



Clay Faber
Director – Regulatory Affairs
8330 Century Park Court
San Diego, CA 92123-1548

Tel: 858-654-3563
Fax: 858-654-1788
CFaber@semprautilities.com

July 31, 2012

ADVICE LETTER 2390-E
(U 902-E)

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

**SUBJECT: REQUEST FOR EXPEDITED APPROVAL OF RESOURCE ADEQUACY
CONTRACT WITH NRG POWER MARKETING LLC FOR THE ENCINA
POWER STATION**

San Diego Gas & Electric Company (“SDG&E”) hereby submits to the California Public Utilities Commission (the “Commission” or the “CPUC”) for approval the *Confirmation for Resource Adequacy Capacity Product for CAISO Resources* with NRG Power Marketing LLC (“NRG”) (“Confirmation”).¹ This Confirmation, under which SDG&E will buy and NRG will sell resource adequacy (“RA”) product from the Encina Power Station (“Encina”) during the period January 1, 2013, through December 31, 2013, was bilaterally negotiated and agreed upon to address capacity requirements within the San Diego area in 2013.

SDG&E respectfully urges the Commission to process this request for approval on an expedited basis.

A. BACKGROUND

Encina is a natural gas-fired conventional thermal/steam plant which is subject to the California Once-Through Cooling (“OTC”) policy and has a 2017 OTC compliance deadline. Encina has a long history of contracting with both SDG&E and the California Independent System Operator (“CAISO”) as part of meeting local reliability needs.

The Confirmation, which contemplates an RA-only transaction for compliance year 2013, will keep the plant available to the CAISO for one year.

¹ The filing of this advice letter does not constitute waiver of SDG&E’s right to assert that it is authorized under its 2012 long-term procurement plan to enter into a transaction such as that described herein without the need to seek Commission approval through an advice letter or application filing.

B. CONTRACT SUMMARY

The following table provides a summary of key aspects of the proposed transaction:

Counterparty	NRG Power Marketing LLC
Resource type	Natural Gas Fired
Location	NRG Encina Power Station, Carlsbad, CA
Capacity	965 MW
Expected Deliveries	Local & System Resource Adequacy Capacity (no energy or ancillary services)
Delivery Point	CAISO Balancing Authority Area / Local Capacity Area ("LCA") within which the Encina units are electrically interconnected.
Length of Contract	One -Year; January 1, 2013 – December 31, 2013

C. THE SDG&E - NRG ENCINA NEGOTIATIONS

The substance of the negotiations conducted between SDG&E and NRG for the 2013 Encina RA capacity and a pricing analysis are provided in Confidential Attachment A to this Advice Letter. Confidential Attachment B contains a full copy of the executed Confirmation. SDG&E believes the contents of both Attachment A & B should be protected from public disclosure and requests that the Commission treat the information provided in those Attachments as confidential. Accompanying this Advice Letter is a Declaration in support of this request to preserve the confidentiality of the information provided in Attachments A & B.

D. LOCAL CAPACITY REQUIREMENTS

This Section D provides an overview of key components of the annual Resource Adequacy process which have come together to establish the circumstances that lead to the current need for the RA transaction described in this advice letter.

1. **ANNUAL GRID TECHNICAL STUDY PROCESS:** On April 30, 2012 the CAISO published its *2013 Local Capacity Technical Analysis – Final Report and Study Results* ("2013 LCT Study").² These annual technical analyses accomplish four purposes:³
 - a) Determining minimum quantities of local generation capacity necessary, the Local Capacity Requirement ("LCR"), to ensure reliable grid operations in transmission-constrained load pockets with limited power-import capability, Local Capacity Areas ("LCA")

² Filed with the CPUC on May 2, 2012; <http://docs.cpuc.ca.gov/efile/REPORT/165689.pdf>

³ CAISO *2012 Local Capacity Technical Analysis – Final Report and Study Results*, April 29, 2011, p. 1

