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Decision 97-03-035 March 18, 1997

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U 338-E) for Order Approving the Settlement Agreement Between Southern California Edison Company and the Procter & Gamble Paper Products Company.	Application 96-08-031 (Filed August 13, 1996)

OPINION

1. Summary

Southern California Edison Company (SCE) seeks approval of a written settlement agreement (Settlement) between SCE and the Procter & Gamble Paper Products Company (P&G). The Settlement resolves certain disputes concerning SCE's purchases of power from P&G under two Interim Standard Offer No. 4 (ISO4) contracts. In this decision we approve the Settlement and grant SCE's application on an ex parte basis.

2. Background

P&G manufactures paper products and owns a plant in Oxnard that produces toilet tissue and paper towels for distribution and sale throughout the West. The plant consists of two paper making machines, numbered 1 and 2, respectively, and associated equipment. The two machines have loads of 10 and 13 megawatts (MW).

The Oxnard plant began paper production in 1975, and has operated on a 365-day schedule ever since. In 1982, P&G installed a 19.8 MW cogeneration facility at the plant. This facility supplies steam, hot air, and electric energy and capacity to the plant, and when operating at full capacity fulfills the electricity requirements of the No. 1 machine and delivers 11.6 MW of firm capacity to SCE under the terms of an ISO4 contract (Oxnard I).

In 1989, P&G installed a second cogeneration facility with a nameplate rating of 49.9 MW. That facility furnishes steam and hot air to the plant's No. 2 paper machine, but the electrical output is dedicated and sold to SCE under the terms of a second ISO4 contract (Oxnard II). The thermal output of both cogeneration plants is used in the production process for drying paper, and without that output P&G could not operate the paper plant.

Oxnard I is a 15-year ISO4 contract specifying a firm contract capacity of 11.6 MW at $122/kilowatt-year (kW-yr.). The facility achieved firm operation on April 18, 1985. The second facility is a 49.9 MW facility. Oxnard II is a 30-year ISO4 contract, with a firm contract capacity of 45 MW at $212/kW-yr. The facility achieved firm operation on January 1, 1990.

Both contracts provide for energy deliveries over the first period of the contract term to be purchased at (1) the Forecast of Annual Marginal Cost of Energy rates specified in the contract for 20% of the energy delivered, and (2) SCE's Published Avoided Cost of Energy for 80% of the energy delivered. The first period of Oxnard I concluded on April 18, 1990, and the first period of Oxnard II will expire on December 31, 1999.

Among the terms of both contracts is a provision that if P&G is unable to provide contract capacity because of "Uncontrollable Forces," the period of interruption or reduction will be treated as though it were allowable maintenance, which carries no contractual penalty. Both contracts define "Uncontrollable Forces" to include failures of facilities which have been maintained in accordance with good engineering and operating practices.

3. The Contract Disputes and the Settlement

A number of disputes concerning the implementation of the two contracts arose during the course of performance. These involved three issues in particular: the appropriate procedures for administering the scheduled maintenance provisions of the

contracts in relation to P&G's claim of protection under the "Uncontrollable Forces" provision; P&G's desire to use generation from the Oxnard I facility on-site during non-peak periods; and the requirements for notifying the other party of incorrect billing statements and making adjustments equitably. SCE and P&G resolved their disagreements concerning these issues through negotiation, and formalized their resolution by entering into the Settlement. This application seeks Commission approval of the Settlement.

SCE filed a motion for a protective order with the application seeking to protect from public inspection the Settlement and much of the supporting testimony, because release of this information could place SCE at a disadvantage in negotiating similar settlements with other qualifying facilities (QFs). By Ruling dated September 20, 1996, the Law and Motion Administrative Law Judge (ALJ) granted SCE's motion with the limited exception of releasing the qualifications of one of the witnesses. By the terms of the Ruling, the protected items will remain under seal for one year from that date.

The Commission's Office of Ratepayer Advocates (ORA) filed a document titled, "Response of the Office of Ratepayer Advocates (ORA) to the Application of Southern California Edison Company" (Response). Although characterized as a "Limited Protest," the Response supports approval of the Settlement as a reasonable resolution of the disputed contractual issues. ORA's protest states:

> "In most instances, applications for ex parte preapproval of QF settlements or buyouts do not provide the staff with the time needed to conduct an adequate analysis. In this limited instance, the ORA was able to conduct an adequate analysis of the Settlement..., because the factors involved in the agreement do not appear factually complex or obscure. Also, the Settlement does not involve a great amount of ratepayer dollars, and ORA is more willing to accept such settlements without rigorous discovery and analysis."

