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Decision 95-11-058 November 21, 1995

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
 Southern California Edison Company)
 (U 338-E) for Order Approving) Application 95-08-009
 Termination Agreement for Termination) (Filed August 16, 1995)
 of ISO4 Power Purchase Agreement)
 Between Southern California Edison)
 Company and Sierra Power Corporation.)

O P I N I O NSummary

Southern California Edison Company (Edison) is an electric utility. Edison is a party to many power purchase agreements (PPAs) with various qualifying facilities (QFs) for the purchase of electricity. Edison seeks our approval for termination of a PPA whereby Edison is obligated to purchase 7.5 MW of firm capacity and energy from a wood waste-fired biomass facility at Terra Bella in the San Joaquin Valley of California under an Interim Standard Offer 4 (ISO4) contract. In the event that we decline to approve termination of the PPA, Edison requests a finding that its payments to date under a termination agreement be found reasonable. The Division of Ratepayer Advocates (DRA) filed a response supporting the application to terminate. We will approve the termination agreement.

Background

Edison filed its application on August 16, 1995 for approval of an agreement to terminate the PPA. Notice of the application appeared in the Daily Calendar on August 24, 1995. No protests were received.

The PPA was executed in December 1984 between Edison and Sierra Power Corporation (Sierra). The PPA project achieved

firm operation in March 1986, producing electrical power using wood waste from an adjacent sawmill owned by an affiliate of Sierra, purchased wood waste, and natural gas. The project operates as a cogeneration facility which supplies steam to the sawmill for wood drying. The project currently burns about 78,000 tons of wood waste per year and has been operating without technical problems.

Edison filed the termination agreement and the prepared testimony and qualifications of its manager who negotiated the termination agreement, its economic analyst who evaluated the ratepayer benefit under the termination agreement, and the report of its consulting engineer who evaluated the technical and economic viability of the plant under the PPA. Edison moved that the termination agreement and the exhibits be kept confidential on the grounds that if other QFs had knowledge of the details of the termination agreement and Edison's analysis, Edison would be at a disadvantage in negotiating future buyouts. The motion was referred to Administrative Law Judge (ALJ) Reed on the law and motion calendar, and, on September 1, 1995, ALJ Reed issued a protective order permitting the termination agreement and the exhibits to be maintained without public access for a period of one year. Accordingly, we will be circumspect in our discussion of the termination agreement and its analysis.

Guidelines for Buyouts of Power Purchase Agreements

In our Rulemaking to Establish Guidelines for the Administration of Power Purchase Contracts Between Electric Utilities and Qualifying Facilities, 29 CPUC2d 415 (1988) (Guidelines), we established guidelines for buyouts of certain PPAs. (Id. at 432-34.) Because we thought that a negotiated buyout, compared to any other type of contract modification, would put the ratepayer at the greatest risk of breathing "life into a moribund" QF, we established a "stringent" threshold test

35of viability. (Id. at 433.) However, we were not yet confronted with examples of PPAs such as this one, in which a utility seeks to buy out an established QF. (Id.) Accordingly, many of the specific viability tests that we articulated (e.g., that the QF have obtained all necessary permits and certifications) do not apply in this case.

What continues to apply, however, is the principle that ratepayers should not pay "money for something they would have received for free, if the project were in fact not viable." (Id. at 434.) Projects that have been operating successfully for several years that are fully "capable of operating as planned and of generating electricity" do not pose the same concerns. (See Order Instituting Investigation on the Commission's own motion to implement the Biennial Resource Plan Update following the California Energy Commission's Seventh Electricity Report _____ CPUC2d _____ (1994) (D.94-05-018, typescript at 5) (hereafter Year 11 Order).) This is an example of such a plant whose technical viability is well established.

Moreover, we cautiously scrutinize the reasonableness of buyouts on a case-by-case basis even when project viability is not in dispute. (See Guidelines at 434.) This is because we developed the long-run standard offer program as part of a planning approach that uses forecasts to value resource additions by projecting avoided costs. (Id. at 433.) Our basic premise was that forecasting errors would cancel out over time in a portfolio of PPAs. (Id.) We were concerned that our long-run standard offer portfolio policy could be subverted if a pattern developed of buyouts of PPAs just as they were about to become economical to ratepayers. (See id. at 434.) We have relied on PPA contract terms as the principal means "to protect ratepayers against loss of the premium above market prices that they have paid during the fixed price period if the QF does not survive long enough after the tenth year to pay back the ratepayers'

advances by generating more economically priced power." (Year 11 Order at 6.)

Technical Viability of the Project

The uncontested evidence that Edison has presented shows that the plant is technically viable.

Economic Viability

Edison's engineer also forecast Sierra's net cash flow for the remaining term of the PPA. The payment rates, estimated production levels and estimated operating costs were considered. The engineer concluded that the plant could operate profitably, given the favorable prices at which Sierra can purchase waste wood and its option to adjust operations under the PPA to concentrate operations during the summer when energy rates are higher.

Commensurate Concessions

The uncontested evidence that Edison has presented shows a substantial ratepayer benefit from terminating the PPA, compared to receiving Sierra's performance as agreed.

Edison's analyst prepared a straightforward assessment of the termination agreement's impact on ratepayers, determined by the following equation, all discounted to January 1, 1995:

- (a) Customer benefits associated with Sierra's agreement not to operate from January 1, 1995 through March 2, 1996 (the end of the high-cost period of the PPA), plus
- (b) Customer benefits associated with Sierra's agreement not to operate from March 2, 1996 through the end of the PPA term, March 2, 2016, minus

- (c) Termination payments under the termination agreement.

The last item was taken from the termination agreement, which sets out a schedule of monthly payments. The other items were calculated based on a range of assumptions regarding the production levels of the facility (based on historic data) and forecasts of the replacement cost of energy.

Edison's analyst concluded that the termination agreement would procure ratepayer savings. Such savings range from \$7.9 million to \$12.8 million, based on Edison's forecast of replacement cost prices at the time of negotiation. Using Edison's current forecasts of replacement cost prices, the benefits range from \$8.4 million to \$9.6 million.

We conclude that the estimated savings to the ratepayer are a commensurate concession for the payments under the termination agreement.

Findings of Fact

1. The PPA is technically and economically viable.
2. The terms and conditions of the termination agreement provide benefit to ratepayers commensurate with the degree of change to the existing contractual arrangement.
3. No protests have been received, and no hearing is necessary.

Conclusions of Law

1. The termination agreement should be approved.
2. Edison should be authorized to recover in rates all payments under the termination agreement through its Energy Cost Adjustment Clause, or any other mechanism authorized by the Commission, to the same extent as any other cost associated with

a QF is recoverable, subject only to Edison's prudent administration of the termination agreement.

ORDER

IT IS ORDERED that:

1. The request of Southern California Edison Company (Edison) for approval of a Contract Termination Agreement, dated December 28, 1994 (Termination Agreement), with Sierra Power Corporation is approved.

2. Edison is authorized to recover in rates all payments under the Termination Agreement through its Energy Cost Adjustment Clause, or any other mechanism authorized by the Commission, to the same extent as any other cost associated with a qualifying facility is recoverable, subject only to Edison's prudent administration of the Termination Agreement.

This order is effective today.

Dated November 21, 1995, at San Francisco, California.

DANIEL Wm. FESSLER
President
P. GREGORY CONLON
JESSIE J. KNIGHT, Jr.
HENRY M. DUQUE
JOSIAH L. NEEPER
Commissioners