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October 14, 2011

Advice 3917-E-A

(Pacific Gas and Electric Company ID U39 E)

Public Utilities Commission of the State of California

Subject: Supplemental Filing for the Amendment to Existing Qualifying Facility Power Purchase Agreement for Procurement of Eligible Renewable Energy Resources Between Pacific Oroville Power, Inc. and Pacific Gas and Electric Company

Purpose:

Pacific Gas and Electric Company (“PG&E”) submits to the California Public Utilities Commission (“Commission”) a supplemental filing to PG&E’s Advice Letter 3917-E, dated October 3, 2011 (“Advice Letter”).¹ The Advice Letter submitted an amendment and a letter agreement (collectively the “Amendment”) to a Qualifying Facility Standard Offer Power Purchase Agreement that PG&E executed with Pacific Oroville Power, Inc. (“POPI”). The Advice Letter is currently pending approval by the Commission.

The purpose of this filing is to provide the Commission with an update to Confidential Appendix B to the Advice Letter and to provide slightly revised Independent Evaluator (“IE”) reports.

PG&E has made revisions to the discussion of compliance with the 33 percent Renewables Portfolio Standard (“RPS”) program included in Confidential Appendix B to the Advice Letter. These revisions reflect an updated methodology used to assess PG&E’s future compliance with the 33 percent program, current knowledge regarding project status under the ownership portion of PG&E’s solar photovoltaic program, and minor clarifying changes. PG&E has included a redline comparison of the original Confidential Appendix B and the revised Confidential Appendix B in the attached Confidential Appendix A. The revised Confidential Appendix B is also attached.

¹ Supplements to Advice Letters are authorized by General Order 96-B, section 7.5.1.

PG&E is also including revised IE reports. The changes made to the confidential and public IE reports are limited to small changes to the IE's ranking of the Amendment's contract price and market valuation. The revised confidential IE report is attached as Confidential Appendix C and the revised public IE report is attached as Public Appendix E. PG&E has also revised Confidential Appendix B to reflect that the IE changed his ranking of the Amendment's contract price from "low" to "low to moderate." As noted above, the revised Confidential Appendix B is attached.

Effective Date:

PG&E requests that this advice filing become effective concurrently with the Commission's disposition of Advice Letter 3917-E.

Confidential Attachments:

In support of this advice filing, PG&E provides the following confidential supporting documentation:

- Confidential Appendix A – Redline Comparison of Original and Revised Confidential Appendix B
- Confidential Appendix B - Contract Amendment Terms and Conditions Explained (Revised October 14, 2011)
- Confidential Appendix C – Confidential Independent Evaluator Report (Revised)

Public Appendix:

- Appendix E – Public Independent Evaluator Report (Revised)

Protests:

Anyone wishing to protest this filing may do so by sending a letter by **November 3, 2011**, which is **20** days from the date of this filing. The protest must state the grounds upon which it is based, including such items as financial and service impact, and it should be submitted expeditiously. Protests should be mailed to:

CPUC Energy Division
Attention: Tariff Unit, 4th Floor
505 Van Ness Avenue
San Francisco, California 94102

Facsimile: (415) 703-2200
E-mail: mas@cpuc.ca.gov and jnj@cpuc.ca.gov

Copies should also be mailed to the attention of the Director, Energy Division, Room 4004, and Honesto Gatchalian, Energy Division, at the address shown above.

The protest should also be sent via U.S. mail (and by facsimile and electronically, if possible) to PG&E at the address shown below on the same date it is mailed or delivered to the Commission:

Pacific Gas and Electric Company
Attention: Brian K. Cherry
Vice President, Regulation and Rates
77 Beale Street, Mail Code B10C
P.O. Box 770000
San Francisco, California 94177

Facsimile: (415) 973-6520
E-mail: PGETariffs@pge.com

Effective Date:

PG&E requests that this advice filing be approved on or before **February 29, 2012**. PG&E submits this request as a Tier 3 advice letter.

Notice:

In accordance with General Order 96-B, Section IV, a copy of this Advice Letter excluding the confidential appendices is being sent electronically and via U.S. mail to parties shown on the attached list and the service lists for R.11-05-005 and R.10-05-006. Non-market participants who are members of PG&E's Procurement Review Group and have signed appropriate Non-Disclosure Certificates will also receive the Advice Letter and accompanying confidential attachments by overnight mail. Address changes to the GO 96-B service list and electronic approvals should be directed to e-mail PGETariffs@pge.com. For changes to any other service list, please contact the

Commission's Process Office at (415) 703-2021 or at Process_Office@cpuc.ca.gov.
Advice letter filings can also be accessed electronically at: <http://www.pge.com/tariffs>.

Handwritten signature of Brian Cherry in cursive script.

Vice President – Regulation and Rates

cc: Service List for R.11-05-005
Service List for R.10-05-006
Andrew Schwartz – Energy Division

Attachments

Limited Access to Confidential Material:

The portions of this Advice Letter marked Confidential Protected Material are submitted under the confidentiality protections of Sections 583 and 454.5(g) of the Public Utilities Code and General Order 66-C. This material is protected from public disclosure because it consists of, among other items, price information and analysis of the proposed Amendment, which are protected pursuant to D.06-06-066 and D.08-04-023. A separate Declaration Seeking Confidential Treatment regarding the confidential information is filed concurrently herewith. Please see above for the list of confidential attachments.

CALIFORNIA PUBLIC UTILITIES COMMISSION

ADVICE LETTER FILING SUMMARY ENERGY UTILITY

MUST BE COMPLETED BY UTILITY (Attach additional pages as needed)

Company name/CPUC Utility No. **Pacific Gas and Electric Company (ID U39 M)**

Utility type:

ELC GAS
 PLC HEAT WATER

Contact Person: David Poster or Greg Backens

Phone #: 415-973-1082 or 415-973-4390

E-mail: DxPU@pge.com or GAB4@pge.com

EXPLANATION OF UTILITY TYPE

ELC = Electric GAS = Gas
 PLC = Pipeline HEAT = Heat WATER = Water

(Date Filed/ Received Stamp by CPUC)

Advice Letter (AL) #: **3917-E-A**

Tier: 3

Subject of AL: **Supplemental Filing for the Amendment to Existing Qualifying Facility Power Purchase Agreement for Procurement of Eligible Renewable Energy Resources Between Pacific Oroville Power, Inc. and Pacific Gas and Electric Company**

Keywords (choose from CPUC listing): Contracts, Portfolio

AL filing type: Monthly Quarterly Annual One-Time Other _____

If AL filed in compliance with a Commission order, indicate relevant Decision/Resolution #: No.

