Mailed 5/4/2000

Decision 00-05-018 May 4, 2000

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U 388-E) For Order Approving Contract Termination Agreement Between Southern California Edison Company and Gas Recovery Systems, Inc.	Application 99-11-030 (Filed November 24, 1999)

O P I N I O N

Summary

By this decision, we approve Southern California Edison Company's (SCE) proposed buyout and termination of a 1984 power purchase agreement with Gas Recovery Systems, Inc. (GRS). Expected customer benefits from the buyout range from $1.2 million to $9.8 million in net present value (NPV). Pursuant to an agreement with the Office of Ratepayer Advocates (ORA), SCE is entitled to a shareholder incentive of $290,000.

Background

GRS is a qualifying facility (QF).[1] It operates a landfill gas biomass facility located near Irvine, California. The facility is designed to operate 24 hours per day.

On November 1, 1984, SCE entered into a 30-year Interim Standard Offer 4 (ISO4) power purchase agreement with GRS's predecessor in interest. GRS

[1] A QF is a small power producer or cogenerator that meets federal guidelines and thereby qualifies to supply generating capacity and electric energy to electric utilities. Utilities are required to purchase this power at prices approved by state regulatory agencies.

commenced construction of the facility in 1986 and achieved firm operation on April 25, 1989.

Under the terms of the original contract, SCE was to purchase up to 12 megawatts (MW) of firm capacity and associated energy from the GRS biomass facility. Following GRS's final selection of equipment, SCE and GRS entered into an amendment to the contract. The amendment increased the capacity commitment to 20 MW, reduced the capacity payment rate, and modified the energy payment terms. A second amendment in 1988 modified the interconnection agreement. After the initial firm capacity demonstration test in 1989, the capacity commitment was reduced to 19.714 MW by mutual agreement of SCE and GRS.

In its current form, the contract provides for GRS to sell energy to SCE under a formula whereby 60% is priced at the Forecast of Marginal Cost of Energy and 40% is priced at SCE's published avoided cost prices until April 24, 1999. After April 24, 1999, energy is priced at SCE's published avoided cost, including an Energy Loss Adjustment Factor (ELAF), for the duration of the contract. The capacity payments under the contract are $198/kilowatt-year, and are subject to the firm capacity performance requirements and obligations defined in the contract. The contract ends on April 24, 2019.

GRS failed to meet its capacity performance requirements during 1989, was placed on probation on January 3, 1990, and the project capacity was derated to 17.1 MW on December 12, 1990. It has the annual capacity test at the 17.1 MW level since that point in time.

On November 24, 1999, SCE filed this application seeking ex parte approval by this Commission to terminate its power purchase agreement with GRS. SCE also presented its proposal to retain 10% of the ratepayer benefits

resulting from the buyout, pursuant to the Commission's authorization in Decision (D.) 95-12-063, as modified by D.96-01-009.

ORA filed comments in support of the termination agreement, but raised concerns over the calculation of expected ratepayer benefits. Specifically, ORA indicated that it was concerned that SCE's analyses failed to account for the possibility that GRS would be unable to use natural gas to supplement its fuel source and that the replacement cost forecasts were not sufficiently conservative.

In Resolution ALJ 176-3028, the Commission preliminarily categorized this proceeding as ratesetting and determined that hearings will be necessary. A prehearing conference (PHC) was held on February 1, 2000. At the PHC, SCE indicated that, should it reach agreement with ORA, it would file a revised request addressing ORA's concerns. On February 11, 2000, SCE filed an errata to its application reflecting a revised deadline for approval of the termination agreement. On February 18, 2000, SCE filed a "Revised Request for Shareholder Incentive Award" indicating agreement with ORA's proposal to modify the shareholder incentive award. On February 22, 2000, SCE filed a revised application in compliance with rulings on its requested protective order.

On February 24, 2000, the Assigned Commissioner issued a scoping memo determining that evidentiary hearings would not be needed in this matter. By D.00-03-048, the Commission ratified the Assigned Commissioner's determination.

Motion for Protective Order

SCE requested a protective order covering certain information submitted in support of its application. Specifically, SCE requested that the Commission keep under seal: (i) the restructuring agreements' specific terms; (ii) SCE's model

for and analysis of customer benefits from the contract termination, including the discount rate and date of net present value used in deriving the benefits; (iii) SCE's analysis of GRS' economic viability; (iv) SCE's experts' analysis of GRS' technical viability; (v) discussion of SCE's analysis of an appeal of Federal Energy Regulatory Commission (FERC) orders; and (vi) SCE's estimates of the range of ratepayer benefits and the corresponding shareholder incentive.

