

Mailed 9/18/98

Decision 98-09-072 September 17, 1998

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U 338-E) for Order Approving Agreements Restructuring the Negotiated Parallel Generation Agreement Between Southern California Edison Company and Sunlaw Cogeneration Partners I.

Application 98-04-050
(Filed April 24, 1998)

O P I N I O N

Summary

This ex parte decision approves the restructuring of the negotiated Parallel Generation Agreement (Contract) between Southern California Edison Company (Edison) and Sunlaw Cogeneration Partners I (Sunlaw). This will result in savings to Edison's ratepayers estimated at from \$1.9 million to \$31.7 million, with an expected level of savings of \$21.0 million.

Background

This application by Edison seeks expedited ex parte approval of the Restructuring Agreements, which restructure the Contract between Edison and Sunlaw. Edison states that the Restructuring Agreements were negotiated because under the existing Contract, Edison is obligated to pay rates for capacity and energy from Sunlaw that are significantly higher than current and expected future costs throughout the remainder of the Contract's term, which ends on June 8, 2006.

Restructuring Agreements

Edison, Sunlaw, and a third party, Citizens Power LLC (Citizens), entered into the Restructuring Agreements, under which Edison's obligation to purchase

energy and capacity at above-market rates ends, and Edison will have the right to cease purchasing power from Sunlaw's generation facilities entirely. In order to achieve this concession, Edison agreed to make either amendment or termination payments, to Citizens.

There are two separate sets of agreements involved:

- The first agreement is the Settlement Agreement between Sunlaw and Citizens, under which Sunlaw will assign its prospective rights and obligations under the existing Contract to Citizens, in exchange for a lump sum payment from Citizens. Commission approval is not needed for the agreement since Edison is not a party thereto, but this agreement is contingent on Commission approval of this application, since it is an integral part of the Restructuring Agreements.
- The second agreement is a master Execution Agreement between Edison and Citizens, to which other agreements are annexed. Upon fulfillment of certain conditions, including Commission approval of this application, Edison and Citizens will enter into two agreements, described below, which will complete the Contract restructuring. Edison states that public disclosure of the terms of the agreements could jeopardize its ability to restructure other similar contracts to the benefit of its ratepayers, and requests that the unredacted version be kept confidential. The Commission agrees with this request and has granted confidentiality. Thus, our discussion will concentrate on what the agreements achieve, rather than their specific terms. The master Execution Agreement consists of the following:
 - An Amended and Restated Parallel Generation Agreement between Edison and Citizens (Amended and Restated Contract). This agreement deals with the terms under which Citizens, pursuant to its agreement with Sunlaw, assumes the rights to sell capacity and energy to Edison under new pricing schedules for capacity and energy. Edison is obligated to make amendment payments to Citizens while this agreement remains in effect, but may exercise the option to terminate the agreement at any time. If it does terminate, the Termination Agreement, described below, will take effect.

- **Termination Agreement.** Under this agreement between Citizens and Edison, Edison would no longer have to purchase capacity and energy from Citizens. It would have to make termination payments to Citizens in the same amount and under the same schedule as the amendment payments under the Amended and Restated Contract above.

The actual capacity and energy purchases from Citizens are expected to be at market prices. Under the Restructuring Agreements Citizens has the right to not sell to Edison if the prices contained in the schedules turn out to be lower than actual market prices at the time. In that case, Citizens would sell in the market and Edison would replace the capacity and energy at market prices from other suppliers. If, on the other hand, market prices are below the schedules' prices, Edison would exercise its right to terminate the Amended and Restated Contract and also purchase capacity and energy at market prices. Thus, Edison will be able to purchase energy at market prices under any condition.

The benefit of the renegotiation to Edison's ratepayers is the savings, which are the net savings due to buying market priced energy at lower than Contract costs, less the cost of amendment or termination payments. Edison estimates these net savings to be a most likely amount of \$21.0 million, with a worst case savings of \$1.9 million and a best case savings of \$31.7 million. The worst case assumes production at the lowest historic year level and high replacement costs, while the best case assumes production at the highest historic year level and low replacement costs. These savings estimates are based on a November 7, 1998 effective date for the transaction, and January 1, 1998 net present value using a 10% discount rate.

