

Decision 99-12-008 December 2, 1999

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Joint Application of Pacific Gas and Electric Company and Mt. Poso Cogeneration Company, L.P. for Order Approving Termination Agreement of ISO4 Power Purchase Agreement between Pacific Gas and Electric Company and Mt. Poso Cogeneration Company, L.P.

Application 98-10-030  
(Filed October 20, 1998)

**FINAL OPINION APPROVING MOTION TO WITHDRAW**

**Summary**

By this decision, we approve a motion by Pacific Gas and Electric Company (PG&E) and Mt. Poso Cogeneration Company, L.P. (Mt. Poso) to withdraw their joint application for buyout and termination of a 1984 power purchase agreement between them.<sup>1</sup>

**Background**

Mt. Poso is a qualifying facility (QF) that operates a 49.5 megawatt (MW), coal-fired cogeneration facility located about 35 miles north of Bakersfield in California's San Joaquin Valley.<sup>2</sup> Mt. Poso supplies process steam to the West Mt. Poso Oil Field for thermally enhanced oil recovery. PG&E and Mt. Poso's predecessor, Pyropower Corporation, in November 1984 executed an Interim

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<sup>1</sup> PG&E and Mt. Poso are herein referred to as the Joint Applicants.

<sup>2</sup> 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.

Standard Offer 4 (ISO4) power purchase agreement. ISO4 was the standard at that time for long-term contracts between electric utilities and QFs. Construction began in 1987 and Mt. Poso achieved firm operation on May 15, 1989.

Under the terms of the ISO4, PG&E purchases 49.5 MWs of firm capacity and associated energy from the Mt. Poso cogeneration facility until the end of the agreement on May 14, 2009. Mt. Poso is compensated for firm capacity at \$167/kilowatt (kW)-year and for as-delivered capacity at \$188/kW-year to the end of the agreement. During the fixed-price period described in the agreement, which ends on April 1, 1999, Mt. Poso is compensated for energy under Energy Payment Option 1 (100% of the forecasted prices). After April 1, 1999, energy prices will equal PG&E's short-run avoided costs.

In early 1997, PG&E and Mt. Poso entered into negotiations for restructuring the ISO4 agreement. PG&E and Mt. Poso agreed on the principal terms of a buyout in February 1998. In order to preserve the benefits of the buyout while pursuing management and regulatory approvals, PG&E and Mt. Poso executed a bridging agreement. Under the bridging agreement, Mt. Poso could curtail deliveries to PG&E and sell power to third parties. Payments for power sold to PG&E during the bridging period were renegotiated. The payments made pursuant to the bridging agreement would be applied to eliminate and reduce the first and second annual payments anticipated under the buyout agreement.

On October 20, 1998, PG&E and Mt. Poso filed their joint application for approval of the termination agreement. PG&E also presented its proposal to

retain 10% of the ratepayer benefits resulting from the buyout, as allowed by the Commission.<sup>3</sup>

The Office of Ratepayer Advocates (ORA) filed a protest on November 23, 1998. In its protest, ORA argued that the application should be denied because PG&E's proposal would allocate to shareholders too large of a portion of the savings in the form of increased headroom.<sup>4</sup> Therefore, ORA opposed PG&E's request for a 10% shareholder incentive award in this proceeding, and recommended that the Commission require PG&E and Mt. Poso to restructure the termination payments so that PG&E obtains only 10% of the net ratepayer benefits during the rate freeze period.

In Resolution ALJ 176-3003, dated November 5, 1998, the Commission preliminarily categorized this application as ratesetting, and preliminarily determined that hearings were necessary.

A prehearing conference (PHC) was held on December 8, 1998. At the PHC, the parties agreed to develop a joint stipulation of facts and reconvene via telephone conference call to further discuss the need for evidentiary hearings. Subsequent to the PHC, all parties agreed that hearings were unnecessary, given the stipulation of facts developed regarding ORA's protested issue.

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<sup>3</sup> See D.99-02-085, mimeo., p. 42, Ordering Paragraph 5; D.95-12-063, 64 CPUC2d 1, 193, Conclusion of Law 47 (1995).

<sup>4</sup> Headroom refers to the difference between the amount of revenue generated by an electric utility during the rate freeze period relative to its costs to provide electric service during that period. Frozen rates and declining costs together create revenues beyond those required to provide electric service. An electric utility can apply these revenues to offset transition costs. By using the savings from the Mt. Poso restructuring to increase its headroom during the rate freeze period, PG&E can increase recovery of transition costs not associated with energy payments to QFs.

By ruling dated January 22, 1999, the assigned Commissioner determined that hearings were not needed, and in Decision (D.) 99-02-079, the Commission ratified that determination.

Opening briefs were filed on March 5, 1999 by Joint Applicants, ORA and Southern California Edison Company (SCE). On March 15, 1999, Joint Applicants and ORA filed reply briefs.

On April 26, 1999, the assigned Administrative Law Judge (ALJ) issued a Draft Decision denying the application. The Draft Decision observed that the proposed buyout would result in accelerated recovery of non-QF transition costs (through the allocation of 46% of the cost savings to the rate freeze period) and a deferral of QF transition costs. Specifically, the Draft Decision stated:

"In this particular case, we believe that PG&E has sacrificed an unreasonable level of ratepayer savings associated with this QF contract restructuring for the purpose of recovering non-QF transition costs during the rate freeze period." (Draft Decision, mimeo., p. 9.)