Does AL replace a withdrawn or rejected AL? No. If so, identify the prior AL: N/A

Summarize differences between the AL and the prior withdrawn or rejected AL: N/A

Is AL requesting confidential treatment? Yes

If so, what information is the utility seeking confidential treatment for: Appendices A,B, and C

Confidential information will be made available to those who have executed a nondisclosure agreement: All members of PG&E's Procurement Review Group who have signed nondisclosure agreements will receive the confidential information

Name(s) and contact information of the person(s) who will provide the nondisclosure agreement and access to the confidential information: Hugh Merriam (415-973-1269)

Resolution Required? Yes No

Requested effective date: February 29, 2012

No. of tariff sheets: N/A

Estimated system annual revenue effect (%): N/A

Estimated system average rate effect (%): N/A

When rates are affected by AL, include attachment in AL showing average rate effects on customer classes (residential, small commercial, large C/I, agricultural, lighting).

Tariff schedules affected: N/A

Service affected and changes proposed: N/A

Protests, dispositions, and all other correspondence regarding this AL are due no later than 20 days after the date of this filing, unless otherwise authorized by the Commission, and shall be sent to:

CPUC, Energy Division

Tariff Files, Room 4005

DMS Branch

505 Van Ness Ave., San Francisco, CA 94102

jnj@cpuc.ca.gov and mas@cpuc.ca.gov

Pacific Gas and Electric Company

Attn: Brian K. Cherry, Vice President, Regulation and Rates

77 Beale Street, Mail Code B10C

P.O. Box 770000

San Francisco, CA 94177

E-mail: PGETariffs@pge.com

**DECLARATION OF HUGH M. MERRIAM
SEEKING CONFIDENTIAL TREATMENT
FOR CERTAIN DATA AND INFORMATION
CONTAINED IN ADVICE LETTER 3917-E-A
(PACIFIC GAS AND ELECTRIC COMPANY - U 39 E)**

I, Hugh M. Merriam, declare:

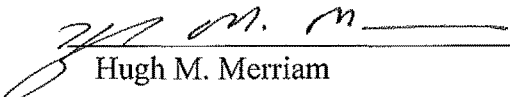
1. I am presently employed by Pacific Gas and Electric Company ("PG&E"), and have been an employee at PG&E since 1983. My current title is Manager within PG&E's Energy Procurement organization. In this position, my responsibilities include negotiating new and amended Power Purchase Agreements. In carrying out these responsibilities, I have acquired knowledge of PG&E's contracts with numerous counterparties and have also gained knowledge of the operations of electricity sellers in general. Through this experience, I have become familiar with the type of information that would affect the negotiating positions of electricity sellers with respect to price and other terms, as well as with the type of information that such sellers consider confidential and proprietary.

2. Based on my knowledge and experience, and in accordance with Decision ("D.") 08-04-023 and the August 22, 2006 "Administrative Law Judge's Ruling Clarifying Interim Procedures for Complying with Decision 06-06-066," I make this declaration seeking confidential treatment of Appendices A, B, and C to PG&E's Advice Letter 3917-E-A submitted on October 14, 2011.

3. Attached to this declaration is a matrix identifying the data and information for which PG&E is seeking confidential treatment. The matrix specifies that the material PG&E is seeking to protect constitutes the particular type of data and information listed in Appendix 1 of D.06-06-066 and Appendix C of D.08-04-023 (the "IOU Matrix"), and/or constitutes information that should be protected under General Order 66-C. The matrix also specifies the category or

categories in the IOU Matrix to which the data and information corresponds, if applicable, and why confidential protection is justified. Finally, the matrix specifies that: (1) PG&E is complying with the limitations specified in the IOU Matrix for that type of data or information, if applicable; (2) the information is not already public; and (3) the data cannot be aggregated, redacted, summarized or otherwise protected in a way that allows partial disclosure. By this reference, I am incorporating into this declaration all of the explanatory text in the attached matrix that is pertinent to this filing.

I declare under penalty of perjury, under the laws of the State of California, that to the best of my knowledge the foregoing is true and correct. Executed on October 14, 2011 San Francisco, California.