Edison hired a consultant, RanBo Energy Associates, Inc. (RanBo), to evaluate the likelihood of Sunlaw being able to continue to perform under the existing contract to the end of the contract period. Such an evaluation was stressed by the Commission in Decision (D.) 88-10-032, which states " we expect

project viability to be considered before negotiations are pursued." (29 CPUC2d 426). Later in D.94-05-018 we stated "... we agree with DRA that the utility should not ignore material facts it becomes aware of that affect the Qualifying Facility's (QF) ability to perform under the original or proposed contract." (51 CPUC2d 386). This viability check is to protect ratepayers from paying for the termination of a contract where little or nothing might be owed due to the QF's inability to perform. Sunlaw operates two generation facilities which generate a total of 56 megawatts (MW) of firm capacity, normally operating 24 hours a day, with the waste heat sold to a nearby ammonia absorption refrigeration system.

RanBo visited the project, and evaluated the following:

1. Technical and operational issues. RanBo concluded that the generating facilities are well-designed, constructed and maintained, and are operated within design parameters. The owners and on-site management monitor the facilities' status, as well as financial and operational performance, and have excellent maintenance and preventative maintenance programs. Both the capacity factor of 96.1% for the past five years, and the availability factor of 95.3% since 1986 point to reliable operation.

2. Environmental compliance. RanBo believes that based on current compliance history and the environmental controls in place, the facilities should continue to comply with environmental requirements for the duration of the contract. RanBo concludes that Sunlaw takes environmental compliance seriously, and has done an effective job in compliance.

3. Ability to meet current and foreseeable future regulatory requirements. RanBo foresees no difficulty in this area and concludes that Sunlaw should meet these requirements.

4. Financial profitability. RanBo concludes that Sunlaw can most likely operate profitably for the remainder of the Contract term. The recorded capacity and availability factors in recent years verify the profitability of operation, and the effective maintenance indicates that it will most likely continue. In addition, the nearby market for waste heat used for refrigeration appears likely to continue.

Based on RanBo's evaluation, Edison believes that Sunlaw can continue to perform to the end of the Contract period, and thus the pursuit of renegotiation of the Contract is worthwhile. The Office of the Ratepayer Advocates (ORA) does not dispute that the facility will be viable for the remaining Contract term.

Protests

Protests were filed by ORA and Southern California Gas Company (SoCalGas).

ORA

The issues raised in ORA's limited protest are:

- The Commission must retain the right to examine the reasonableness of costs incurred under Section 17 of the Termination Agreement and the Settlement Agreement. Edison agrees that costs incurred under the Termination Agreement are subject to Edison's reasonable administration, and unless it elects to use this agreement no costs under it will be incurred. The Settlement Agreement of August 18, 1997 between Edison and Sunlaw is not a part of this application; rather, Edison has included that in its 1998 Energy Cost Adjustment Clause proceeding, Application (A.) 98-05-053. ORA is now satisfied that those costs will be subject to reasonableness review since the administration of the agreement is subject to such a review, and that Edison has the burden of proof in demonstrating reasonableness. Thus, ORA is now satisfied that these issues are resolved.

- The increase in Edison's headroom for recovery of Competitive Transition Costs. This issue has been resolved to ORA's satisfaction, since Edison's errata to the application has eliminated any increase in headroom associated with the Restructuring Agreements, by modifying the schedule of restructuring payments made to Citizens.

ORA's motion to withdraw its protest due to resolution of these issues, is contingent on two conditions being satisfied:

- Edison must withdraw its June 15, 1998 reply to ORA's limited protest; and
- Edison must file an errata to its application to modify the schedule of restructuring payments.

Edison satisfied the first condition by filing a motion to withdraw its reply to ORA's limited protest, contingent on the Commission granting ORA's motion to withdraw.

The second condition is satisfied since Edison filed the first amendment to the application dated July 14, 1998. This amendment, submitted under seal for the confidential information portion, contains a renegotiated payment schedule to Citizens which satisfies ORA that headroom will not increase.

SoCalGas

SoCalGas protested the application because of concerns that the renegotiation may result in less demand for gas from Sunlaw, which is supplied by SoCalGas, resulting in harm to its ratepayers. As a result of ongoing discussions with the parties to the application, SoCalGas is now satisfied that it and its ratepayers will not be harmed by Commission approval of the application. SoCalGas' withdrawal of protest was filed June 25, 1998.

Edison filed a second amendment on September 1, 1998, which, among other things, adds a new condition precedent, in which the parties' obligation to restructure Sunlaw's contract will not be effective unless either Proposition 9, the proposed Initiative No. SA 97 RF 0064, is defeated on November 3, 1998, or Proposition 9 is approved and Edison waives this condition precedent. This amendment also updates the estimated ratepayer savings to reflect the necessary later anticipated action by the Commission in this matter.

ORA continues to support the application after this amendment, but believes that if Proposition 9 passes and Edison decides not to execute the restructuring of the contract, it should support the reasonableness of that decision.

Therefore, since all parties who had protested have withdrawn their protests, and there are no requests for hearing in this matter, hearings are not necessary.

