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Decision 99-11-025 November 4, 1999

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking on the Commission's Proposed Policies Governing Restructuring California's Electric Services Industry and Reforming Regulation.	Rulemaking 94-04-031 (Filed April 20, 1994)
Order Instituting Rulemaking on the Commission's Proposed Policies Governing Restructuring California's Electric Services Industry and Reforming Regulation.	Investigation 94-04-032 (Filed April 20, 1994)

OPINION REGARDING MOTION REQUESTING APPROVAL FOR POWER EXCHANGE BASED PRICING UNDER PUB. UTIL. CODE § 390(c)

Summary

On July 1, 1999, several Qualifying Facilities (QFs)[1] filed a motion (Motion) requesting the Commission's approval for short-run avoided cost (SRAC) energy payments to be based on the Power Exchange (PX) market-clearing price for those QFs that voluntarily elect such an option. The moving parties request this action pursuant to Pub. Util. Code § 390 (c) and believe that *ex parte* action is appropriate, since our approval is necessary only to effectuate an existing statutory right.

The Office of Ratepayer Advocates (ORA), Southern California Edison Company (Edison), Pacific Gas and Electric Company (PG&E), San Diego Gas &

[1] The moving parties to this Motion are Independent Energy Producers Association, Wheelabrator Shasta Energy Company, Inc., Wheelabrator Hudson Energy Company, Inc., Burney Forest Products Joint Venture, and GWF.

Electric Company (SDG&E)[2], the California Cogeneration Council (CCC), the Association of California Water Agencies (ACWA), and Watson Cogeneration Company (Watson) filed responses to the Motion. The moving parties filed a reply to the responses. In addition, Fairhaven Power Company filed reply comments.[3]

We grant this motion on an interim basis, subject to true-up, as discussed herein.

Background

In general, SRAC energy prices paid to nonutility power generators by public utilities are based upon a benchmark energy price adjusted for changes over time in a gas index, as described in Decision (D.) 96-12-028 and provided for in Pub. Util. Code § 390(b).[4] However, § 390(c) allows qualifying facilities to exercise a one-time option to elect to thereafter receive energy payments based on the Power Exchange (PX) market-clearing price. The statute does not otherwise define the market-clearing price and states that the QFs must provide appropriate notice to the utilities.

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[2] SDG&E submitted its comments 5 calendar days after the filing deadline, on July 21. SDG&E moves that its comments be accepted, because SDG&E did not receive the Motion until July 6, and thus is filing within 15 days of service receipt; SDG&E did not view other parties comments prior to filing; and the Commission's acceptance of SDG&E's response will not prejudice other parties. We grant this motion and accept SDG&E's comments, but note that in general, responses are due within 15 days of the date of service, rather than a particular party's receipt of a document.

[3] Fairhaven moves to respond out-of-time, due to confusion regarding whether to file comments responding to the motion or the Assigned Commissioner's Ruling issued on June 27. Because Fairhaven has a direct interest in this proceeding, we grant the motion to file out-of-time and accept Fairhaven's reply comments.

[4] All statutory references are to the Pub. Util. Code, unless otherwise noted.

The moving parties now ask that we issue an order approving this election, so that QFs that do so can use the PX's day-ahead zonal market-clearing price as the basis for SRAC energy prices. The investor-owned utilities would recover in rates all PX-based energy payments, which would be presumed reasonable. The moving parties explain that the day-ahead market-clearing price is publicly available and is currently tracked and used for multiple purposes. They propose that 15-days notice to the utility be deemed appropriate notice. Under the proposal, the method approved by the Commission would not be a precedent and would not affect Commission action on the more comprehensive § 390 proceeding. (See the Assigned Commissioner Ruling, issued in this docket on July 27, 1999.)

The moving parties recognize that § 390(d) requires that QFs operating under certain power purchase contract provisions and that are also receiving PX-based energy prices cannot also receive the value of capacity in the PX market-clearing price, if any such value exists. The moving parties explain that use of the PX-based energy pricing will preclude the payment of any capacity value.

Positions of the Parties

The CCC, ACWA, and Watson support the Motion in its entirety. Watson argues that use of a PX-based SRAC for energy payments would draw more generation into the market in California, and thereby hold down summer peak prices. Watson maintains that lowering the PX price by this means benefits all parties, i.e., ratepayers, utilities, and QFs. Watson claims a delay in addressing the Motion is unwarranted, since not many QFs are likely to opt to switch, and the method proposed in the Motion will likely be very close to the one ultimately adopted by the Commission in the broader § 390 proceeding.