Hugh M. Merriam

PACIFIC GAS AND ELECTRIC COMPANY Advice Letter 3917-E-A October 14, 2011								
IDENTIFICATION OF CONFIDENTIAL INFORMATION PER DECISION 06-06-066 AND DECISION 08-04-023								
Redaction Reference	1) The material submitted constitutes a particular type of data listed in the Matrix, appended as Appendix 1 to D.06-06-066 and Appendix C to D.08-04-023 (Y/N)	2) Which category or categories in the Matrix the data correspond to:	3) That it is complying with the limitations on confidentiality specified in the Matrix for that type of data (Y/N)	4) That the information is not already public (Y/N)	5) The data cannot be aggregated, redacted, summarized, masked or otherwise protected in a way that allows partial disclosure (Y/N)	PG&E's Justification for Confidential Treatment	Length of Time	
1	Document: Advice Letter 3917-E-A							
2	Appendices A and B - Contract Amendment Terms and Conditions Explained	Y	Item V C) LSE Total Energy Forecast Bundled Customer (MWh). Item VI B) Utility Bundled Net Open (Long or Short) Position for Energy (MWh). Item VII B) Contracts and power purchase agreements between utilities and non-affiliated third parties. Item VII F) Renewable Resource Contracts under RPS program - Contracts with SEPs.	Y	Y	Y	This Appendix restates and describes the Amendment terms, analyzes the effect of the Amendment on the terms of the existing Power Purchase Agreement ("PPA"), and describes the financial circumstances of Pacific Oroville Power and how the Amendment will enable the Facility to operate and deliver power to PG&E at the specified price. Disclosure of this information would provide valuable market sensitive information to competitors. Individual contract information, such as price, other key terms, and descriptive information for the PPA and Amendment are protected from disclosure by Item VII B) in the IOU Matrix. Information about the counterparty's financial condition and business plans is protected by General Order 66-C, paragraph 2.8. It constitutes "[i]nformation obtained in confidence from other than a business regulated by the Commission where the disclosure would be against the public interest." Disclosure would inhibit generators from providing PG&E with the information the Commission needs for its reasonableness review and hamper negotiations between PG&E and the seller.	For information covered under Items V C), VI B), VII B), VII F), VII G), and VII (un-numbered category following VII G)), remain confidential for three years. For information covered under Item VIII A) remain confidential until after final contracts submitted to CPUC for approval.
	Appendices A and B - Contract Amendment Terms and Conditions Explained (continued)		Item VII G) Renewable Resource Contracts under RPS program - Contracts without SEPs. Item VII (un-numbered category following VII G)) Score sheets, analyses, evaluations of proposed RPS projects. Item VIII A) Bid information. Item VIII B) Specific quantitative analysis involved in scoring and evaluation of participating bids. General Order 66-C.				The Amendment is subject to a confidentiality agreement between the parties which prohibits either party from making an unauthorized disclosure of the information within the Amendment. Thus, the Amendment is not already public. Information in the Appendix cannot be aggregated, redacted, summarized, masked or otherwise protected to allow partial public disclosure without violating the non-disclosure agreement. The description of the Amendment in the Appendix consists only of information that is commercially sensitive and limited information from the public advice letter which is necessary to provide a logical context for the confidential information. This Appendix also analyzes the Amendment's contribution toward PG&E's compliance with California's Renewables Portfolio Standard ("RPS") program, assesses the Facility's viability, and compares the Amendment to other alternatives for PG&E to procure RPS-eligible energy. This information is protected from disclosure by Items V C), VI B), VII F), VII G), VII (un-numbered category following VII G)), VIII A) and VIII B) in the IOU Matrix. Disclosure of this information would provide valuable market sensitive information to competitors.	For information covered under Item VIII B), remain confidential for three years after winning bidders selected. For information covered by General Order 66-C, remain confidential indefinitely.
3	Appendix C - Independent Evaluator Report	Y	Item VII B) Contracts and power purchase agreements between utilities and non-affiliated third parties. Item VII (un-numbered category following VII G)) Score sheets, analyses, evaluations of proposed RPS projects. General Order 66-C.	Y	Y	Y	This Appendix contains information regarding the terms of the PPA and the Amendment and the financial circumstances of Pacific Oroville Power. Disclosure of this information would provide valuable market sensitive information to competitors. Individual contract information, such as price, other key terms, and descriptive information for the PPA and Amendment are protected from disclosure by Item VII B) in the IOU Matrix. Information about the counterparty's financial condition is protected by General Order 66-C, paragraph 2.8. It constitutes "[i]nformation obtained in confidence from other than a business regulated by the Commission where the disclosure would be against the public interest." Disclosure would inhibit generators from providing PG&E with the information the Commission needs for its reasonableness review and hamper negotiations between PG&E and the seller.	For information covered under Items VII B) and VII (un-numbered category following VII G)), remain confidential for three years. For information covered by General Order 66-C, remain confidential indefinitely.

Redaction Reference	1) The material submitted constitutes a particular type of data listed in the Matrix, appended as Appendix 1 to D.06-06-066 and Appendix C to D.08-04-023 (Y/N)	2) Which category or categories in the Matrix the data correspond to:	3) That it is complying with the limitations on confidentiality specified in the Matrix for that type of data (Y/N)	4) That the information is not already public (Y/N)	5) The data cannot be aggregated, redacted, summarized, masked or otherwise protected in a way that allows partial disclosure (Y/N)	PG&E's Justification for Confidential Treatment	Length of Time
Appendix C - Independent Evaluator Report (continued)						<p>The Amendment is subject to a confidentiality agreement between the parties which prohibits either party from making an unauthorized disclosure of the information within the Amendment. Thus, the Amendment is not already public. The Amendment cannot be aggregated, redacted, summarized, masked or otherwise protected to allow partial public disclosure without violating the non-disclosure agreement. PG&E has already summarized the terms of the Amendment in more general terms in the body of the Advice Letter. The description of the Amendment in the Appendix consists only of information that is commercially sensitive and limited information from the public IE report which is necessary to provide a logical context for the confidential information.</p> <p>This Appendix also analyzes the fairness of negotiations between PG&E and Pacific Oroville Power and reviews the merits of the Amendment for Commission approval (including contract price and market valuation, portfolio fit, and project viability). This information is protected from disclosure under Item VII (un-numbered category following VII G)) in the IOU Matrix. Disclosure of this information would provide valuable market sensitive information to competitors.</p>	

Advice 3917-E-A

Public Appendix E

Public Independent Evaluator Report (Revised)

ARROYO SECO CONSULTING

PACIFIC GAS AND
ELECTRIC COMPANY
CONTRACT
AMENDMENT
EVALUATION

ADVICE LETTER REPORT OF THE
INDEPENDENT EVALUATOR ON AN
AMENDED CONTRACT WITH PACIFIC
OROVILLE POWER, INC.

SEPTEMBER 28, 2011

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EXECUTIVE SUMMARY

This report provides an independent evaluation of the process by which the Pacific Gas and Electric Company (“PG&E”) negotiated and executed a contract amendment to an existing long-term Qualifying Facility (QF) contracts with Pacific Oroville Power, Inc. (“POPI”), a wholly-owned subsidiary of Covanta Energy Corporation, itself a subsidiary of Covanta Holding Corporation.

This proposed amendment originated from the project owner’s pursuit of temporary price relief from the existing contract. An independent evaluator (IE), Arroyo Seco Consulting (Arroyo), conducted activities to review and assess PG&E’s processes as the utility evaluated and negotiated the contract amendment.

The structure of this report generally follows the 2011 RPS Independent Evaluator Report Template provided by the Energy Division of the CPUC.¹ Topics covered include:

- The role of the IE;
- The fairness of the design of PG&E’s least-cost, best-fit (LCBF) methodology;
- Fairness of project-specific negotiations; and
- Merit of the amendment for CPUC approval.

Arroyo’s opinion is that the negotiations between PG&E and Covanta were generally conducted fairly, although the treatment of POPI may have been less than fully fair to other counterparties. Ratepayer protections in the amendment are stronger than those in the existing QF contracts and Arroyo’s opinion is that ratepayers were treated fairly in the project-specific negotiations.