Discussion

The Restructuring Agreements will benefit Edison's ratepayers by allowing Edison to purchase energy and capacity at market rates, which are substantially lower than the prices Edison is now obligated to pay Sunlaw under the Contract. These savings outweigh the cost of renegotiation of the Contract, which are in the form of amendment or termination payments to Citizens. Edison properly sought this renegotiation to benefit its ratepayers. This removes some of the burden of paying rates that are far above market until mid-2006. To continue under the present contract would be harmful to Edison's ratepayers as they would be paying prices for capacity and energy that are significantly above market prices both presently and most likely for the remaining term of the Contract.

We are satisfied that Sunlaw's operation is reliable and profitable, especially considering the ready market for waste heat used for refrigeration. We agree with Edison's consultant that it most likely would continue to operate at high capacity and availability levels for the remainder of the contract. Sunlaw has implemented effective maintenance programs and upgrades to assure continued reliable operation.

ORA was concerned with the increased headroom that would have resulted from the initial application. That concern has been alleviated by Edison's first amendment which prevents an increase in headroom from the renegotiation, and ORA has withdrawn its protest. Under this amendment, Edison and Citizens have entered into an amendment to the Execution Agreement which modifies the payment schedule in a manner that avoids the increase in headroom.

All parties involved in this application now agree that it should be approved by the Commission. We find that it is in the best interests of Edison's ratepayers and will approve it in the order that follows. We note that the administration of the Termination Agreement remains subject to reasonableness review, as acknowledged by both Edison and ORA, while in Edison's 1998 ECAC, we will review the Settlement Agreement. A decision by Edison to not execute the restructuring of the contract will also be subject to reasonableness review.

In Resolution ALJ 176-2992 dated May 7, 1998, the Commission preliminarily categorized this proceeding as ratesetting, and preliminarily determined that hearings were necessary. In light of the complete disposition of this application by this decision, the need for hearing having been eliminated by the withdrawal of the protests, there is no need to issue a separate order changing the preliminary hearing determination, as contemplated in Rule 6.5(b).

Findings of Fact

1. Edison is an electric utility subject to the jurisdiction of the Commission.
2. Edison, Sunlaw, and Citizens entered into Restructuring Agreements that restructure the Contract between Edison and Sunlaw.
3. Notice of this application appeared in the Commission's Daily Calendar on May 5, 1998.
4. This matter was categorized as ratesetting by Resolution ALJ 176-2992.
5. Edison's motion for protective order on redacted proprietary information in the Restructuring Agreements was granted by ALJ Ruling dated June 3, 1998.
6. Edison requests a protective order on redacted information in the amendments to the application filed on July 15, 1998 and September 1, 1998.
7. ORA and SoCal Gas filed protests and requested hearings in this matter.
8. ORA and SoCal Gas subsequently requested withdrawal of their protests to the application.
9. The Restructuring Agreements will result in savings to Edison's ratepayers.

Conclusions of Law

1. A hearing is not necessary.
2. The Restructuring Agreements are reasonable.
3. The Restructuring Agreements should be approved, subject to the conditions stated in the order that follows.
4. Edison's amendments to the application should be approved, and the unredacted information should be granted protection.
5. The motion of ORA to withdraw its limited protest should be granted.
6. The withdrawal of protest of SoCalGas should be granted.
7. The motion of Edison to withdraw its reply to ORA's protest should be granted.
8. This order should be effective on the date signed.

9. This proceeding should be closed.

O R D E R

IT IS ORDERED that:

1. The Restructuring Agreements are approved, subject to the conditions stated in this Opinion.
2. Southern California Edison Company's (Edison) amendment to the application dated July 14, 1998, and modifying the schedule of restructuring is approved, and shall be followed.
3. Edison's second amendment to the application, dated September 1, 1998, adding a condition precedent, is approved.
4. The unredacted version of the amendments to the application which have been submitted under seal by Edison shall remain under seal for a period of two years from the effective date of this order, and during that period shall not be made accessible or disclosed to anyone other than Commission staff except on further order of the Commission.
5. The Motion to Withdraw Limited Protest of the Office of Ratepayer Advocates is granted.
6. The Withdrawal of Protest of Southern California Gas Company (U 904 G) is granted.

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7. The Motion to Withdraw Reply of Edison (U 338-B) to Limited Protest of the ORA is granted.

8. This proceeding is closed.

This order is effective today.

Dated September 17, 1998, at San Francisco, California.

RICHARD A. BILAS

President

P. GREGORY CONLON

JESSIE J. KNIGHT, JR.

HENRY M. DUQUE

JOSIAH L. NEEPER

Commissioners