ACWA notes that its QF members are unusual in that they both consume and generate large amounts of electricity. ACWA points out what it terms the illogical decoupling of the prices at which its members buy from the market (at the PX clearing price) and sell to the utilities (at the historical SRAC price). Furthermore, ACWA agrees with Watson that market-based price signals would draw more QFs into generating during times of peak demand, thereby holding down peak summer prices.

ORA opposes the Motion and recommends that the matters raised by the Motion be considered in a separate rulemaking and investigation addressing § 390. ORA maintains that the issues pertaining to the voluntary one-time switch could be handled on an expedited basis within the broader proceeding. ORA contends that granting the Motion would exacerbate problems with high payments to QFs. ORA believes that IEP's claim that the PX day-ahead market price contains no capacity component is without any factual record. ORA is concerned that using a PX-based price, with no adjustment for embedded capacity value, would pay the QFs twice for capacity, exactly what § 390(d) aims to avoid. The moving parties maintain that this is not the case, while noting that the ancillary services markets establish the market value for capacity and reliability-related products.

ORA also believes that there are several statutory interpretation issues that must be considered before the Motion can be granted. For example, ORA argues that the "one-time" election requires an analysis of whether this election continues into perpetuity, whether it can be applied retroactively, or whether the Commission may specify a timeframe in which the QFs may select this option. ORA recommends that the Commission must determine what constitutes appropriate notice. Finally, ORA notes that some QF contracts contain the condition that energy payments are at a certain negotiated percentage of SRAC

and states that the Motion implied that these provisions for less than full SRAC payment would be eliminated.

PG&E supports the moving parties' goal, but maintains that a true-up is necessary and that certain aspects of the QFs' proposal must be clarified. PG&E explains that, although this election is voluntary on the part of the QF, § 390 also refers to a mandatory transition to a PX-based energy price. If the Commission declares that the PX is functioning properly for purposes of determining the SRAC energy payments, and certain other requirements have been met, SRAC will be based on the same PX market-clearing price. PG&E contends that the Commission must determine a methodology for determining the PX-based energy price for all QFs in the upcoming rulemaking on § 390 issues. However, PG&E agrees that because QFs have the right to elect to receive a PX-based price prior to such a transition, we must determine an interim price now. To ensure that payments made using the interim price neither under-compensate nor over-compensate recipients when compared to the methodology we ultimately adopt, PG&E recommends that the interim price should be subject to a true-up. PG&E does not oppose using the day-ahead market-clearing price on an interim basis. PG&E notes that instituting an interim mechanism with a true-up would provide parties an incentive to move expeditiously to resolve issues in the more comprehensive § 390 proceeding.

PG&E also recommends a number of other modifications to the Motion. PG&E requests clarification of what is meant by "appropriate notice" (§ 390(c)). PG&E suggests that such notification must be made sufficiently in advance to enable a utility to make any administrative changes necessary to change the energy payments from the SRAC methodology to the PX-based price. The Motion proposes a 15-day notification period, but does not state whether these

are calendar or business days. PG&E proposes that if calendar days are used, then 30 calendar days would be adequate.

PG&E maintains that such an election must be irrevocable, and not provide QFs with an option to withdraw notification of payment switch, as suggested in IEP's "Proposed Order" (Attachment A, section B). PG&E also proposes to modify the IEP-proposed language regarding recovery in rates of payments to QFs (Attachment A, section D). The main effect of PG&E's suggested changes is to include costs and expenses associated with the SRAC payment switchover – in addition to the SRAC payments themselves – among those items deemed reasonable *per se* for rate recovery. PG&E also asks that the proposed interim pricing mechanism be subject to periodic review and adjustment. Finally, PG&E suggests the form of the memorandum account that should be created to implement the true-up which it proposes.