In a ruling dated January 14, 2000, the assigned administrative law judge (ALJ), after consulting with the Assigned Commissioner, denied the blanket protection requested but granted part of SCE's motion. The ALJ provided SCE with an additional opportunity to request specific protection consistent with General Order 66-C. A follow-up ruling was issued on January 27, 2000, again following consultation with the Assigned Commissioner, which provided protection for several other items but continued to deny protection for certain items. SCE did not comply with the ALJ's Ruling to revise and serve its application and testimony by February 1, 2000. The basis for the rulings of the ALJ and Assigned Commissioner was their need for sufficient evidence to support the issuance a final decision in this case that would contain a supportable statement of reasons, findings and conclusions.

SCE's noncompliance was discussed at the February 1 PHC. SCE chose not to defend or explain its position that it would not comply with the order of the presiding officer. Following the PHC, SCE requested the opportunity to present additional arguments off the record in an ex parte meeting with the Assigned Commissioner. On February 10, the Assigned Commissioner met with SCE, ORA, and Energy Division. On February 17, 2000, the ALJ and the Assigned Commissioner issued a joint ruling addressing several procedural matters, but significantly making no change to the protective order rulings. On February 22, 2000, SCE complied with the rulings. We affirm all three rulings.

Before turning to the merits of this case, we remind SCE that our Rules clearly state that the presiding officer has authority to rule upon "all objections or motions which do not involve final determination of proceedings." (Rule 63.) Through these Rules, the Commission has delegated the authority to make procedural rulings to the presiding officer in each proceeding. The Commission has articulated its reluctance to review evidentiary and procedural rulings before the proceeding has been submitted. While noting that interlocutory appeals from ALJ Rulings on procedural matters are not absolutely barred, the Commission has consistently expressed reluctance to consider them.

> "There is no appeal from a procedural or evidentiary ruling of a presiding officer prior to consideration by the Commission of the entire merits of the matter. The primary reasons for this rule are to prevent piecemeal disposition of litigation and to prevent litigants from frustrating the Commission in the performance of its regulatory functions by inundating the Commission with interlocutory appeals on procedural and evidentiary matters. (55 CPUC2d 672, 676) (1994) (quoting D.87070, granted in *Re Alternative Regulatory Frameworks for Local Exchange Carriers.*)

The Commission recently offered an additional rationale:

> "...We have a further reason to assure the presiding officer adequate power to control a hearing. We now have to decide, with few exceptions, adjudicatory cases within 12 months of filing and other matters within 18 months. An impotent presiding officer faced with an intransigent litigant could not manage the case expeditiously, resulting, perhaps, in actual harm to other participants." (D.98-03-073, mimeo., at 126.)

In Re Southern California Edison

In D.98-03-073, we affirmed a ruling by the assigned ALJ that imposed sanctions for SCE's noncompliance with discovery rulings. In that case, we required SCE to reimburse costs associated with its interlocutory appeal of the

presiding officer's ruling. Although SCE did not formally appeal the Rulings of the ALJ in this case, which were issued after consultation with the Assigned Commissioner, its noncompliance with the ALJ's Rulings and its request to present additional arguments ex parte served to delay the proceeding in much the same manner that an interlocutory appeal would cause delay. In this case, SCE sought to contest a procedural ruling through ex parte communications when it had foregone previous opportunities to make its case on the record in writing and at a prehearing conference. SCE never formalized its objections to the rulings in writing. Instead it chose to remain out of compliance for 21 days before eventually complying with the rulings.

Where issues are in dispute regarding the scope of a protective order or any other procedural matter, parties should make their objections and arguments on the record. On reflection, we do not approve of efforts by any party to present arguments on disputed procedural matters outside of the public record, through ex parte meetings, although we acknowledge that parties are not precluded from such tactics by our rules.

When the presiding officer has ruled on any procedural matters before him/her, parties are expected to proceed consistent with that ruling. Pub. Util. Code § 7 provides that "(w)henever a power is granted to, or a duty is imposed upon, a public officer, the power may be exercised or the duty may be performed by a deputy of the officer or by a person authorized, pursuant to law, by the officer, unless this code expressly provides otherwise." Section 311 (c) provides that "(t)he evidence in any hearing shall be taken by the commissioner or the administrative law judge designated for that purpose. The commissioner or the administrative law judge may receive and exclude evidence offered in the hearing in accordance with the rules of practice and procedure of the commission." Through Rule 63 of its Rules of Practice and Procedure, the

Commission has delegated the authority to rule on procedural matters to the presiding officer. Such rulings constitute "an order of the Commission" within the meaning of Section 2107, which provides in pertinent part:

> "Any public utility which ... fails to comply with any ... part of provision of any order, decision, decree, rule, direction, demand, or requirement of the commission, ... is subject to a penalty of not less than five hundred dollars ($500), nor more than twenty thousand dollars ($20,000) for each offense."