While Arroyo agrees with PG&E that the amendment merits CPUC approval, Arroyo has a few reservations that are described in greater detail in the confidential appendix to this report. In Arroyo’s opinion, the contract amendment ranks as moderate in net valuation and ranks low to moderate in contract price relative to competing short-term in-state alternatives available to PG&E. Arroyo ranks the currently operational facility as quite high in physical project viability, and as moderate in portfolio fit. Continued operation of the project will contribute to Executive Order S-06-06’s goal for the role of biomass in the state’s renewable energy mix.

¹ The amendments are not modern RPS contracts, but rather amended QF contracts, so this report does not strictly follow the RPS IE template but omits sections relevant for an RPS solicitation.

1. ROLE OF THE INDEPENDENT EVALUATOR

This chapter elaborates on the prior CPUC decisions that form the basis for an Independent Evaluator's participation in reviewing contracts that are negotiated by IOUs, describes key roles of the IE, details activities undertaken by the IE in this transaction to fulfill those roles, and identifies the treatment of confidential information.

A. CPUC DECISIONS REQUIRING INDEPENDENT EVALUATOR PARTICIPATION

The CPUC first mandated a requirement for an independent, third-party evaluator to participate in competitive solicitations for utility power procurement in its Decision 04-12-048 on December 16, 2004 (Findings of Fact 94-95, Ordering Paragraph 28). In that Decision, which addressed the approval of three utilities' long-term procurement plans, the CPUC required the use of an IE when Participants in a competitive procurement solicitation include affiliates of investor-owned utilities (IOUs), IOU-built projects, or IOU-turnkey projects. The Decision envisaged that establishing a role for an IE would serve as a safeguard in the process of evaluating IOU-built or IOU-affiliated projects competing against Power Purchase Agreements (PPAs) with independent power developers, a safeguard to protect consumers from any anti-competitive conduct between utilities and their corporate affiliates or from anti-competitive conduct by utilities developing their own generation.

Later, in approving the IOUs' 2006 RPS procurement plans and solicitation protocols, the CPUC issued Decision 06-05-039 on May 25, 2006. In that Decision, the CPUC expanded its requirement, ordering that each IOU use an IE to evaluate and report on the entire solicitation, evaluation, and selection process, for the 2006 RPS RFO and all future competitive solicitations, whether or not a utility affiliate or utility-owned generation is involved. The POPI contract amendment did not arise from a competitive solicitation.

Subsequently, as part of Rulemaking 08-08-009 to continue implementation of the RPS program, the CPUC issued Decision 09-06-050 on June 19, 2009. In that decision, the Commission concluded that short-term bilaterally negotiated RPS contracts (e.g. those with term of less than ten years but more than one month) should be governed by the same contract review processes and standards as contracts that arise through competitive solicitations, including review by an IE.

Arroyo perceives there to a spectrum between (1) a minimally amended 1980s-style Standard Offer contract with a renewable QF (e.g. one in which, say, the delivery point is altered by amendment but all other terms and conditions are unchanged) and (2) a fully renegotiated agreement with a renewable QF that closely follows PG&E's 2011 RPS Form Agreement and for which price, delivery term, and most terms and conditions are altered from 1980s' language to 2011 language. Arroyo would speculate that (2) would likely meet

the intent of Decision 09-06-050 and clearly require an accompanying IE report, while (1) might not. Arroyo perceives the amendment to the POPI QF agreement to be closer to (1) than to (2) and appears to fall into a gray area where it is unclear whether an IE report is formally required. The Energy Division has directed the utility to provide an accompanying IE reports with its advice letters for amendments to biomass-fueled QF agreements.

B. KEY INDEPENDENT EVALUATOR ROLES

PG&E retained Arroyo Seco Consulting to serve as IE for the POPI contract amendment.

The CPUC stated its intent for participation of an IE in competitive procurement solicitations to “separately evaluate and report on the IOU’s entire solicitation, evaluation and selection process”, in order to “serve as an independent check on the process and final selections.”² More specifically, the Energy Division (ED) of the CPUC has provided a template to guide how IEs should report on the 2011 RPS competitive procurement process, outlining specific issues that should be addressed:

1. Describe the IE’s role.
2. Did the IOU do adequate outreach to potential bidders, and was the solicitation robust?
3. Was the IOU’s least-cost, best-fit (LCBF) methodology designed such that bids were fairly evaluated?
4. Was the LCBF bid evaluation process fairly administered?
5. Describe the fairness of the project-specific negotiations.
6. Does the contract merit CPUC approval?

In this situation, in which the contract is an amendment to an existing QF contract with an eligible renewable resource rather than a modern RPS contract that resulted from a competitive solicitation, Arroyo’s focus is in reporting is on the first, third, fifth, and sixth of these elements of a standard IE report for RPS solicitations.

C. IE ACTIVITIES

To fulfill the role of evaluating the POPI contract amendment, several tasks were undertaken. Arroyo had performed several of these tasks within its work scope of serving as IE for PG&E’s 2011 RPS competitive solicitation; these prior activities were directly relevant to the evaluation of the POPI contract amendment.

² CPUC Decision 06-05-039, May 25, 2006, “Opinion Conditionally Approving Procurement Plans for 2006 RPS Solicitations, Addressing TOD Benchmarking Methodology”, page 46.

- Reviewed the 2011 RPS RFO Solicitation Protocol and its various attachments including the Forms of Power Purchase Agreement (PPA) and PG&E’s detailed description of its LCBF bid evaluation and selection process and criteria;
- Examined the utility’s nonpublic protocols detailing how PG&E evaluates proposed contracts against various criteria, including market valuation, portfolio fit, transmission adders, credit, project viability, and RPS goals;
- Interviewed members of PG&E’s evaluation committee and sub-committees regarding the process, data inputs and parameters, background industry and utility information, quantitative models, and other considerations taken into account in evaluating contracts against non-quantitative criteria and in performing market valuation of contracts;
- Reviewed in detail various data inputs and parameters used in PG&E’s LCBF market valuation methodology.
- Spot-checked contract-specific data inputs to PG&E’s valuation model;
- Built an independent valuation model and used it to value proposed contracts. This served as a cross-check against PG&E’s LCBF market valuation model. The IE model used independent inputs and a different methodology than PG&E’s LCBF methodology. It was much simpler and lacked detail and granularity used in aspects of the PG&E model.
- Developed an independent project viability score, using the ED’s 2011 version of the Project Viability Calculator;
- Reviewed PG&E’s evaluation on criteria other than market valuation and project viability, testing for consistency and fairness in the treatment of contracts;
- Attended meetings of PG&E’s Procurement Review Group (PRG) in which the utility updated the PRG on negotiations with biomass-fueled QFs;
- Directly observed (telephonically) negotiation sessions between PG&E and Covanta Energy;
- Reviewed documents that passed between the two parties during the negotiation, including draft term sheets, draft contracts, and supporting documentation.