SCE agrees that QFs have the statutory right to opt for a PX-based SRAC energy price, but notes that almost all QF contracts require SRAC payments to be based on a Commission-approved price. Therefore, SCE holds that the Motion should be granted, but only with certain safeguards. In its discussion of these safeguards, SCE makes five main points. First, SCE contends that the PX price contains some capacity value, which must be removed. Second, to be consistent with the Motion's emphasis on actual market payments – by proposing use of the zonal day-ahead market price – SCE recommends that the methodology should also reflect real line losses, which have been developed by the Independent System Operator in its Generator Meter Multiplier (GMM). Third, to ensure that these and other concerns are addressed, SCE also maintains that the Commission should order a true-up to the level ultimately approved by the Commission. Fourth, SCE recommends that the initial notification period for the switchover should be 90 days after a Commission decision, with a 15-day notification period

after that. Finally, SCE notes that the combination of a proposed retroactive switchover, subsequent option to rescind, and lack of clarity as to whether switching back and forth will be allowed, could provide QFs with an incentive for gaming, which is unfair to ratepayers.

SDG&E recommends adoption of the Motion, with several provisos. First, SDG&E believes it should be exempted from the scope of the Commission decision on this matter, particularly since none of the moving parties has contacted SDG&E which it states would have been appropriate for an *ex parte* motion. SDG&E also recommends that Commission action on this matter should be subject to revision, should unforeseen changes occur, and that Commission action on this matter should not be precedential for the more comprehensive § 390 proceeding. In addition, SDG&E contends that a 30-day notice requirement is more appropriate than a 15-day notice and that QFs should not be allowed the opportunity to revise their election status once it is made. Finally, SDG&E believes that implementation costs associated with this election should be deemed reasonable for utility rate recovery in addition to the revised energy payments.

Discussion

There is no question that QFs have a statutory right to exercise a one-time option to elect to receive energy payments based on the PX market-clearing price (§ 390(c)(3)). However, we must determine whether to grant this motion in its entirety, or not. In addition, we will clarify what constitutes appropriate notice and whether a true-up is appropriate.

The moving parties acknowledge that initially a longer time frame (such as 30 days) may be necessary to establish billing and payment systems, but maintain that subsequently, a 15-day notice period should suffice. Moving parties do not indicate whether the notice period should encompass calendar or business days.

It is reasonable to require sufficient notice such that the utilities can modify their billing and payment systems. Fifteen calendar days should be sufficient as long as the election itself does not take place until the first day of the QF billing cycle after such notification. We may adjust this notice period later, as we make further determinations in the broader § 390 proceeding.

We find no unique circumstances for SDG&E that would justify the requested exemption. The statute does not allow for an exemption for SDG&E. The one-time option to receive energy payments based on the PX market-clearing price applies to QFs in the service territories of PG&E, SCE, and SDG&E.

The moving parties maintain that the PX day-ahead zonal market-clearing price is the preferred basis for the new SRAC, as it holds the most significant volumes, because PX tariffs and protocols provide for transparent pricing in this market, and because a single market price is simpler administratively. Furthermore, the PX day-ahead market is already in use for several other purposes, such as in calculating headroom associated with the rate freeze. We agree that it is reasonable to base the price on the PX day-ahead zonal market clearing price, but we recognize that there are other market-clearing prices that may be applicable. Payments made using the interim adopted day-ahead zonal market-clearing price should not under-compensate nor over-compensate the QFs, compared to the payments made pursuant to the methodology we may ultimately adopt in the more comprehensive § 390 proceeding. Therefore, we authorize the utilities to establish tracking accounts to track the interim PX-based price made to those QFs that exercise this one-time option. The tracking accounts shall be effective as of the date of this decision and should be established by compliance advice letters. These accounts shall track the day-ahead zonal price paid to the QF, the kilowatt hours delivered, and any separate capacity payments. For purposes of later true-up, we will rely on the data published by

the PX and available on its website (www.calpx.com). Any amounts to be refunded to or received from the QF will earn the short-term commercial interest rate.

The moving parties agree that the Commission should remain open to future requests for prospective modifications to SRAC pricing as conditions indicate. The moving parties object to the recommendation for a true-up mechanism on two grounds. First, the moving parties are concerned that the Commission might never issue a definitive ruling, raising the prospect of multiple and continuing true-ups. Second, the QFs contend that the prospect of a large true-up undermines the commercial certainty that has been a hallmark of QF contracts. Because we are ruling on this motion prior to a full consideration of the many interrelated issues addressed in § 390, it is reasonable to grant the motion on an interim basis, and subject to true-up. Granting the motion on an interim basis, subject to true-up, allows the QFs to exercise their statutory rights, but also allows this Commission to review the appropriate market-clearing price in a more comprehensive manner. We do not intend to consider multiple true-ups. We intend to initiate a proceeding in the near future to consider the issues related to a permanent switch from SRAC to PX pricing, pursuant to § 390. At this point, we cannot be certain when that proceeding will conclude or if the § 390(c) criteria will be met, so as to trigger the permanent switch. At the same time, we do not believe that it is appropriate to leave the issues associated with a true-up unresolved for an indefinite period. Therefore, if we have not adopted a permanent methodology changing SRAC energy payments to energy payments based on the PX market-clearing price by December 31, 2000, we will adopt a permanent methodology for the one-time election.