- b) Serving as a basis for the local procurement obligations issued by the CPUC to Load Serving Entities (“LSE”) under its resource adequacy program⁴
 - c) Assisting in cost allocation regarding any CAISO capacity procurement needed to achieve grid reliability, and
 - d) Providing additional information on LCA sub-area needs and effectiveness factors in order to allow LSEs to engage in more informed capacity procurement in their LCA
2. **EVOLVING LOCAL CAPACITY AREAS:** There are ten (10) major LCAs within the CAISO Balancing Authority Area each of which can have further refined LCA sub-areas. For SDG&E there has always been just one major LCA, the San Diego local capacity area (“SD Area”), extending as far east as the Miguel and Sycamore substations, along with 5-10 LCA sub-areas (these may change year-to-year based on load growth and transmission grid enhancements). The LCR for the traditional SD Area, as determined in the annual technical study, has historically been the basis for the CPUC in assigning local RA obligations to LSEs in the San Diego region. While the sub-areas have not come into play in establishing LSE RA obligations, the CAISO, as discussed in Section D.3 below, has the authority to procure capacity needed to meet grid reliability criteria even to the sub-area level.

The 2012 planning cycle was affected by the placing into service of the Sunrise Powerlink transmission line (“SRPL”). The result of the addition of a major 500 KV transmission line was that the San Diego area grid constraints shifted significantly enough to cause the creation of a new San Diego-Greater Imperial Valley Area (“SD-IV Area”). In the 2012 technical study this new SD-IV Area was introduced, however, its LCR was less than that of the traditional San Diego local capacity area so RA obligations continued to be based on the SD Area. Since local SD Area generation resources can also satisfy SD-IV Area local capacity requirements, the establishment of this new Area had no impact on local RA capacity procurement that first year.

However, leading up to the 2013 LCT Study two other critical factors emerged:

- The WECC⁵ 1,000 MW SRPL path rating limitation was eliminated
- Certain WECC regional reliability criteria changed

These factors combined to significantly impact RA capacity procurement for 2013. For the first time, the new SD-IV Area LCR exceeded that of the traditional SD Area. Significantly, this resulted in (i) the San Diego local capacity area being deemed a sub-area (“SD Sub-Area”), albeit a sub-area that contains all of SDG&E’s load, and (ii) SDG&E’s 2013 RA obligation now being based on the SD-IV Area LCR. It is important to note that per CAISO’s 2013 LCT Study, not all SD-IV Area generation resources (e.g., those interconnecting at the Imperial Valley Substation) satisfy SD Sub-Area local capacity requirements.

⁴ D.12-06-025 under R.11-10-023, “*Decision Adopting Local Procurement Obligations For 2013 and Further Refining The Resource Adequacy Program*” dated June 21, 2012 (“2013 RA Decision”)

⁵ Western Electricity Coordinating Council

3. **CAISO CAPACITY PROCUREMENT TO ACHIEVE RELIABILITY CRITERIA:** The CAISO is under statutory and contractual obligation⁶ to ensure efficient use and reliable operation of the transmission grid by complying with a body of planning standards & reliability criteria set forth by NERC⁷, WECC, and the Participating Transmission Owners. The CAISO FERC⁸-approved tariff further gives it the authority to (i) establish additional reliability requirements⁹, and (ii) engage in reliability procurement of LCA capacity resources to maintain the integrity of the interconnected transmission grid under both steady-state and contingency conditions.¹⁰

Operationally, according to the CAISO *Business Practice Manual* (“BPM”)¹¹, within a local capacity area CAISO reliability procurement occurs in two basic circumstances:

- a) Individual LSEs are short of their assigned LCR, and/or
- b) Despite all LSEs having met their assigned LCR so that sufficient MW are available, the LCA portfolio overall may fail to comply with reliability criteria because particular units needed to resolve specific contingencies were not procured by the LSEs. In such cases, the CAISO would rely on the Capacity Procurement Mechanism (“CPM”) provisions in its Tariff for authority to engage in backstop procurement and the allocation of those procurement costs to ratepayers of the LSEs.

Avoidance of this second circumstance of CAISO reliability capacity procurement is one example of why the annual technical analysis also provides LCA sub-area information (see Section D.1.d above). The implication for SDG&E is that there may be circumstances where some procurement strategies may be more efficient than others at optimizing ratepayer costs.