D. TREATMENT OF CONFIDENTIAL INFORMATION

The CPUC’s Decision 06-06-066, issued on June 29, 2006, detailed specific guidelines for the treatment of information as confidential vs. non-confidential in the context of IOU electricity procurement and related activities, including competitive solicitations and bilaterally negotiated agreements. For example, the Decision provides for confidential

treatment of “Score sheets, analyses, evaluations of proposed RPS projects”,³ as opposed to public treatment (after submittal of final contracts for CPUC approval) of the total number of projects and megawatts bid by resource type.

To the extent that Arroyo’s reporting on the evaluation of the POPI contract amendment requires a more explicit discussion of such analyses, scores, and evaluations, an in-depth narrative of commercially sensitive negotiations, and a more specific critique of specific contract terms and conditions, these are handled in greater detail in the confidential appendix to this report.

³ California Public Utilities Commission, “Interim Opinion Implementing Senate Bill No. 1488, Relating to Confidentiality of Electric Procurement Data Submitted to the Commission”, June 29, 2006, Appendix 1, page 17

2. FAIRNESS OF PG&E'S CONTRACT EVALUATION METHODOLOGY

The key finding of this chapter is that, based on IE activities and findings, PG&E's evaluation methodology was designed fairly. The same methodology that the utility applies to bilaterally negotiated RPS proposals was applied to the review of the POPI contract amendment.⁴

The following discussion identifies principles for evaluating the methodology, describes the methodology, evaluates the strengths and weaknesses of the chosen methodology, and identifies some specific issues with the methodology and its inputs that Arroyo recommends be addressed in future solicitations.

A. PRINCIPLES FOR EVALUATING THE METHODOLOGY

The Energy Division of the CPUC has usefully suggested a set of principles for evaluating the process used by IOUs for evaluating contracts in competitive renewable solicitations, within the template intended for use by IEs in reporting. The principles include:

- The IOU bid evaluation should be based only on information submitted in bid proposal documents.
- There should be no consideration of any information that might indicate whether the bidder is an affiliate.
- Procurement targets and objectives were clearly defined in the IOU's solicitation materials.
- The IOU's methodology should identify quantitative and qualitative criteria and describe how they will be used to rank bids. These criteria should be applied consistently to all bids.
- The LCBF methodology should evaluate bids in a technology-neutral manner.
- The LCBF methodology should allow for consistent evaluation and comparison of bids of different sizes, in-service dates, and contract length.

Some additional considerations appear relevant to the specific situation PG&E finds itself in when evaluating renewable power contracts. Unlike some utilities, PG&E does not rely on weighted-average calculations of scores for various evaluation criteria to arrive at a

⁴ This approach is a modified version of the methodology applied to Offers received in PG&E's competitive RPS solicitations; the modification is described below, under "Transmission Cost Adders"

total aggregate score. Instead, the team ranks contracts by net market value using its methodology, after which, “[u]sing the information and scores in each of the other evaluation criteria, PG&E will decide which Offers to include and which ones not to include on the Shortlist.”⁵ The application of judgment in bringing the non-valuation criteria to bear on decision-making, rather than a mechanical, quantitative means of doing so, implies an opportunity to test the fairness and consistency of the method using additional principles:

- The methodology should identify how non-valuation measures will be considered; non-valuation criteria used in evaluating contracts should be clear to counterparties.
- The logic of using non-valuation criteria or preferences to reject high-value contracts and select low-value contracts should be applied consistently and without bias.
- The valuation methodology should be reasonably consistent with industry practices.

B. PG&E’S LEAST-COST BEST-FIT METHODOLOGY

The California state legislation that mandated the RPS program required that the procurement process use criteria for the selection of least-cost and best-fit renewable resources; in its Decisions D.03-06-071 and D.04-07-029 the CPUC laid out detailed guidelines for the IOUs to select LCBF renewable resources. PG&E adopted selection and evaluation processes and criteria for its 2011 RPS RFO. These are summarized in Section XI of PG&E’s 2011 Solicitation Protocol for its renewable solicitation, and detailed in Attachment K to that Solicitation Protocol.

Additionally, PG&E developed nonpublic documents for internal use that detail the protocols for each individual criterion used in the evaluation process. These include:

- Market valuation
- Portfolio fit
- Credit (including provision of collateral requirements)
- Project viability
- RPS goals
- Adjustment for transmission cost adders
- Ownership eligibility
- Sites for development

The first six of these are listed as evaluation criteria in the 2011 RPS RFO solicitation protocol. Additionally, the protocol states two other evaluation criteria: the materiality and

⁵ “Renewables Portfolio Standard, 2011 Solicitation Protocol, Pacific Gas and Electric Company, May 11, 2011 (Updated June 7, 2011)”, page 40

cost impact of counterparty's proposed modifications to PG&E's Form Agreement, and the total volume of offers submitted by a single counterparty (considering the volume of energy already under contract as well).

This section summarizes PG&E's methodology briefly and at a high level; readers are referred to the Solicitation Protocol and its Attachment K for a fuller treatment of the detailed methodology.

MARKET VALUATION

PG&E measures market value as benefits minus costs. Benefits include energy value and capacity value (Resource Adequacy value); ancillary services value is assumed zero. Costs are PG&E's payments to the counterparty, appropriately adjusted by Time-of-Delivery (TOD) factors as specified in the Solicitation Protocol. The TOD factors serve as a multiplier to the contract price per megawatt-hours (MWh) based on the time of day and season of the delivery, and are intended to reflect the relative value of the energy and capacity delivered in those time periods. Also, costs are adjusted to reflect transmission adds. The costs of integrating an intermittent resource into the electric system, such as load-following, providing imbalance services, operational reserves, and regulation, are assumed zero. Both benefits and costs are discounted from the entire contract period to 2011 dollars per MWh in the methodology.