There are certain questions regarding factual matters concerning capacity value and line losses. We need more time and information to ensure that these

costs are not included in the components of the PX market-clearing price. These factual matters can be determined in the broader proceeding. Since the payments made on an interim basis will be deemed reasonable, we must ensure that ratepayers do not bear costs which the QFs are not entitled to. For example, we must ensure that the PX market-clearing price does not include a capacity component. At this point, we will not make additional adjustments true-up for line loss factors. Again, this is an issue that should be addressed in the broader proceeding.

At this time, we will not provide for the utilities to recover the implementation costs associated with the interim provisions of this order. Administrative costs associated with QF contracts are subject to reasonableness reviews in the Annual Transition Cost Proceedings (ATCP). Whether or not the utilities will incur costs related to the QFs' one-time switch that aren't already covered under their rates is a factual matter that can be explored during the more comprehensive consideration of § 390.

The moving parties clarify that a switch could not occur prior to the date the Commission rules on the Motion and that there is no intention to allow QFs to switch back and forth at will. However, Fairhaven disagrees and contends that it gave notice to PG&E on June 28 for a one-time election effective July 1. Fairhaven believes that this notice must stand and that its one-time option should be effective on the date requested. We disagree. The Commission must determine what constitutes appropriate notice and must specify the particular market-clearing price to apply. While we agree that the voluntary election is unilateral on the QFs' part, we cannot agree that two-days notice is appropriate. Therefore, such an election cannot take place prior to the effective date of this Order, although notice can certainly be provided prior to that date. Consistent with the plain language of the statute, this switch is a one-time option, and

therefore, irrevocable. However, if a QF provided notice prior to the effective date of this order and wishes to withdraw its election, it may do so within 10 days of the effective date of this order. Other than this limited exception, the election is irrevocable. As we have previously stated, the Commission will make further determinations regarding the appropriate market-clearing price and the determination of whether the PX is properly functioning, consistent with the statute.

Comments on Draft Decision

The draft decision of the ALJ in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g) and Rule 77.1 of the Rules of Practice and Procedure. PG&E, Edison, ORA, IEP, and CCC filed comments on the draft decision.[5] Reply comments were filed on October 4, 1999. We have clarified the tracking accounts and the true-up mechanism, as well as clarifying that the election should not begin until the first day of the billing cycle that occurs at least 15 days after the QF provides notice to the utility. In addition, we more fully explain our approach related to the broader rulemaking to consider issues raised by § 390.

Findings of Fact

1. SRAC energy prices paid to nonutility power generators by public utilities are based upon a benchmark energy price adjusted for changes over time in a gas index, as provided for in § 390(b).

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[5] We note that Walnut Valley Water District filed comments on September 23, but these comments were a response in support of IEP's motion. While the comments conclude by recommending that the Commission support the proposed decision, responses to IEP's motion were due on July 16. We therefore reject Walnut Valley Water District's comments as untimely.

2. Section 390(c) allows QFs to exercise a one-time option to elect thereafter to receive energy payments based on the PX market-clearing price.

3. It is reasonable to require sufficient notice such that the utilities can modify their billing and payment systems. Fifteen calendar days is sufficient notice for this purpose as long as the election itself does not take place until the first day of the QF billing cycle after such notification.

4. QFs in the service territories of PG&E, SCE, and SDG&E have a statutory right to make this election.

5. Payments made using the interim market-clearing price should not under-compensate or over-compensate the QFs compared to the payments made pursuant to the methodology we may adopt in the more comprehensive § 390 proceeding.

6. It is reasonable to base the energy price on the PX day-ahead zonal market-clearing price, subject to later true-up.

7. If we have not adopted a permanent methodology charging SRAC energy payments to energy payments based on the market-clearing price by December 31, 2000, we will adopt a permanent methodology for the one-time election.

