the same quantity of energy by approximately \$33 million. DRA asserts that its calculations of excess payments are conservative. According to DRA, gas prices are expected to remain reasonably stable through the life of Cholla-4 contract and so these excess payments are likely to continue. DRA maintains that Cholla-4 is Edison's highest priced firm energy inter-utility contract.

Edison contends that it has demonstrated that the Cholla-4 contract was reasonable when executed and amended based upon facts known when executed and that it is unlikely that renegotiation or termination of the contract would benefit the ratepayers.



agreements. Edison claims that in accordance with prior Commission statements, it has attempted to achieve some concessions from APS.

DRA believes that Edison opposes its recommendation regarding the Cholla-4 contract largely because it misunderstands the recommendation. DRA agrees with Edison's contention that prudence of a contract must be judged by the facts the utility knew or could have known when it entered onto the contract. That is why, DRA maintains that it is not recommending a disallowance; it is merely recommending contract renegotiation or termination.

DRA also points out that its recommendation does not require Edison to renegotiate or terminate the contract if it is uneconomic to do so.

#### Discussion

It is clear from the record that for the Record Period payments for energy under the Cholla-4 contract exceed Edison's avoided cost of the same quantity of energy by \$33.7 million. Therefore, purchases of energy from Cholla-4 were not cost-effective during the Record Period. We recognize that the energy purchases from Cholla-4 have been cost-effective in the past, but the future cost-effectiveness of the Cholla-4 contract is dependent on the price of fossil fuel and cannot be predicted with certainty at this time.

We note that Edison has met with APS on three separate occasions in 1986 to renegotiate the contract with APS. The exact nature of Edison's attempt to renegotiate the contract is not clear. However, we do know that APS declined to discuss renegotiation of the contract.

We share DRA's concern about the high cost of energy from Cholla-4 and reiterate our position that for long-term contracts a utility has the duty to monitor and assess the value of the contract from year to year throughout its remaining term and to take every reasonable step to protect the interests of the ratepayers. In keeping with our policy regarding long-term

contracts, we require Edison to assess the cost of terminating the Cholla-4 contract and, with its next ECAC filing, provide a complete description of its efforts to renegotiate the contract and a report on the cost of such a termination.

Summary of The Remaining Reasonableness Phase Issues

A summary of DRA's position regarding the remaining reasonableness phase issues is as follows:

1. Hydroelectric Generation

According to DRA's analysis, Edison's hydroelectric generation expenses during the Record Period were reasonable.

2. Coal Generation

DRA found that Edison's expenses for coal and gas burned at Mohave and at Four Corners during the Record Period were reasonable.

3. Nuclear Generation and Price

DRA found nuclear generation and costs during the Record Period to be reasonable except for replacement energy expenses for an eight-day period for SONGS Unit 1 discussed earlier.

DRA also recommended that the reasonableness of uranium ore costs be subject to the Commission's decision in Order Instituting Investigation (I.) 85-05-002. D.87-10-042 in that proceeding found Edison's purchases of uranium ore to be reasonable.

In addition, DRA recommends that no final judgment be made on the reasonableness of any replacement fuel costs for SONGS Units 2 and 3 until the reasonableness review of SONGS Units 2 and 3 post commercial operating date costs have been completed.

4. Purchased Power

DRA found that Edison's expenses for economy energy purchases for the Record Period were reasonable. For firm purchased power expenses, DRA does not recommend any disallowance.

However, DRA recommends that the Commission order Edison to renegotiate or terminate the Cholla-4 contract as discussed earlier.

5. Cogeneration

As stated previously, review of Edison's purchases from cogenerators for the 1985 and 1986 Record Periods has been deferred to be held in Edison's pending ECAC proceeding A.88-02-016.

6. Fossil Fuel Generation and Heat Rate

DRA found Edison fossil plant outages for the Record Period to be reasonable.

The Commission indicated an interest in the heat rate performance of Edison's fossil fuel units and in D.86-04-059 recommended that Edison adopt a heat rate deviation method similar to that adopted for Pacific Gas and Electric Company (PG&E). In order to evaluate heat rate performance, Edison proposed an Efficiency Deviation Method. This method serves as a performance standard and provides a measurement of the improvements in heat rate efficiency.

The Efficiency Deviation Method is based on changes from historic performance utilizing individual unit/hourly operating information to establish theoretical fuel consumption. This theoretical fuel use is then compared against actual fuel consumption to determine deviation from theoretical.

DRA agreed that the Efficiency Deviation Method is a reasonable approach; however, DRA believes that heat rate improvement should be measured in BTU/kWh and not by the percentage method used by Edison.

Edison and DRA subsequently agreed to use the 1984 and 1985 recorded system heat rate data, including Redondo Units 7 and 8, as the base for the Efficiency Deviation Method. Edison provided tables which reflect both the percentage and BTU/kWh deviations from the

Edison and DRA subsequently agreed to use the 1984 and 1985 recorded system heat rate data, including Redondo Units 7 and 8, as the base for the Efficiency Deviation Method. Edison provided tables which reflect both the percentage and BTU/kWh deviations from the recorded 1984 through 1985 base heat rate standard.

7. Natural Gas Expenses

DRA agreed that Edison's natural gas expense was reasonable.