With regard to CAISO engaging in backstop capacity procurement for reliability reasons, aside from the obligations, authority, and business practices cited above, CAISO has made it clear in public forums that it intends to implement such ability should the need arise. Below are a few examples:

- **Backstop at the Category-C Level:** “The CAISO applies Option 2 [Category C] for its purposes of identifying necessary local capacity needs and the corresponding potential scope of its backstop authority.”¹²
- **Backstop at the LCA Sub-Area Level:** “Setting an artificially low sub-area local capacity requirements may result in the ISO having to use its back stop authority to procure the additional resource adequacy capacity needed. This backstop procurement through the ISO’s capacity procurement mechanism may result in higher costs to ratepayers.”¹³

⁶ CAISO’s *Final Manual–2013 Local Capacity Area Technical Study*, January 2012, p. 3

⁷ North American Electric Reliability Council

⁸ Federal Energy Regulatory Commission

⁹ *CAISO Tariff*- reliability requirements generally (sec. 40)

¹⁰ *Ibid*, - procurement generally (sec. 40.3), - RMR contracts (sec. 41), - Other contracts (sec. 42), - CPM (sec. 43)

¹¹ CAISO BPM, sec 7.2.3

¹² 2013 LCT Study, p. 15; “*Option 2 is the local capacity level that the CAISO requires to reliably operate the grid per NERC, WECC, and CAISO standards.*” It is based on the NERC Reliability Standard Category-C (double contingency) and results in a higher LCR level than Category=B (single contingency).

¹³ CAISO 2013 LCT Study Reply-Comments to the CPUC in R.11-10-023, p. 3

4. **SDG&E's 2013 NET RA POSITION:** Following the publishing of CAISO's 2013 LCT Study in late April 2012, the CPUC issued its 2013 RA Decision in late June, which will be followed-up in mid-September with the Commission releasing the Final 2013 RA Obligations for LSEs.

For the 2013 RA compliance year, SDG&E's current estimate, based on the 2013 LCT Study, of the total grid LCR requirement for the SD-IV Area is 2,938 MW. SDG&E's share of this is dependent on the amount allocated to the direct access Electric Service Providers in its service territory.

Consistent with the 2013 RA Decision, SDG&E's RA Obligations from the CPUC for 2013 are anticipated to be based on the LCR for the SD-IV Area, thus requiring that additional SD-IV Area RA capacity be added to SDG&E's 2013 RA portfolio. However, even if SDG&E contracts for its full portion of the SD-IV Area LCR, if it does not contract with the Encina facility there remains a high probability that the CAISO will exercise its backstop procurement authority to procure from Encina, at a significantly increased cost to San Diego ratepayers who will, in effect, be double paying for RA.

For the San Diego region, the sub-areas are small isolated load pockets where the available generation in the sub-areas is often times procured to satisfy the larger LCA requirements thus at the same time satisfying the sub-area requirements. However, in the current situation RA capacity procured from resources within the SD-IV Area does not necessarily satisfy the SD-Sub-Area requirement. The reverse, however, is true that RA capacity procured in the SD Sub-Area will simultaneously satisfy the SD-IV Area.

Therefore, SDG&E proposed to optimize its procurement and minimize ratepayer costs by procuring the Encina facility to satisfy its SD-IV Area requirement and avoid the more expensive backstop procurement that the CAISO would likely undertake. The Independent Evaluator Report has indicated that execution of this Confirmation is a reasonable decision in meeting 2013 RA requirements.

5. **LOOKING AHEAD:** The unique situation faced by SDG&E in 2013 may be eliminated in 2014 if the CAISO allows the System Protection Scheme to manage certain contingencies. The CAISO has not yet made a determination as to whether this will happen, or if it does, on what timeframe. SDG&E is engaged in discussions with the CAISO on this matter.

E. PROCUREMENT REVIEW GROUP (PRG) INVOLVEMENT

Since March 2012, when the first draft of the 2013 LCT Study was issued, SDG&E has been discussing with its PRG its concerns regarding the emerging 2013 RA complexities and obtaining its feedback. The topic was presented to the PRG at each meeting between March and July, with each month's discussion narrowing in on potential solutions to the challenges associated with 2013 resource adequacy in the San Diego Local Capacity Area.

After discussions with the PRG, there appears to be a general consensus among the PRG members that the transaction proposed herein is in the best interest of SDG&E's ratepayers.