The Draft Decision concluded that the result would be a level of cost savings to ratepayers that was not reasonable.

On May 17, 1999, the assigned ALJ granted the parties a sixty-day extension of time for the filing of comments on the Draft Decision. On July 17, 1999, the assigned ALJ granted an additional three-week extension of time for filing comments on the Draft Decision.

During this time, PG&E undertook negotiations to restructure the proposed termination payments with Mt. Poso. PG&E and Mt. Poso could not reach agreement concerning modifications to the proposed restructuring. The assigned ALJ granted additional extensions of time to file comments until September 3, 1999.

On September 2, 1999, ORA and the Joint Applicants reached agreement on settlement terms and filed a Petition To Set Aside Submission For Consideration Of Proposed Settlement and All-Party Motion For Adoption of Settlement (Petition). The Petition also requested that the Commission grant a waiver of Rule 51.1 (notice and convening of a settlement conference), Rule 51.2 (limitation on when a settlement may be proposed) and Rule 51.4 (submission of comments and replies).<sup>5</sup>

On September 9, 1999, the assigned ALJ issued a ruling soliciting comments on the joint request to waive Rules 51.1, 51.2 and 51.4

No objections were filed. SCE responded that it does not object to the settlement or to the waivers sought in the joint request. O'Brien California Cogeneration Limited gave notice of its withdrawal from the proceeding.

On September 27, 1999, Mt. Poso informed PG&E that it decided not to terminate its ISO4 power purchase agreement with PG&E and exercised its right to terminate the power purchase termination agreement.

On October 5, 1999, Joint Applicants filed a Motion to Withdraw Application (Motion). ORA and SCE, the two other active parties, do not oppose this motion, and Joint Applicants request that the Commission act on this motion without waiting for the 15-day response period to expire. (Motion, p. 1, footnote 1.)

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<sup>5</sup> All references to Rules in this decision refer to the Commission's Rules of Practice and Procedure.

## Discussion

In reviewing the proposed power purchase termination agreement, we affirm that Mt. Poso has the right to unilaterally terminate that agreement, pursuant to the following provision:

"...if CPUC does not issue an ORDER acceptable to both Parties in their respective sole and absolute discretion so as to permit this Agreement to close as defined in paragraph 1.1.3 as amended, by March 31, 1999, either Party may at any time after March 31, 1999 terminate this Agreement by written notice to the other Party." (Application Revised Public Version dated November 18, 1998, tab 5, page 4, paragraph 6.)

In its September 27, 1999 letter, Mt. Poso cites several reasons for deciding to terminate the agreement, including "substantial delay in obtaining regulatory approval, the impact of deregulation and changes in the tax treatment of the termination." (Motion, p. 1.) While the reasons for Mt. Poso's election to terminate the agreement are not relevant to our determination that such election is within Mt. Poso's legal rights, we do take issue with Mt. Poso's characterization of how this Commission responded to the joint application. There was no "substantial delay" in our process, in fact, the contested application was considered quite expeditiously by the Commission, i.e., a proposed decision was issued approximately seven months from the date of filing. As discussed above, delays beyond April, 1999 occurred at the request of Joint Applicants to pursue settlement of the contested issues and related concerns raised in the ALJ's proposed decision.

In approving the request for withdrawal of the joint application, we must decide how to address the bridging agreement discussed above. If the termination agreement had been approved, the payments PG&E has been making to Mt. Poso pursuant to the bridging agreement would have fulfilled

PG&E's obligation to make its first and second annual payment pursuant to the termination agreement. In light of the present circumstances, PG&E should seek review of the reasonableness of its payments to Mt. Poso pursuant to the bridging agreement by a new application or in PG&E's next Annual Transition Cost Proceeding application.

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

#### **Finding of Fact**

By letter dated September 27, 1999, Mt. Poso elected to terminate the power purchase termination agreement submitted in the joint application.

#### **Conclusions of Law**

1. Under the terms of the power purchase termination agreement, either PG&E or Mt. Poso has the right to terminate the agreement any time after March 31, 1999, if the Commission does not issue a decision acceptable to either party by March 31, 1999.
2. Joint applicants motion to withdraw the joint application is reasonable and should be adopted.
3. This proceeding should be closed.

### **FINAL ORDER**

**IT IS ORDERED** that:

1. The October 5, 1999 Motion of Pacific Gas and Electric Company (PG&E) and Mt. Poso Cogeneration Company (Mt. Poso) to Withdraw Application is approved.

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2. PG&E shall seek review of the reasonableness of its payments to Mt. Poso pursuant to the bridging agreement by a new application or in PG&E's next Annual Transition Cost Proceeding application.

3. Application 98-10-030 is closed.

This order is effective today.

Dated December 2, 1999, at San Francisco, California.

RICHARD A. BILAS  
President  
HENRY M. DUQUE  
JOSIAH L. NEEPER  
JOEL Z. HYATT  
CARL W. WOOD  
Commissioners