For as-available energy delivery, PG&E measures energy value by projecting a forward energy curve (in hourly granularity) out to the time horizon of the contract period, and multiplying projected hourly energy price by the projected hourly generation specified by the contract's generation profile. For peaking or baseload contracts, the energy quantity is based on the performance requirements of the contract.

PG&E projects Resource Adequacy (capacity) value as a nominal dollar per kilowatt-year estimate. The CPUC recently revised the Resource Adequacy methodology that load-serving entities use to calculate Net Qualifying Capacity for intermittent generation that is sold on an as-available basis. While previously capacity quantity was calculated based on the annual average of the generation profile for the noon to 6 p.m. period, now the calculation is based on averaging the generation profile over five-hour blocks, the hours of which differ between April-October and November-May to reflect the different timing of peak demand in different seasons.⁶ Also, the CPUC decided to base the Net Qualifying Capacity on a 70% exceedance level for these solar and wind resources whose output is stochastic in nature, in a calculation that takes into account diversity benefits of multiple individual generators with different profiles. The PG&E team has adapted its calculations of Resource Adequacy value to reflect the new definition of Net Qualifying Capacity.

For baseload and dispatchable resources, the capacity quantity is determined by the performance requirements of the contract. Capacity benefit is calculated as the product of capacity value and quantity, and discounted to 2011 nominal dollars.

⁶ California Public Utilities Commission, Decision 09-06-028, "Decision Adopting Local Procurement Obligations for 2010 and Further Refining the Resource Adequacy Program", June 18, 2009

PG&E incorporates compliance costs for greenhouse gases into the costs of non-renewable generation. This feature only affects the net valuation of contracts indirectly, to the extent that projected future compliance costs are estimated to affect the value of capacity.

PORTFOLIO FIT

For the 2011 renewable solicitation, PG&E employed a quantitative scoring system to assess the portfolio fit of a contract into its overall set of energy resources and obligations. The team calculated one score for the firmness of delivery of the offered resource and another score for the time of delivery of the resource (relative to PG&E's portfolio needs). The overall score for portfolio fit is the numerical average of the two. This detailed methodology is not typically employed by PG&E for evaluating bilateral contracts.

CREDIT

PG&E assesses the degree to which counterparties propose to meet the requirements for providing collateral to meet their obligations. The requirements for collateral, described in detail in Section VII of the Solicitation Protocol, include posting Project Development Security after a PPA or PSA is executed and before Commercial Operation Date of the project, and posting Delivery Term Security for a PPA following the commencement of commercial operation.

PROJECT VIABILITY

PG&E uses the 2011 final version of the Project Viability Calculator provided by the ED as a screening tool to assess the likelihood that a proposed generation facility will be completed and enter full commercial operation on the proposed on-line date.

The viability score is developed through an assessment of several attributes of the project, including

- Project development experience,
- Ownership and operating and maintenance experience,
- Technical feasibility,
- Resource quality,
- Manufacturing supply chain (e.g. degree of constraints upon availability of key components),
- Site control,
- Permitting status,
- Project financing status,

- Interconnection progress,
- Transmission requirements, and
- Reasonableness of Commercial Operation Date (COD).

In POPI's case, the generating facility already exists and is currently operating, so physical viability is not a concern. The Calculator is most useful in screening proposed new projects to assess their relative viability as opposed to evaluating existing, operating projects.

RPS GOALS

PG&E assesses the degree to which a contract is consistent with and will contribute to the state of California's goals for the RPS Program, and the degree to which a contract will contribute to PG&E's goals for supplier diversity. The CPUC has articulated specific attributes of renewable generation projects which can be considered in utility procurement evaluations, such as benefits to low-income or minority communities, environmental stewardship, and resource diversity, that do not clearly fall within the other evaluation criteria. Similarly, the CPUC has issued a Water Action Plan, and to the extent a renewable energy project makes use of water on site, its proposed use of water is evaluated for consistency or inconsistency with the CPUC's recommended water conservation practices.

Additionally, the California Legislature articulated program benefits anticipated for the RPS program in the Legislative Findings and Declarations associated with the laws passed to create the program, and PG&E assesses the degree to which contracts would promote these benefits.

The Governor of California issued Executive Order S-06-06 that, among other things, established a goal that the state will meet 20% of its renewable energy needs with electricity generated from biomass. PG&E assesses the extent to which a project supports that goal.

PG&E has well-defined corporate objectives for supplier diversity, and evaluates whether the counterparty is, or will make a good faith effort to subcontract with, Women-, Minority-, and Disabled Veteran-owned Business Enterprises.

PG&E's methodology for scoring projects in the RPS solicitations on their support for RPS Goals involves scoring attributes of the proposal and calculating a weighted-average numerical score. This numerical approach is typically not employed to evaluate bilaterally negotiated contracts.

TRANSMISSION COST ADDERS

The cost of transmission to move power from a project offered in the solicitation to PG&E retail customers is considered in the process of market valuation. The methodology takes into account the possible need to upgrade the transmission network in order to accommodate the increment of new renewable generation in locations (clusters) that may require significant capital outlay, either by PG&E or by other IOUs. Each California IOU publishes a Transmission Ranking Cost Report (TRCR) which identifies clusters that would require network upgrades to accommodate some level of new generation, and estimates a

proxy for the cost of upgrades and the amount of new generation that would trigger the need for upgrades. If a CAISO interconnection study has been completed, the team can use the more project-specific estimate of transmission network upgrade costs identified in the study rather than the TRCR proxy.

PG&E does not use TRCR adders in the evaluation of bilaterally negotiated contracts, and did not use a TRCR adder in evaluating the POPI contract amendment; the facility is already interconnected to the grid and operating, and continued operation will likely require no network upgrades as long as the QF continues operating under its existing agreement, which includes a CPUC-jurisdictional interconnection.

UTILITY OWNERSHIP ALTERNATIVES AND SITES FOR DEVELOPMENT

PG&E has developed protocols for evaluation of proposals to sell the utility a site for development of renewable generation, to build and transfer to utility ownership a new facility, to provide the utility with an option to purchase a facility after some period of commercial operation, or to undertake joint development and/or joint ownership of a new facility. The evaluation of such Offers includes both an analysis of the economics of the project generation under utility ownership, analogous to the valuation of PPAs, as well as a consideration of the extent to which ownership of such a project is compatible with the utility's core competencies.