F. INDEPENDENT EVALUATOR REPORT

SDG&E engaged the services of an Independent Evaluator to (i) review and confirm the implications of the 2013 LCT Study as it relates to resource adequacy in the San Diego market, (ii) monitor the bilateral negotiations, (iii) report on the fairness of the negotiations and the final RA agreement with NRG for Encina's RA capacity during 2013, and (iv) render an opinion on the reasonableness of the chosen solution for meeting 2013 resource adequacy requirements and make a recommendation regarding moving forward with the Confirmation.

Merrimack Energy Group, Inc., of Portsmouth, New Hampshire, was engaged as the Independent Evaluator. Wayne J. Oliver and Ed Selgrade served as the firm's principals for this engagement. Their report, entitled "*San Diego Gas & Electric Company Submission of a Bilateral Transaction with NRG Power Marketing LLC for the Encina Units*," dated July 31, 2012, regarding the above listed topics is attached as Confidential Attachment C to this Advice Letter. Two versions of this report have been prepared: (i) a public version in which certain market sensitive information has been redacted; and (ii) a confidential version in which the full details of the negotiations are provided.

G. EFFECTIVE DATE

The SDG&E-NRG Encina RA Confirmation is conditioned on the receipt of timely Commission approval with such approval not including any conditions or requirements that are not acceptable to either party.

Pursuant to the direction provided by Commission staff, SDG&E submits this Advice Letter filing as a Tier 2 Advice Letter, subject to Energy Division disposition. SDG&E respectfully requests this filing be approved no later than **August 15, 2012**. This date is critical to SDG&E's ability to cost-effectively meet known and anticipated grid reliability needs during 2013. In order to make a timely submittal of its annual resource adequacy compliance demonstration for 2013 by October 31, 2012, Commission approval must be obtained by no later than August 15, 2012.

H. PROTEST

Anyone may protest this Advice Letter to the Commission. The protest must state the grounds upon which it is based, including such grounds as financial and service impact. **SDG&E requests a shortened protest period, with protests due no later than August 10, 2012. SDG&E also proposes a shortened protest reply period, with replies due on August 13, 2012.** Any protest must be made in writing and must be received by August 10, 2012, ten days from the date of filing of this Advice Letter. There is no restriction on who may file a protest. The address for mailing or delivering a protest to the Commission is:

CPUC Energy Division
Attention: Tariff Unit
505 Van Ness Avenue
San Francisco, CA 94102

Copies of the protest should also be sent via e-mail to EDTariffUnit@cpuc.ca.gov. A copy of the protest should also be sent via both e-mail and facsimile to the address shown below on the same date it is mailed or delivered to the Commission.

Attn: Megan Caulson
Regulatory Tariff Manager
8330 Century Park Court, Room 32C
San Diego, CA 92123-1548
Facsimile No. (858) 654-1879
E-Mail: mcaulson@semprautilities.com

I. NOTICE

A copy of this filing has been served on the utilities and interested parties shown on the attached list including parties in R.12-03-014 R.11-10-023 by either providing them a copy electronically or by mailing them a copy hereof, properly stamped and addressed.

Address changes should be directed to SDG&E Tariffs by facsimile at (858) 654-1879 or by e-mail at SDG&ETariffs@semprautilities.com.

CLAY FABER
Director - Regulatory Affairs

(cc list enclosed)

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. **SAN DIEGO GAS & ELECTRIC (U 902)**

Utility type:

ELC GAS
 PLC HEAT WATER

Contact Person: Joff Morales

Phone #: (858) 650-4098

E-mail: jmorales@semprautilities.com

EXPLANATION OF UTILITY TYPE

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

(Date Filed/ Received Stamp by CPUC)

Advice Letter (AL) #: 2390-E

Subject of AL: Request for Approval of Resource Adequacy Contract with NRG Power Marketing LLC
For the Encina Power Station

Keywords (choose from CPUC listing): Procurement, Renewables, Supplemental

AL filing type: Monthly Quarterly Annual One-Time Other

If AL filed in compliance with a Commission order, indicate relevant Decision/Resolution #:

Does AL replace a withdrawn or rejected AL? If so, identify the prior AL: None

Summarize differences between the AL and the prior withdrawn or rejected AL¹: N/A

Does AL request confidential treatment? If so, provide explanation: See attached

Resolution Required? Yes No

Tier Designation: 1 2 3

Requested effective date: 8/15/2012

No. of tariff sheets: 0

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: None

Service affected and changes proposed¹: None

Pending advice letters that revise the same tariff sheets: None

Protests 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
Attention: Tariff Unit
505 Van Ness Ave.,
San Francisco, CA 94102
EDTariffUnit@cpuc.ca.gov

San Diego Gas & Electric
Attention: Megan Caulson
8330 Century Park Ct, Room 32C
San Diego, CA 92123
mcaulson@semprautilities.com

¹ Discuss in AL if more space is needed.