In recognition of the absence of controversy, no hearing is necessary.

As summarized in ORA's Response, the Settlement provides that:

> "The Oxnard I Contract will be terminated and converted into a new SO1-based contract with payment terms based on (SCE's) Standard Offer No. 1 (SO1) power purchase contract. Oxnard I will serve all of P&G's load including both paper machines at all times.
>
> "The Oxnard II contract has been restructured such that...Edison will make a lower, levelized payment to P&G effective July 1, 1996. In addition, the expected Competition Transition Charges (CTC) will be treated as if the contract restructuring had not taken place. If P&G becomes subject to CTC charges for no longer taking power from (SCE), then P&G will remain obligated to pay them. No incentive payment will be paid to (SCE) in connection with QF contract buyouts and buydowns as authorized in D.95-12-063."

Utilizing SCE's computations of payments to SCE, as offset by revenue losses, under this new arrangement, ORA reports that the positive net benefit to ratepayers for termination of the Oxnard I contract will be an estimated $288,000.

ORA also notes that the Settlement guarantees SCE (and thus its customers) the benefit of any future CTC that would have applied to P&G's current 12.9 MW of demand under Oxnard II. It also protects SCE's customers in the unlikely event that P&G shuts down the Oxnard I facility before the term of the current contract expires by requiring SCE to be refunded capacity overpayments to the same extent as currently under Oxnard I. ORA states that the Settlement eliminates the disputes over maintenance scheduling and severely curtails the circumstances under which an equipment failure should be treated as an Uncontrollable Force under Oxnard II, and the formula for P&G's entitlement to capacity payments is considerably more rigorous than previously. The price

paid for energy is also changed, with a resultant net ratepayer benefit of $415,318 (Net Present Value, 1/1/96).

ORA summarizes the potential ratepayer benefits as including the resolution of disputes and prevention of the likelihood of future disputes; savings of $703,318 (NPV 1/1/96) for the two contracts in power purchase costs; avoidance of the risks and expenses associated with litigating the contract disputes; protection of ratepayers from Uncontrollable Force claims based upon equipment failures; and implementation of favorable energy and capacity payment terms. ORA states that it has analyzed the agreement and run sensitivity analyses using changed assumptions, and agrees that SCE has demonstrated that the Settlement is a cost-effective agreement for ratepayers.

4. Discussion

In applications of this type the Commission requires a persuasive showing that the new power purchase agreement will benefit ratepayers more than would the existing one, and a showing that the generating facility is a viable one that would not be likely to shut down prior to expiration of the contract. See San Diego Gas & Electric Company, Decision (D.) 94-12-038 (December 21, 1994); Southern California Edison Company, D.95-10-041 (October 18, 1995), Southern California Edison Company, D.95-11-058, 165 PUR4th 441 (1995). See, generally, Power Purchase Contracts, D.88-10-032, 29 CPUC2d 415 (1988); Opinion on Guidelines for Year 11-Related Restructuring, D.94-05-018, 54 CPUC2d 383 (1994).

First, the Settlement meets the Commission's requirement of a showing that it will benefit SCE's ratepayers, particularly in light of ORA's comments and analysis. Second, SCE's testimony that the Oxnard I and Oxnard II facilities are viable and would not likely shut down prior to the end of the period of performance for the applicable contract is compelling and uncontradicted, and leaves little doubt that the facilities will be an integral feature of the manufacturing process for the foreseeable future.

Consequently, the Settlement meets both tests for allowing modification or amendment and restatement of the power purchase contracts which are its subject matter.

The Settlement also satisfies the test for approval of an all-party settlement, see D.92-12-019, 46 CPUC2d 538: All active parties have joined in its sponsorship; the sponsoring parties (with the inclusion of ORA's endorsement) are fairly reflective of affected interests; no term of the Settlement contravenes statutory provisions or prior Commission decisions; and the Settlement conveys sufficient information to permit us to discharge our future regulatory obligations with respect to the parties and their interests.

