

JUL 6 1995

Decision 95-07-004 July 6, 1995

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company for an Order Approving the Termination Agreement for the Power Purchase Agreement for Long-Term Energy and Capacity Between Pacific Gas and Electric Company and SAI Soledad Energy, Inc.

Application 95-01-033

(Filed January 25, 1995)

ORIGINAL

OPINION

Pacific Gas and Electric Company (PG&E) seeks an order approving an agreement to terminate the Interim Standard Offer 4 (ISO4) power purchase contract, it signed with a biomass qualifying facility (QF), SAI Soledad Energy, Inc. (SAIE). The Commission's Division of Ratepayer Advocates (DRA) supports approving the agreement for it finds the agreement beneficial to ratepayers.

The power purchase agreement PG&E seeks to terminate was entered into in 1985. It is an ISO4 contract which provides for the purchase of energy and capacity from a 16-megawatt (MW) facility located at the Soledad Industrial Park in Monterey County for a term of 30 years. The power purchase agreement, as amended in 1989, provides a firm capacity price of \$186/kilowatt-year (kW) for the first ten years and \$196/kW-year for the remaining 20 years of the contract. By prior decision, the Commission authorized a paid

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deferral, amounting to approximately \$2.5 million paid prior to energy deliveries, so that the project on-line date was deferred from June 26, 1990 to June 26, 1996. This deferral and payment, as authorized by the Commission, was agreed to in the First Amendment and Amendment to Paragraph 10 of the power purchase agreement.

The termination agreement, as amended, provides for PG&B to pay SAIB approximately \$10 million in exchange for terminating the ISO4 agreement. Specifically, the termination agreement provides for the following payments: (1) an initial payment of \$2.5 million within 30 days after the project receives both of its critical permits (Section 3.1); (2) monthly application payments of \$100,000, not to exceed \$500,000, until the Commission issues a decision on this application (Section 6.1); (3) a reimbursement up to \$1 million for project costs SAIB incurs in connection with cancellation if termination is approved and provided written documentation is given to PG&B (Section 6.2); and (4) a final payment of \$6 million as compensation for termination (Section 7.1). The critical permits were received. PG&B has paid the \$2.5 million initial payment and has begun to make the monthly payments. PG&B seeks findings that the terms of the termination agreement are reasonable, its actions in entering the termination agreement were reasonable, the termination agreement adequately serves PG&B's ratepayers, and PG&B may recover all termination agreement payments made to SAIB in rates.

1. The power purchase agreement (Docket #89-11-041) See Decision (Docket #95-01-033) The two permits referred to are the Conditional Use Permit from the City of Soledad and the Authority to Construct from the Monterey Bay Unified Air Pollution Control District. SAIB is a subsidiary of SAI Energy.

Our Final Guidelines for Contract Administration of Standard Offers (Guidelines) provide the standard for review of the termination agreement (D.88-10-032, 291 CPU2d 415, at 439 - 442). Three aspects of the Guidelines must be addressed in evaluating this application: project viability, ratepayers' interests, and reasonableness of the buyout. The Guidelines provide that the QF's viability under the power purchase agreement is a prerequisite to modifications (Guidelines, IV.1). Therefore we will first determine whether the SAIE project is viable.

The SAIE project was found viable by the Commission when it authorized the on-line date deferral in November 1989 (D.89-11-041 [Conclusion of Law 1]). PG&E provides in Exhibits G and H' updated final viability information for each of the delineated aspects of QF project development contained in the Guidelines. Specifically, PG&E has testified to:

1. The completion of the Project Description and Interconnection Study Form, updated and subsequently resubmitted October 1994;
2. Proof of site control, biomass fuel supply, timely equipment procurement, engineering design development, financing letters of intent, and confidence in the developer's prior experience in the design, construction, management, and operation of major power projects;
3. The completion of the detailed interconnection study, updated in 1994;
4. Exhibit G is the testimony of PG&E employee Janos Laszlo. Exhibit H is the testimony of Robert J. Membreno, President and Chief Executive Officer of SAIE Energy, Inc. and SAIE Soledad Energy, Inc.

with cost estimates escalated to 1995 levels;

Receipt of proof that an escrow account had been established for the project fee, resulting in an interconnection priority identification;

5. The reactivation in September and

December 1994, of the two critical permits, the Conditional Use Permit by the City of Soledad and the Authority to Construct Permits by the Monterey Bay Unified Air Pollution Control District;

6. The feasibility of constructing the facility by the required on-line date;

7. The economic viability of the project, stating that even in a high fuel cost scenario, the facility produces a positive cash flow.

Our review of the PG&E and SAIB testimony confirms these representations regarding the viability of the SAIB project. We therefore conclude that the project is viable.

Our Guidelines also state that buyouts may be considered only if ratepayers' interests will be served demonstrably better by such termination (Guidelines, III.7). In its testimony, PG&E assesses ratepayer benefits from termination using a number of different assumptions. The ratepayer benefits analysis is most sensitive to the assumed capacity factor of the plant and the gas price forecasts. Gas price affects the value of replacement energy to PG&E.