General Order No. 96-B
ADVICE LETTER FILING MAILING LIST

cc: (w/enclosures)

Public Utilities Commission

DRA

Y. Schmidt
W. Scott

Energy Division

P. Clanon
S. Gallagher
H. Gatchalian
D. Lafrenz
M. Salinas

CA. Energy Commission

F. DeLeon
R. Tavares

Alcantar & Kahl LLP

K. Harteloo

American Energy Institute

C. King

APS Energy Services

J. Schenk

BP Energy Company

J. Zaiontz

Barkovich & Yap, Inc.

B. Barkovich

Bartle Wells Associates

R. Schmidt

Braun & Blaising, P.C.

S. Blaising

California Energy Markets

S. O'Donnell
C. Sweet

California Farm Bureau Federation

K. Mills

California Wind Energy

N. Rader

CCSE

S. Freedman
J. Porter

Children's Hospital & Health Center

T. Jacoby

City of Chula Vista

M. Meacham
E. Hull

City of Poway

R. Willcox

City of San Diego

J. Cervantes
G. Lonergan
M. Valerio

Commerce Energy Group

V. Gan

Constellation New Energy

W. Chen

CP Kelco

A. Friedl

Davis Wright Tremaine, LLP

E. O'Neill
J. Pau

Dept. of General Services

H. Nanjo
M. Clark

Douglass & Liddell

D. Douglass
D. Liddell
G. Klatt

Duke Energy North America

M. Gillette

Dynegy, Inc.

J. Paul

Ellison Schneider & Harris LLP

E. Janssen

Energy Policy Initiatives Center (USD)

S. Anders

Energy Price Solutions

A. Scott

Energy Strategies, Inc.

K. Campbell
M. Scanlan

Goodin, MacBride, Squeri, Ritchie & Day

B. Cragg
J. Heather Patrick

J. Squeri

Goodrich Aerostructures Group

M. Harrington

Hanna and Morton LLP

N. Pedersen

Itsa-North America

L. Belew

J.B.S. Energy

J. Nahigian

Luce, Forward, Hamilton & Scripps LLP

J. Leslie

Manatt, Phelps & Phillips LLP

D. Huard
R. Keen

Matthew V. Brady & Associates

M. Brady

Modesto Irrigation District

C. Mayer

Morrison & Foerster LLP

P. Hanschen

MRW & Associates

D. Richardson

OnGrid Solar

Andy Black

Pacific Gas & Electric Co.

J. Clark
M. Huffman
S. Lawrie
E. Lucha

Pacific Utility Audit, Inc.

E. Kelly

R. W. Beck, Inc.

C. Elder

School Project for Utility Rate
Reduction

M. Rochman

Shute, Mihaly & Weinberger LLP

O. Armi

Solar Turbines

F. Chiang

Sutherland Asbill & Brennan LLP

K. McCrea

Southern California Edison Co.

M. Alexander

K. Cini

K. Gansecki

H. Romero

TransCanada

R. Hunter

D. White

TURN

M. Florio
M. Hawiger

UCAN

M. Shames

U.S. Dept. of the Navy

K. Davoodi

N. Furuta

L. DeLacruz

Utility Specialists, Southwest, Inc.

D. Koser

Western Manufactured Housing
Communities Association

S. Dey

White & Case LLP

L. Cottle

Interested Parties

R.11-10-023

R.12-03-014

San Diego Gas & Electric Advice Letter 2390-E
July 31, 2012

**CONFIDENTIAL
ATTACHMENT A**

San Diego Gas & Electric Advice Letter 2390-E
July 31, 2012

**CONFIDENTIAL
ATTACHMENT B**

San Diego Gas & Electric Advice Letter 2390-E
July 31, 2012

ATTACHMENT C

San Diego Gas & Electric Company
Submission of a Bilateral Transaction with NRG Power
Marketing LLC for the Encina Units

Report of the
Independent Evaluator

July 31, 2012

Prepared by
Merrimack Energy Group, Inc.