SCE's application includes a request that the Commission's order authorize SCE to exclude 12.9 MW of demand and related sales associated with the termination of Oxnard I in calculating SCE's authorized base rate levels, in the event that the Commission eliminates the Electric Revenue Adjustment Mechanism (ERAM) balancing account for SCE. By supplemental letter furnished at the request of the ALJ, SCE explained that this provision is necessary because recent legislation, Assembly Bill 1890, imposed a rate freeze period which is expected to extend beyond the October 18, 2000, termination date applicable to both the existing Oxnard I contract and the modified agreement that will replace that contract if the settlement is approved. SCE, in preparing the sales forecast that was used for purposes of rate setting during the freeze period, included the 12.9 MW of P&G demand that will be eliminated by Commission approval of the settlement. That forecast has now been accepted as the foundation of SCE's rates during the rate freeze period. Unless SCE were to have an opportunity to provide a modified sales forecast for recalculating base rates during the rate freeze period, elimination of the 12.9 MW of demand would not have any further impact on SCE's rates. By its request, SCE seeks confirmation in the Commission's decision that approval

of the settlement will entitle SCE to exclude the 12.9 MW of current P&G demand from any future sales forecast made for rate setting purposes, but this will not have an impact upon any presently applicable sales forecast.

The application also asks the Commission to authorize SCE to collect from P&G any CTC that would have applied to the 12.9 MW of power that will now be served by the Oxnard I facility under the new arrangement, had the parties not entered into the Settlement. As explained by SCE in its letter, the reason for this is to protect SCE from loss under the principle that any settlement between the parties should leave them in the same relative financial position they occupied before the settlement. "Under pre-settlement conditions [SCE] would have retained as a customer the 12.9 MW of [P&G's] total electric demand that will now instead be served by [P&G's] Oxnard I cogeneration facility as a result of the settlement. Accordingly, in the absence of the settlement, [P&G,] as a customer, would have remained subject to the same CTC obligations as any other customer having a similar demand served by [S&E]. In anticipation that industry restructuring would produce a rule like that embodied in new Public Utilities Code § 372(a)(1), which exempts CTC liability for certain self-generation project," the parties agreed to P&G's guarantee of payments equivalent to those which it would have had to make if the service were not terminated under the Settlement. We find this provision to be reasonable, and we approve it.

We will approve the Settlement in accordance with the terms and conditions of the Order.

Findings of Fact

1. On April 17, 1985, SCE and P&G entered into a 15-year ISO4 contract (QFID No. 2013).

2. On April 16, 1985, SCE and P&G entered into a 30-year ISO4 contract (QFID No. 2072).

3. A number of disputes between SCE and P&G have arisen during the course of performance of the two power purchase contracts. In order to resolve these disputes, SCE and P&G entered into the Settlement which is the subject of the application herein.

4. Implementation of the Settlement will resolve the current disputes and prevent the likelihood of future disputes; save ratepayers $703,318 (NPV 1/1/96) in power purchase costs; avoid the risks and expenses associated with litigating the contract disputes; protect ratepayers from Uncontrollable Force claims under the existing contracts, based upon equipment failures; and implement favorable energy and capacity terms.

5. The underlying cogeneration facilities are viable facilities that would not be likely to shut down prior to the end of the period of performance for the applicable power purchase contract.

6. The Settlement is reasonable.

7. All active parties have joined in the sponsorship of the Settlement.

8. The sponsoring parties (including ORA) are fairly reflective of affected interests.

9. No term of the Settlement contravenes statutory provisions or prior Commission decisions.

10. The Settlement conveys sufficient information to permit us to discharge our future regulatory obligations with respect to the parties and their interests.

11. SCE's entering into the Settlement and its attachments is prudent.

12. In similar proceedings, the Commission has conditioned permanent recovery of expenses incurred under the approved agreements upon reasonable contract administration by the utility.

<u>Conclusions of Law</u>

1. The Settlement should be approved.

2. SCE's request for authorization to recover the cost of the Settlement through its Energy Cost Adjustment Clause or successor power purchase cost recovery mechanism should be granted, subject to reasonable contract administration.

3. Other relief should be granted, as specified in the Order.

O R D E R

IT IS ORDERED that:

1. The application of Southern California Edison Company (SCE) for approval of the Settlement Agreement between SCE and the Procter and Gamble Paper Products Company (P&G) executed February 23, 1996, is approved.

2. SCE is authorized to exclude the 12.9 megawatts of demand and related sales associated with the termination of QFID No. 2013 in calculating SCE's authorized base rate levels in the event that this Commission eliminates the Electric Revenue Adjustment Mechanism balancing account for SCE.

3. SCE is authorized to collect from P&G any Competition Transition Charges that would have applied to the 12.9 megawatts of demand that will be served by the Oxnard I cogeneration facility pursuant to the Settlement had the parties not entered into the Settlement.

4. This proceeding is closed.

This order is effective today.

Dated March 18, 1997, at San Francisco, California.

P. GREGORY CONLON
President
JESSIE J. KNIGHT, JR.
HENRY M. DUQUE
JOSIAH L. NEEPER
RICHARD A. BILAS
Commissioners