COUNTERPARTY CONCENTRATION

In the 2011 RPS solicitation protocol, PG&E stated explicitly that it will consider its total exposure to volume of contracted deliveries from any individual counterparty as well as the volume already contracted with the counterparty in making short list decisions. Arroyo regards supplier concentration as a legitimate business concern for the utility, both with respect to credit risk for the utility's supply portfolio as well as risk of development failure.

PG&E'S PREFERENCES REGARDING OFFERS

In addition to the various evaluation criteria, PG&E's 2011 solicitation protocol stated two preferences regarding selection of Offers. In section III regarding Solicitation Goals, the discussion of resource needs indicates that because of uncertainty about regulatory implementation of SBX 2 the utility "will encourage bids that recognize that uncertainty and offer flexibility toward meeting a range of possible targets" Arroyo views this as a reasonable preference to take into account when making a short list given the utility's current procurement position and the state of flux in regulatory decisions.

PG&E also stated in its solicitation protocol a preference for projects that deliver power to "a nodal delivery point...within PG&E's service territory" over projects that deliver to CAISO interface points (e.g. the California-Oregon Border, or COB, or points such as Mead, Palo Verde, or Four Corners substations) or to "California locations outside of the CAISO's control area", or to out-of-state locations.

Arroyo regards this as a reasonable preference, and appropriate to state in the protocol. Some of the operators of control areas external to the CAISO have in the past chosen not to provide services such as imbalance service or operating reserves that would be required to enable an intermittent generator such as a wind or solar photovoltaic facility that

interconnects in their territory to schedule firm deliveries to a CAISO intertie. For other control area operators, there is a limitation on availability of transmission to wheel power within their territory from a generator to and across a CAISO interface point, as there has been on Path 42 between the IID and Southern California Edison territories.

In addition to these preferences stated in the 2011 RPS RFO solicitation protocol, in the bidders' conference for the RFO PG&E stated that it "expects to focus on the latter part of the second (2014-2016) compliance period".

3. FAIRNESS OF PROJECT-SPECIFIC NEGOTIATIONS

This chapter gives an independent review of the extent to which PG&E's negotiations with Covanta to enter into a contract amendment to the existing POPI QF agreement were conducted fairly. A more detailed narrative of discussion points of the negotiation and issues of fairness to other counterparties is provided in the confidential appendix to this report.

A. PRINCIPLES FOR EVALUATING THE FAIRNESS OF NEGOTIATIONS

Arroyo took into account several principles to evaluate the degree of fairness with which POPI and other entities that are seeking to obtain temporary price relief PG&E were treated in the course of project-specific negotiations.

- Were counterparties treated fairly and consistently by PG&E during negotiations? Were all counterparties given equitable opportunities to advance their proposals towards final PPAs? Were individual counterparties given unique opportunities to move their proposals forward or concessions to improve their contracts' commercial value, opportunities not provided to others?
- Was the distribution of risk between Seller and Buyer in the PPAs distributed equitably across PPAs? Did PG&E's ratepayers take on a materially disproportionate share of risks in some contracts and not others? Were individual counterparties given opportunities to shift their commercial risks towards ratepayers, opportunities that were not provided to others?
- Was non-public information provided by PG&E shared fairly with all counterparties in discussions? Were individual counterparties uniquely given information that advantaged them in securing contracts or realizing commercial value from those contracts?
- If any individual counterparty was given preferential treatment by PG&E in the course of negotiations, is there evidence that other counterparties were disadvantaged by that treatment? Were other proposals of comparable value to ratepayers assigned materially worse outcomes?
- Were some parties denied the opportunity to make changes to basic terms of the contract amendment while other parties were allowed to adjust those terms in their amendments based on their preferences or concerns?

**B. INDEPENDENT EVALUATOR'S OBSERVATIONS OF NEGOTIATIONS
BETWEEN POPI AND PG&E**

Arroyo observed several negotiation sessions between PG&E's and Covanta's staffs over the course of several weeks. Arroyo was also able to review several draft versions of term sheets and agreements in order to identify specific proposals and counterproposals the parties made regarding terms in the course of discussion, as well as supporting documents.

Based on this review, Arroyo did not identify any situations where PG&E provided POPI with concessions in contract terms that Arroyo considered to be materially unfair to ratepayers. Arroyo believes that information provided to Covanta has generally been made available to other competing counterparties that are renewable QF generators actively seeking contract amendments. Arroyo's opinion is that POPI was not unfairly advantaged (to the detriment of ratepayers or competing facilities) by PG&E providing unique confidential information that has not been provided to others. Arroyo believes that in the course of the summer of 2011, PG&E stood open to pursue discussions with other contracted renewable QFs with issues similar to POPI, with the qualification that Arroyo is not directly involved in all contacts the utility has with all owners of renewable QFs.

The executed POPI amendment provides ratepayers with several specific protections not provided in the existing QF contracts. The QF contract as amended shifts certain risks towards POPI from ratepayers that the project does not bear in the existing contract. Arroyo believes that the POPI contract amendment falls somewhat short of the ratepayer protections provided by modern short-term RPS contracts that PG&E has entered, though there are provisions in the amendment that significantly mitigate concerns about these variances. Arroyo does not believe that, given the situation where a 1980's-era QF agreement is amended for a short portion of the remaining term, rather than a fully new long-term RPS contract being executed, these variances create a serious level of concern about the fairness to ratepayers of the amendment, especially given the new protections given to ratepayers compared to the unamended contract. These issues are discussed in detail in the confidential appendix to this report.

Arroyo's review of the POPI contract amendment suggests that in most respects it does not provide the project with terms and conditions that are materially more advantageous to the sellers than could have been the case had the parties used a short-term version of PG&E's RPS Form Agreement. In that sense the amended contract is almost comparable in ratepayer protections to other agreements with terms less than five years that PG&E has executed.

Arroyo has been asked by the ED to opine on the extent to which project-specific negotiations with biomass-fueled QFs have been fair to the individual sellers; this has not been an aspect of procurement of RPS-eligible energy that Arroyo routinely discusses in the course of other IE reports. While Arroyo believes that POPI itself was generally treated fairly in the course of negotiations, there are a case in which disparate treatment of another project tended to disfavor that seller compared to the treatment that POPI received. Arroyo's opinion is that the treatment of competing sellers appears to be less than fully fair; details are provided in the confidential appendix to this report.