After due consideration of this matter, we will not impose a penalty under § 2107, because SCE has complied, albeit belatedly, with the ALJ's rulings.

However, this is not the first time that SCE has sought an overbroad protective order on a QF buyout. In A.97-12-043, we addressed a similar request for protective order and ordered public disclosure consistent with that required in this proceeding. Decisionmaking in the absence of public disclosure is very difficult, and we place SCE on notice that in the future we may consider appropriate sanctions, including dismissal of applications that on their face provide insufficient public information on which to make a decision.

Project Viability and Ratepayer Benefits

There is no dispute over the facts presented in this case on the viability issue. SCE internally evaluated the project's economic and technical viability and retained R.W. Beck, Inc. (Beck), an independent consultant with expertise in forecasting landfill gas production and energy systems, to verify GRS's viability. Beck visited the site to assess equipment status and operations and maintenance. Beck analyzed GRS's historic landfill gas production and estimated future production. Based on the site visit, Beck concluded that the facility is in good condition and that personnel have been well trained to perform their duties.

GRS's energy production has been relatively stable since startup. In 1996, GRS began to use supplemental gas in its energy production, consistent with two FERC orders: *Laidlaw Gas Recovery Systems, Inc. and Coyote Canyon Landfill Gas Power Plant*, 74 F.E.R.C. (CCH) ¶ 61,176 (1996) and *Laidlaw Gas Recovery Systems, Inc. and Coyote Canyon Landfill Gas Power Plant*, 84 F.E.R.C. (CCH) ¶ 61,070 (1998) (decision denying rehearing.) These orders permitted GRS to use natural gas for up to 25% of its total, annual energy input as a supplement to landfill gas. SCE filed an appeal of the FERC orders. On November 2, 1999 the United States Court of Appeals, District of Columbia Circuit, issued a decision agreeing with SCE's position and vacating the FERC orders. The decision has since become final (195 F.3d 17).

SCE's analysis of the project's economic viability used data from Beck's report to assess viability. This data included information on expected plant performance, operation and maintenance, and timing of energy deliveries under scenarios using supplemental natural gas and without supplemental natural gas.[2] SCE concludes that even without the use of supplemental gas, GRS will continue to meet its contractual capacity requirements for the life of the contract. The results of SCE's analyses establish that GRS is expected to enjoy strong net revenue and profit streams for the remainder of the contract term, even under the worst case scenario. ORA agrees with SCE's conclusion that there is no foreseeable impediment to the successful operation of the facility throughout the remainder of the ISO4 agreement's term.

[2] Beck's report focuses on GRS's performance under the supplemental natural gas use scenario. Beck informally provided SCE with data under the no supplemental natural gas scenario.

Ratepayer cost savings result from the replacement of GRS's high energy and capacity prices under the existing contract with lower-priced energy and capacity based on SCE's projected replacement costs, net of termination payments. SCE performed sensitivity analyses that examined how the forecast market prices during the remaining years of the contract would affect these cost savings. SCE's analyses produce savings that range from $1.2 million to $9.8 million in NPV,[3] taking into account varying assumptions concerning energy prices, performance, and the impact of the FERC appeal on ratepayer savings.[4] SCE prepared best, worst, and expected cases assuming GRS could use supplemental natural gas and assuming no natural gas could be used. In addition, SCE prepared its analysis using two different ELAFs. SCE forecasts that expected ratepayer savings will be between $3.1 million and $3.4 million NPV in the no supplemental gas case and requested $340,000 as a shareholder incentive.

ORA and SCE do not agree on a reasonable estimate of the benefits of the buyout. However, ORA conducted its own analysis of SCE's application and concluded that the ratepayers savings estimates in the no supplemental gas case are robust. ORA indicates that NPV ratepayer benefits will accrue even if replacement capacity costs increase by 12%. As a result of discussions between ORA and SCE, SCE has modified its shareholder incentive request to $290,000

---

[3] January 1, 2000 NPV @ 10% discount rate.

[4] SCE assigned probabilities to the outcome of the FERC appeal and assessed the possibility of related repayment of contract payments by GRS to SCE. SCE then reflected this assessment in its calculation of net savings under the various scenarios to arrive at estimates of ratepayer benefits.

but continues to support its estimate of expected ratepayer savings. ORA agrees that ratepayer benefits will accrue under a range of assumptions. ORA supports $290,000 as a shareholder incentive based on its estimate of ratepayer savings.

Discussion

The Commission scrutinizes the reasonableness of buyouts on a case-by-case basis. We look closely, therefore, at whether the buyout produces a reasonable level of cost savings to ratepayers, taking into account the buyout payment terms and the expected reduction in energy payments. We also look closely at whether the QF project is likely to continue in operation, since it would make no sense to make buyout payments to an energy supplier that was not likely to stay in business under the existing contract.