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I. Introduction

A. Overview

On July 31, 2012 San Diego Gas & Electric Company (“SDG&E”) submitted a Tier 2 Advice Letter to the California Public Utilities Commission (“CPUC”) seeking approval of a Confirmation for Resource Adequacy Capacity Product for CAISO Resources with NRG Power Marketing LLC (“NRG”) for [REDACTED] of Resource Adequacy (“RA”) from the Encina Units for a term of one year beginning on January 1, 2013. The contract is designed to meet a portion of SDG&E’s Local Capacity Requirements in the San Diego - Imperial Valley (IV) area. In addition, the contract for the Encina Units can also meet the capacity requirements in the San Diego- Sub Area. Under the Agreement, SDG&E shall receive and purchase the RA Attributes and Local RA Attributes from the Units. The contract is for [REDACTED]

SDG&E is submitting this contract for fast-track Commission approval using a Tier 2 advice letter.

Pursuant to regulatory requirements of the CPUC, SDG&E retained Merrimack Energy Group, Inc. (“Merrimack Energy”) as the Independent Evaluator (“IE”) for this bilateral contract filing.

B. Regulatory Requirements for the IE

The requirements for participation by an IE in utility solicitations are outlined in Decisions (“D”).04-12-048 (Findings of Fact 94-95, Ordering Paragraph 28), D.06-05 - 039 (Finding of Fact 20, Conclusion of Law 3, Ordering Paragraph 8) of the CPUC, D.09-06-050 and D.10-07-042.

In D.04-12-048 (December 16, 2004), the CPUC required the use of an IE by investor-owned utilities (IOUs) in resource solicitations where there is an affiliated bidder or bidders, or where the utility proposed to build a project or where a bidder proposed to sell a project or build a project under a turnkey contract that would ultimately be owned by a utility. The CPUC generally endorsed the guidelines issued by the Federal Energy Regulatory Commission (“FERC”) for independent evaluation where an affiliate of the purchaser is a bidder in a competitive solicitation, but stated that the role of the IE would not be to make binding decisions on behalf of the utilities or administer the entire process.¹ Instead, the IE would be consulted by the IOU, along with the Procurement Review Group (“PRG”) on the design, administration, and evaluation aspects of the Request for Proposals (“RFP”). The Decision identifies the technical expertise and experience of the IE with regard to industry contracts, quantitative evaluation methodologies, power market derivatives, and other aspects of power project development. From a process standpoint, the IOU could contract directly with the IE, in consultation with its PRG, but the IE would coordinate with the Energy Division.

¹ Decision 04-12-048 at 129-37. The FERC guidelines are set forth in Ameren Energy Generating Company, 108 FERC ¶ 61,081 (June 29, 2004).

In D.06-05-039 (May 25, 2006), the CPUC required each IOU to employ an IE regarding all RFPs issued pursuant to the RPS, regardless of whether there are any utility -owned or affiliate-owned projects under consideration. In addition, the CPUC directed the IE for each RFP to provide separate reports (a preliminary report with the shortlist and final reports with IOU advice letters to approve contracts) on the entire bid, solicitation, evaluation and selection process, with the reports submitted to the utility, PRG, and CPUC and made available to the public (subject to confidential treatment of protected information). The IE would also make periodic presentations regarding its findings to the utility and the utility's PRG consistent with preserving the independence of the IE by ensuring free and unfettered communication between the IE and the CPUC's Energy Division, and an open, fair, and transparent process that the PRG could confirm.

In D.09-06-050 issued on June 18, 2009 in Rulemaking 08-08-009, Order Instituting Rulemaking to Continue Implementation and Administration of California Renewable Portfolio Standard Program, the CPUC required that bilateral contracts should be reviewed according to the same processes and standards as contracts that come through a solicitation. This includes review by the utility's PRG and its IE, including a report filed by the IE.