8. PG&E, SCE, and SDG&E should establish tracking accounts, which should be effective as of the date of this decision, to track the interim PX-based price the kilowatt hours delivered, and any separate capacity payments paid to those QFs that exercise this option. If a particular market-clearing price is adopted in the § 390 rulemaking, the tracking accounts should be compared to the applicable published data on the PX website (www.calpx.com). Any amounts to be refunded to or received from the QF should earn interest at the short-term commercial paper rate.

9. We need more time and information to study the components of the market-clearing price and the impact of capacity value and line losses on such a price. We will not make additional adjustments for line losses at this time and line losses will not be part of the true-up mechanism.

10. Whether or not the utilities will incur costs related to the QFs' one-time switch that are not already covered in their rates is a factual matter that can be determined in the more comprehensive § 390 proceeding.

Conclusions of Law

1. Pursuant to § 390(c), QFs have a statutory right to exercise a one-time option to elect to receive energy payments based on the PX market-clearing price.

2. The Commission must determine what constitutes appropriate notice and must specify the particular market-clearing price to apply in such an election.

3. The statute does not provide an exemption for SDG&E.

4. Because we are ruling on this motion prior to a full consideration of the interrelated issues addressed in § 390, it is reasonable to grant the motion, as described herein, on an interim basis, and subject to true-up.

5. Granting the motion on an interim basis allows the QFs to exercise their statutory rights but also allows the Commission to review various factual and policy matters in a more comprehensive way.

6. The energy prices paid to QFs that elect this option should be deemed reasonable.

7. The one-time election cannot take place prior to the effective date of this order, although notice can be provided prior to that date.

8. This election is irrevocable, with the limited exception that parties providing notice to the utilities before the effective date of this order may withdraw this election within 10 days of the effective date of this order.

9. Nothing in this ruling prejudges or compromises in any way this Commission's discretion, or the parties' rights, to propose some alternative PX-based SRAC energy pricing basis of general applicability to QFs.

10. This decision should be effective today.

ORDER

IT IS ORDERED that:

1. The Motion of the Independent Energy Producers Association, Wheelabrator Shasta Energy Company, Inc., Wheelabrator Hudson Energy Company, Inc., Burney Forest Products Joint Venture, and GWF Power Systems, for an Order Approving PX Based Pricing Pursuant the One-Time Election of Qualifying Facilities Under Public Utilities Code Section 390(c) is granted, as modified herein.

2. Any Qualifying Facility (QF) may upon at least 15 calendar days advance notification to its purchasing utility have its payments for short-run avoided cost (SRAC) energy based upon the Power Exchange (PX) clearing, price effective at the start of the QF's next billing cycle.

3. If 15 or more calendar days prior to the date of this Order, a QF has notified its purchasing utility of its election to convert its payments for SRAC energy based upon the PX clearing price, such QF may:

   a. confirm its election within ten (10) days of the effective date of this Order, in which case the PX clearing price basis of its energy pricing will commence as of the date of this order, or such other later date as the QF may specify, or,

   b. choose to proceed, or not, at the QF's sole discretion; however, such notification must be provided within ten (10) days of the effective date of this Order.

4. For purposes of this Order and the utilities' assured cost recovery of payments made based on the PX clearing price for SRAC energy, the "PX

clearing price" means the hourly energy price by zone applicable to the location of the QF as published by the PX for the its day-ahead energy market.

5. Payments made by utilities pursuant to this Order are reasonable and are fully recoverable in rates, through the QF entries in the utilities' Transition Cost Balancing Accounts, notwithstanding the relationship between the payments authorized pursuant to this Order and payments which would have been under the administrative formula currently in place.

6. Within 15 days of the effective date of this decision, Pacific Gas and Electric Company, Southern California Edison Company, and San Diego Gas & Electric Company shall file compliance advice letters that reflect all necessary Preliminary Statement and tariff changes required by this decision.

This order is effective today.

Dated November 4, 1999, at San Francisco, California.

RICHARD A. BILAS
President
HENRY M. DUQUE
JOSIAH L. NEEPER
Commissioners

I dissent.

/s/ JOEL Z. HYATT
Commissioner

I dissent.

/s/ CARL W. WOOD
Commissioner