SCE has demonstrated to our satisfaction that GRS meets the Commission's viability criteria and that the buyout will produce savings for its ratepayers under a range of economic and operational assumptions. SCE analyzed the NPV savings for a supplemental gas case and a no supplemental gas case and examined three sets of assumptions for production levels and replacement costs and two ELAFs resulting in six scenarios.

SCE's estimate of expected ratepayer savings was based on its no supplemental gas case. Like ORA, we agree that, given the facts specific to this case, this is the proper scenario on which to base the expected case. The no supplemental gas case analysis results in a range of ratepayer NPV savings from $1.2 million to $4.6 million. Although this range gives us some concern because it is so close to zero, we are convinced that the assumptions used by SCE are sufficiently conservative so as to limit ratepayer's risk of the savings approaching zero. ORA's comments add further support that ratepayers will benefit from this termination agreement based on its assessment that, even with a 12% increase in

replacement capacity costs, ratepayer benefits still accrue. ORA and SCE have not agreed on an expected forecast of ratepayer benefits; however, they have agreed that shareholder incentive of $290,000 is warranted.

SCE's application, as modified, has met our criteria for approval of QF contract buyouts and is hereby approved. Today's approval for rate recovery of termination payments is subject only to Edison's prudent administration of the termination agreement and the rate freeze provisions of Pub. Util. Code §§ 330 et al.

311(g)(2) Relief Granted

This is an uncontested matter in which the decision grants the relief requested. Accordingly, pursuant to Section 311(g)(2), the otherwise applicable 30-day period for public review and comment is waived.

Findings of Fact

1. Site visits have confirmed that the GRS biomass facility is a well-designed, built, operated and maintained plant. Its production has been relatively stable since 1989.

2. The range of savings in the no supplemental gas case analysis gives us concern because it is so close to zero; however, the assumptions used by SCE are sufficiently conservative so as to limit ratepayer's risk of the savings approaching zero.

3. The benefits of the buyout range from $1.2 million to $9.8 million in NPV. These cost savings result from the replacement of GRS's high energy and capacity prices under the existing contract with lower-priced energy and capacity based on SCE's projected replacement costs, net of termination payments.

4. SCE has demonstrated to our satisfaction that GRS meets the Commission's viability criteria and that the buyout will produce savings for its ratepayers under a range of economic and operational assumptions.

5. SCE was out of compliance with rulings by the presiding officer for a total of 21 days.

6. Where issues are in dispute regarding the scope of a protective order or any other procedural matter, parties should make their objections and arguments on the record.

Conclusions of Law

1. SCE's November 24, 1999 application, as revised on February 22, 2000, and as modified by SCE's errata dated February 11, 2000 and its February 18, 2000 "Revised Request for Shareholder Incentive," is reasonable and should be approved.

2. SCE's request for recovery of expenses incurred under the termination agreement should be conditioned on SCE's reasonable performance of its obligations and exercise of its rights under the agreement. Rate recovery should also be subject to the rate freeze provisions of Pub. Util. Code § 330 et al.

3. Because the Commission has delegated the authority to rule on procedural matters to the presiding officer under Rule 63 of the Rules of Practice and Procedure, such rulings constitute an order of the Commission.

4. Pub. Util. Code § 2107 provides for penalties of not less than $500, nor more than $20,000 for each offense when a utility fails to comply with Commission rulings.

5. Because all issues have been addressed by this decision, this proceeding should be closed.

6. In order to proceed expeditiously with the proposed buyout, this decision should be effective today.

ORDER

IT IS ORDERED that:

1. The November 24, 1999 application of Southern California Edison Company (SCE), as revised February 22, 2000, for approval of the contract termination and settlement agreement between SCE and Gas Recovery Systems, Inc. (GRS), as modified by errata dated February 11, 2000 and the February 18, 2000 "Revised Request for Shareholder Incentive," is approved.

2. The termination agreement as set forth in Exhibit SCE-2 of the application is reasonable, and SCE's actions in entering into the agreement were prudent. The termination agreement achieves estimated savings between $1.2 million and $9.8 million net present value, of which $290,000 shall be the shareholder incentive payment authorized in Decision (D.) 95-12-063, as modified by D.96-01-009.

3. SCE is authorized to recover in rates all payments under the termination agreement, to the same extent as any other cost associated with a qualifying facility is recoverable, subject only to SCE's prudent administration of the termination agreement and the rate freeze provisions of Pub. Util. Code § 330 et al.

4. This proceeding is closed.

This order is effective today.

Dated May 4, 2000, at San Francisco, California.

LORETTA M. LYNCH
President
HENRY M. DUQUE
JOSIAH L. NEEPER
RICHARD A. BILAS
CARL W. WOOD
Commissioners