In D.10-07-042 issued on July 29, 2010, the Commission reaffirmed the role of the IE and required the Energy Division to revise the IE Template to ensure that the IEs focus on their core responsibility of evaluating whether an IOU conducted a well-designed, fair, and transparent RFO for the purpose of obtaining the lowest market prices for ratepayers, taking into account many factors (e.g. project viability, transmission access, etc.).

This IE report is submitted in conformance with the above requirements and is generally consistent with the requirements outlined in the CPUC's Short Form IE Report Template.

C. Issues Addressed in this Report

This report addresses Merrimack Energy's assessment regarding the following issues associated with the evaluation and execution of the Encina Contract.

1. Review the basis for the requirements for the Encina contract. This review includes a brief assessment of the 2013 Local Capacity Technical Analysis Final Report and Study Results completed by the California Independent System Operator ("CAISO") and issued on April 30, 2012. Merrimack Energy has also reviewed SDG&E's assessment of need and options as identified in the past five Procurement Review Group ("PRG") presentations;²
2. Review and assessment of the analysis and assessment undertaken by SDG&E as the basis for pursuing bilateral contract negotiations with NRG Power Marketing for the Encina units;

² SDG&E provided the sections of the presentations to the PRG for March, April, May, June and July 2012. Merrimack Energy was present at the May 2012 PRG presentation.

3. Overview of the contract negotiation process;
4. Summary and assessment of the RA Confirm with NRG for the Encina units including a review and assessment of the fairness of the negotiations;
5. IE assessment of the reasonableness of the selection process;
6. Recommendations

II. Description of the Role of the IE throughout the Solicitation

In compliance with D.09-06-050 SDG&E requested that Merrimack Energy serve as IE for the Encina contract negotiation on July 24, 2012 . As a result, Merrimack Energy's role as IE began shortly after the formal contract negotiation process was initiated with NRG for the short-term contract.

Merrimack Energy's role during the contract negotiation process included the following:

- Monitored several negotiation sessions between SDG&E and NRG;
- Reviewed several contract turns and discussed contract negotiation issues with SDG&E;
- Reviewed the sections of the presentations to the PRG associated with Local Capacity Requirements and options considered by SDG&E to meet capacity requirements in the San Diego Sub-Area and the San Diego-IV Area;
- Reviewed SDG&E's analysis of their resource position , generation available and options considered and evaluated;
- Reviewed the Final Report and Study Results of the 2013 Local Capacity Technical Analysis, including the study results for the San Diego -Imperial Valley Local Area to assess the reasonableness of SDG&E's analysis and planning assumptions and inputs;
- Participated in several calls with SDG&E personnel to discuss the basis of the analysis contained in the PRG presentations and the supporting information which underlined the basis for the assessment;
- Reviewed and replicated SDG&E's analysis including the assumptions and inputs;

- Reviewed Reports and Decisions prepared by the CAISO and CPUC dealing with replacement requirements for scheduled generation outages, Capacity Procurement Mechanism provisions, and CPUC Decisions regarding RA counting requirements;
- Prepared final IE Report for filing with Tier 2 Advice Letter

III. Background to Resource Decision - 2013 Local Capacity Requirement

SDG&E raised the issue of its 2013 RA capacity position beginning with the March 2012 presentation to the PRG, along with the implications of the addition of the San Diego-IV Area. However, at that time the CAISO’s 2013 Local Capacity Technical Analysis had not been completed and there was still uncertainty associated with the capacity requirements due to the definition of the San Diego-IV area as a new area, with a capacity requirement established. At the March 16, 2012 PRG meeting, SDG&E indicated that its preliminary analysis showed that it was [REDACTED]

[REDACTED]. SDG&E also noted that there were a number of uncertainties which may affect [REDACTED] to fulfill its requirements, the amount of RA required by type, and development of an optimal strategy. These were identified as:

- The timing associated with creation of the San Diego-IV sub-area and the exact limiting factors. SDG&E expected this information to be available from CAISO in the April – May timeframe;
- Definition by the CPUC on whether category “B” or “C” will drive the requirements calculation;
- The uncertainty over [REDACTED].

SDG&E provided some preliminary scenarios for 2013 to fulfill RA requirements and identified two key variables for SDG&E to consider to minimize costs:

- [REDACTED];
- [REDACTED].