4. MERIT FOR CPUC APPROVAL

This chapter provides an independent review of the merits of the amendment to the contracts between PG&E and POPI against criteria identified in the Energy Division's 2011 RPS IE template.⁷

A. CONTRACT SUMMARY

On August 8, 2011, PG&E and POPI executed a contract amendment to their existing QF contract that governs delivery of renewable energy from a woody waste biomass-fueled generator. The existing, operating facility is located in the southern part of the city of Oroville in Butte County, and has produced renewable energy for PG&E customers for more than two decades. The term of the amendment is three years and can be extended at PG&E's option by two periods of an additional year and an additional seven months (to the termination date of the existing QF agreement). The amendment sets a contract quantity of 123 GWh annually.

B. NARRATIVE OF EVALUATION CRITERIA AND RANKING

The 2011 template for IEs provided by the Energy Division calls for a narrative of the merits of the proposed project on the criteria of contract price, portfolio fit, and project viability. More specific details are provided in the confidential appendix to this report.

CONTRACT PRICE AND MARKET VALUATION

Arroyo has compared the net value of the POPI amendment to relevant peer groups of previously and currently offered competing sources of RPS-eligible energy, using both PG&E's LCBF methodology and the simpler but independent IE model. Based on those comparisons, Arroyo opines that the market valuation of the POPI amendment ranks as moderate compared to relevant peer groups of competing proposals, and the contract price ranks as low to moderate. The confidential appendix to this report provides a more detailed discussion of the pricing of the contract amendment and the basis for Arroyo's opinion that the net valuation of the amendment ranks as moderate among competing alternatives.

PORTFOLIO FIT

Arroyo ranks the POPI contract amendment's fit with PG&E's supply portfolio needs as moderate. The existing facility generally operates as a baseload generator. While PG&E does not have an immediate need for more baseload generation, removing the project's

⁷ While the amendments modify existing QF contracts for power delivery from eligible renewable resources and are not strictly RPS agreements, Arroyo regards the 2011 RPS IE template as the most applicable approach to discussing the amendments' merits, rather than a non-RPS template.

production from the portfolio might create or accelerate such a need at some point in time. Similarly, if POPI should curtail or cease production in the absence of temporary price relief, this might create or accelerate a need for PG&E to procure more RPS-eligible power in the first or second RPS compliance periods.

PROJECT VIABILITY

In Arroyo's opinion, the physical project viability of the POPI facility is high. The project has operated for decades to provide PG&E customers with renewable energy. An existing, currently operating project is more viable, in a physical sense, than any proposed as-yet-unbuilt generator.

RPS GOALS

The POPI contract amendment would advance PG&E and the state towards the goal stated in Executive Order S-06-06 of providing at least 20% of the state's renewable power needs from biomass-based generation. Arroyo believes that PG&E currently exceeds that target, but over time there is some risk that biomass as a portion of PG&E's portfolio will drop below 20% because of impending rapid growth in other sources of renewable generation. Arroyo believes that approval of the contract amendment will significantly increase the likelihood that POPI will continue to provide PG&E customers with generation over the term of the amendment, as opposed to seasonally curtailing or ceasing its production under the pricing of the existing contract.

Additionally, the legislative findings stated in Senate Bill 1078 that established the RPS program included a view that increasing the use of renewable energy sources may create employment opportunities. The CPUC's Decision 04-07-029 included benefits to low-income communities as a qualitative attribute that could be taken into consideration by utilities in evaluating competitive offers for new renewable generation. In the absence of a contract amendment there is greater risk to POPI's employment base. The project is sited in a location with higher incidence of poverty and lower median household income than the state as a whole.

C. DISCUSSION OF MERIT FOR APPROVAL

Arroyo concurs with PG&E management that the POPI contract amendment merits CPUC approval, although Arroyo has a few reservations about the amendment, described in greater detail in the confidential appendix to this report. In Arroyo's opinion the contract amendment offers moderate net value, low to moderate contract price, and high project viability. They would contribute to PG&E's efforts to meet its RPS Goals. In particular, the contract amendment would support continued compliance with Executive Order S-06-06 regarding the goal for biomass-fueled generation in the state. It would protect against employment losses in a locality with a higher proportion of low-income residents than the state at large.

Arroyo's opinion is that the special considerations relating to the contract amendment's support of RPS program goals and grid reliability outweigh the IE's modest reservations. However, any individual decision-maker's judgment about the merits of the POPI contract amendment may depend on the policy-maker's relative emphasis placed on the cost impact

of the amendment upon ratepayers or the fairness with how the amendment was negotiated, vs. the contribution of the projects' continued operation to meeting the state's biomass-fueled generation goal, to employment stability, and to local grid reliability.

**PG&E Gas and Electric
Advice Filing List
General Order 96-B, Section IV**

AT&T	Dept of General Services	Northern California Power Association
Alcantar & Kahl LLP	Douglass & Liddell	Occidental Energy Marketing, Inc.
Ameresco	Downey & Brand	OnGrid Solar
Anderson & Poole	Duke Energy	Praxair
Arizona Public Service Company	Economic Sciences Corporation	R. W. Beck & Associates
BART	Ellison Schneider & Harris LLP	RCS, Inc.
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California Energy Commission	Lawrence Berkeley National Lab	Southern California Edison Company
California League of Food Processors	Los Angeles Dept of Water & Power	Spark Energy, L.P.
California Public Utilities Commission	Luce, Forward, Hamilton & Scripps LLP	Sun Light & Power
Calpine	MAC Lighting Consulting	Sunshine Design
Cardinal Cogen	MBMC, Inc.	Sutherland, Asbill & Brennan
Casner, Steve	MRW & Associates	Tabors Caramanis & Associates
Chris, King	Manatt Phelps Phillips	Tecogen, Inc.
City of Palo Alto	McKenzie & Associates	Tiger Natural Gas, Inc.
City of Palo Alto Utilities	Merced Irrigation District	TransCanada
City of San Jose	Modesto Irrigation District	Turlock Irrigation District
Clean Energy Fuels	Morgan Stanley	United Cogen
Coast Economic Consulting	Morrison & Foerster	Utility Cost Management
Commercial Energy	NLine Energy, Inc.	Utility Specialists
Consumer Federation of California	NRG West	Verizon
Crossborder Energy	NaturEner	Wellhead Electric Company
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Defense Energy Support Center	North America Power Partners	
Department of Water Resources	North Coast SolarResources	