8. Fuel Oil Expense

In D.87-06-021, the Commission ordered a disallowance of 10 percent of the Chevron Option Agreement Demand charges which were \$580,000 for the Record Period. DRA agreed that Edison's August 1986 Low Sulfur Fuel Oil burn of 993,000 barrels was reasonable and that Edison's fuel oil carrying charges were reasonable.

Discussion

As this summary indicates, there is agreement that Edison's operations during the Record Period, except as discussed earlier, were reasonable. We concur with Edison's showing and the DRA's analysis.

Comments on the Proposed Decision

Edison and DRA have filed comments on the ALJ's proposed decision. Based on our review, we believe that the following modifications to the decision, other than correction of typographical errors, should be made:

1. Effective Dates for Revocation of the CPIP and Adoption of the Economic Modifier to the Nuclear Unit Incentive Procedure

The proposed decision revokes the CPIP on the effective date of the order. The proposed decision also adopts an Economic Modifier to the Nuclear Unit Incentive Procedure.

recorded 1984 through 1985 base heat rate standard.

7. Natural Gas Expenses

DRA agreed that Edison's natural gas expense was reasonable.

8. Fuel Oil Expense

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Discussion

As this summary indicates, there is agreement that Edison's operations during the Record Period, except as discussed earlier, were reasonable. We concur with Edison's showing and the DRA's analysis.

Findings of Fact

1. DRA finds Edison's expenses for coal and gas burned during the Record Period at Mohave and Four Corners to be reasonable.
2. DRA recommends that for the Record Period, Edison be granted a reward of \$7,881,737 under the CPIP .
3. DRA recommends that the CPIP be revoked until such time that conditions warrant reinstitution of this incentive program. In the alternative, DRA recommends that the CPIP apply only to Mohave.
4. Edison agrees with DRA that the CPIP be revoked for both Mohave and Four Corners.
5. The CPIP has achieved its objective of improving coal plant performances.

6. DRA and Edison have filed a Stipulation and Agreement which settles DRA-recommended disallowance for replacement energy during a SONGS-1 outage in November, 1986.

7. The Stipulation and Agreement recommends that the Commission adopt a disallowance of \$798,682 (plus interest at the ECAC Balancing Account rate from June 1, 1986 to the effective date of this order) to Edison's ECAC Balancing Account.

8. The Stipulation and Agreement is a reasonable settlement of the SONGS-1 outage issue and is fair to Edison's ratepayers.

9. There is no opposition to the Stipulation and Agreement regarding the SONGS-1 outage.

10. DRA and Edison have agreed to use the 1984 and 1985 recorded system heat rate data, including Redondo Units 7 and 8, as the base for the Efficiency Deviation Method.

11. DRA agrees that the Edison proposed Efficiency Deviation Method to evaluate the heat rate performance of Edison's fossil fuel generating units is reasonable.

12. Edison proposes to establish an additional Economic Modifier to the Nuclear Unit Incentive Procedure when a SONGS Unit's refueling outage schedule is changed to meet the system reliability needs of one or more SONGS Parties.

13. Adoption of the proposed Economic Modifier to the Nuclear Unit Incentive Procedure will not have adverse impact on Edison's ratepayers.

14. There is no opposition to Edison's proposed modification to the Nuclear Unit Incentive Procedure.

15. DRA recommends that Edison be ordered to renegotiate or terminate Cholla-4 contract with APS mainly because the cost of energy from Cholla-4 exceeds Edison's current avoided costs.

16. Edison disagrees with DRA's recommendation regarding the Cholla-4 contract.

17. The Cholla-4 contract was reasonable when executed and amended.

18. Edison has attempted to renegotiate the Cholla-4 contract.

19. Other than the issues discussed in the preceding findings of fact, DRA finds Edison's operations during the Record Period to be reasonable.

Conclusions of Law

1. The CPIP for Edison's Mohave and Four Corner plants should be revoked.

2. Edison should be awarded a reward of \$7,881,737 under the CPIP.

3. The Stipulation and Agreement filed by DRA and Edison should be adopted.

4. Edison's ECAC Balancing Account should be reduced by \$798,682 (plus interest at the ECAC Balancing Account rate from June 1, 1986 to the effective date of this order) to account for the replacement energy during SONGS-1 outage.

5. Edison should continue to try to achieve concessions from APS regarding the Cholla-4 contract and should file a report describing in detail its efforts to do this. Edison should also file a report on the cost of terminating the Cholla-4 contract with its next ECAC filing.

6. Subject to the observations made by the Commission as set forth here, Edison's operations during the period December 1, 1985 to November 30, 1986 were reasonable.

O R D E R

IT IS ORDERED that:

1. The Coal Plant Incentive Procedure for Southern California Edison Company's (Edison) Mohave Generating Station and Four Corners Generating Station shall be revoked on the effective date of this order.

2. Edison's ECAC Balancing Account shall be reduced by \$798,682 plus interest at the ECAC Balancing Account rate from June 1, 1986 to the effective date of this order.

3. Edison shall be awarded a reward of \$7,138,400 under the Coal Plant Incentive Procedure and its ECAC balancing account shall be adjusted accordingly.

4. Edison shall continue to try to achieve concessions from APS regarding the Cholla-4 contract and shall file a report in its next ECAC proceeding describing in detail its efforts to do this. Edison shall also file a report on the cost of terminating the Cholla-4 contract with its next ECAC filing.

5. This proceeding is concluded.

This order is effective today.

Dated \_\_\_\_\_, at San Francisco, California.