An "adverse case" was prepared, in it, PG&E assumed a relatively low capacity factor for the first ten years of

operation, (2) a high gas price for purposes of determining the cost of replacement power, and (3) that the facility would cease operating after the tenth year. The estimated net present value of overpayments avoided with termination in the adverse case is \$60.4 million.

Using its base case assumptions, PG&E asserts that the termination agreement allows it to avoid paying \$81 million to SAIE over the life of the power purchase agreement.

In the termination agreement, PG&E has agreed to pay SAIE approximately \$10 million in order to avoid the overpayments ranging from \$60.4 million to \$81 million. By termination, PG&E will also be relieved from making two payments to SAIE contained

in the First Amendment to the ISO4 power purchase agreement, which amount to \$1.8 million in savings. Avoiding the \$1.8 million payment reduces the cost to ratepayers of terminating the ISO4 to \$8.2 million. Therefore, PG&E estimates ratepayer benefits from terminating the ISO4 total from \$52.2 million to \$72.8 million.

DRA filed its support for the application because termination, DRA asserts, is expected to provide substantial ratepayer benefits.

Our review of the record confirms PG&E's assessment of ratepayer benefits. Even when the costs associated with initially deferring (approximately \$2.2 million) and then terminating the contract are totaled, ratepayers are served demonstrably better from termination.

We turn now to the third aspect of the Guidelines, Reasonableness of the buyout. Guideline III.8 states that is that cost-effective energy and capacity additions (be they utility built or purchased power) could lower the operating cost of the PGE system.

The reasonableness of contract deferrals and buyouts will be determined by evaluating the need for generating capacity, ... the costs avoided by deferring or buying out unneeded capacity, and the benefits (both monetary and non-monetary) granted projects acceding to deferral or buyout.

The costs and benefits have been discussed above. We have but to address the need for the generating capacity. When we last considered whether PG&E has a need for new capacity we determined that it has no reliability-based need. (D.92-04-045, 44 CPUC2d 58 [Finding of Fact 42].) PG&E has not subsequently advised us of any new reliability-based need. Therefore, it is reasonable for PG&E to terminate the contract.

PG&E also seeks a finding that its actions in entering the termination agreement were reasonable. This record does not detail the actions taken by PG&E, so we are in no position to find unknown actions reasonable.

Findings of Fact

1. PG&E and SAIE are parties to an ISO4 power purchase agreement executed by SAIE's predecessor-in-interest in 1985, amended in 1988 and 1989, pursuant to which PG&E is to purchase the electrical output from SAIE's proposed 16 MW biomass qualifying facility. The on-line deadline for the project is June 26, 1996.

2. In November 1994, PG&E and SAIE entered into an agreement, amended in December 1994, to terminate the ISO4 power

We turn now to the third aspect of the guidelines,

5. In that decision, we did find that PG&E has an economic need. That is, that cost-effective energy and capacity additions (be they utility built or purchased power) could lower the operating cost of the PG&E system.

purchase agreement. PG&E has agreed to pay SAIE approximately \$10 million in exchange for terminating the ISO4 agreement.

3. The SAIE project was found viable by the Commission when it authorized an on-line date deferral in November 1989. The updated, final viability information PG&E testified to conforms with our Final Guidelines for Contract Administration of Standard Offers and demonstrates that the project remains viable.

4. Termination of the ISO4 contract will avoid overpayments, net of termination payments, ranging from \$52.2 million to \$72.8 million. If the \$2.2 million costs of initially deferring the project in 1989 are also considered, the overpayments avoided are nevertheless substantial.

5. In D.92-04-045, when we last considered PG&E's need for new capacity, we determined that it has no reliability-based need. PG&E has not advised us of subsequent changes in reliability-based need.

6. Notice of the application appeared on the Commission's Daily Calendar on January 31, 1995. There are no protests. The Division of Ratepayer Advocates supports the application. A public hearing is not necessary.

Conclusions of Law

1. The terms of the amended Termination Agreement are reasonable.

2. PG&E's execution of the amended Termination Agreement was prudent.

3. PG&E's ratepayers will be adequately served by the amended Termination Agreement.

4. The Termination Agreement, as amended, should be approved.

A.95-01-033 ALJ/BAR/gab *

5. PG&E may recover the reasonably incurred termination agreement payments, totaling approximately \$10 million, through PG&E's Energy Cost Adjustment Clause or any other mechanism this Commission establishes that provides for full recovery of the payments in rates.

6. Because the Termination Agreement will benefit ratepayers, this decision should be effective today.

O R D E R

IT IS ORDERED that:

1. The approval sought by Pacific Gas and Electric Company (PG&E) of the 1994 Termination Agreement with SAI Soledad Energy, Inc. (SAIE) and the termination of the associated Interim Standard Offer 4 power purchase agreement is granted.

2. PG&E may recover the termination payments, not to exceed \$10 million, pursuant to the 1994 Termination Agreement through PG&E's Energy Cost Adjustment Clause, provided it reasonably administers the agreement.

3. This proceeding is closed.

This order is effective today.

Dated July 6, 1995, at San Francisco, California.

DANIEL Wm. PESSLER
President
P. GREGORY CONLON
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
Commissioners

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

Wesley Franklin

Acting Executive Director