At the April 20, 2012 PRG meeting, SDG&E reported the results of the CAISO Study Result for the San Diego-Imperial Valley Local Area which was presented at the Stakeholders meeting on April 12, 2012. SDG&E indicated that it was still attempting to assess and comprehend the study results but used the results to conduct an initial

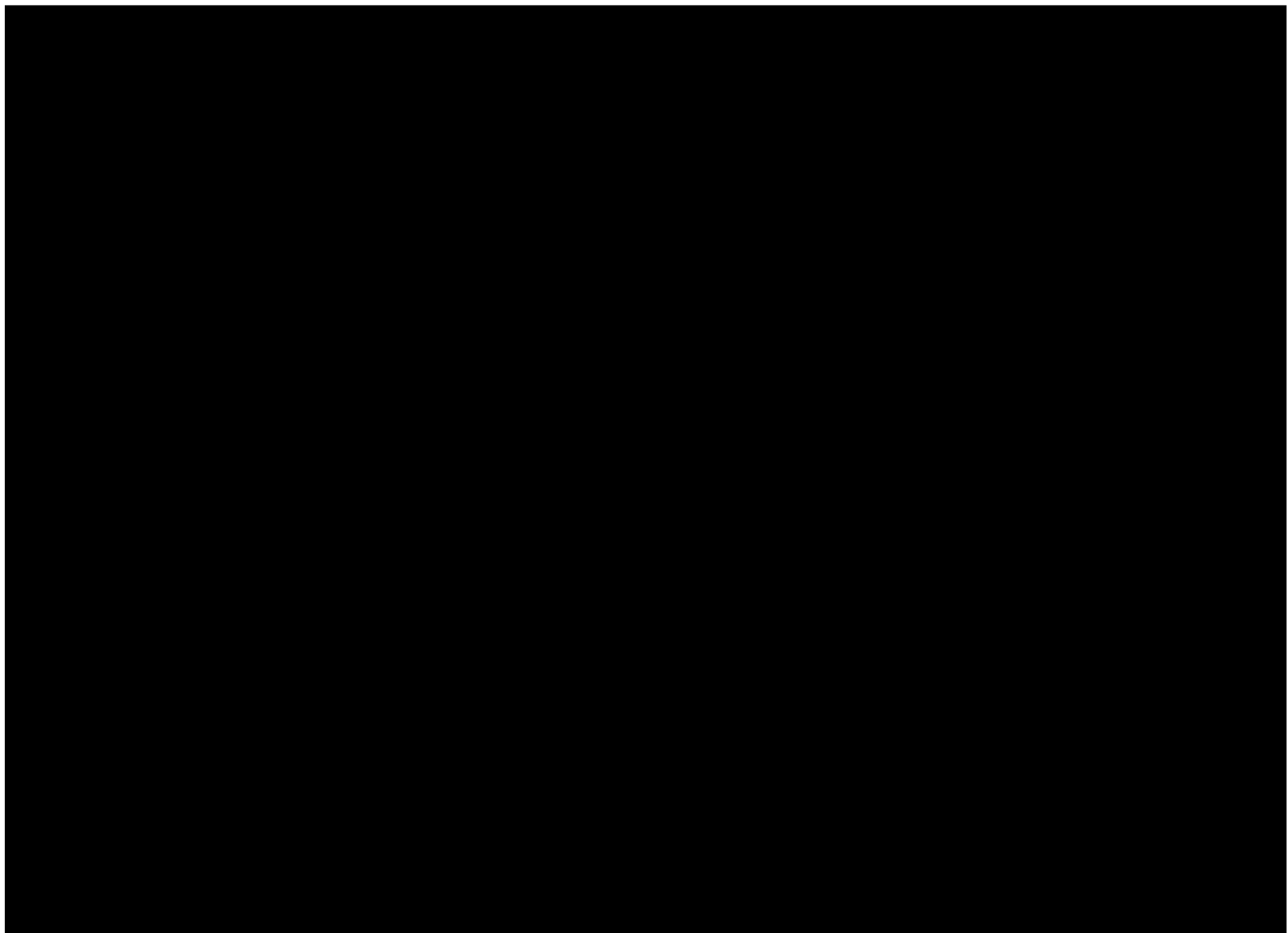
assessment of RA needs. SDG&E informed the PRG that the results of the study illustrated the following:

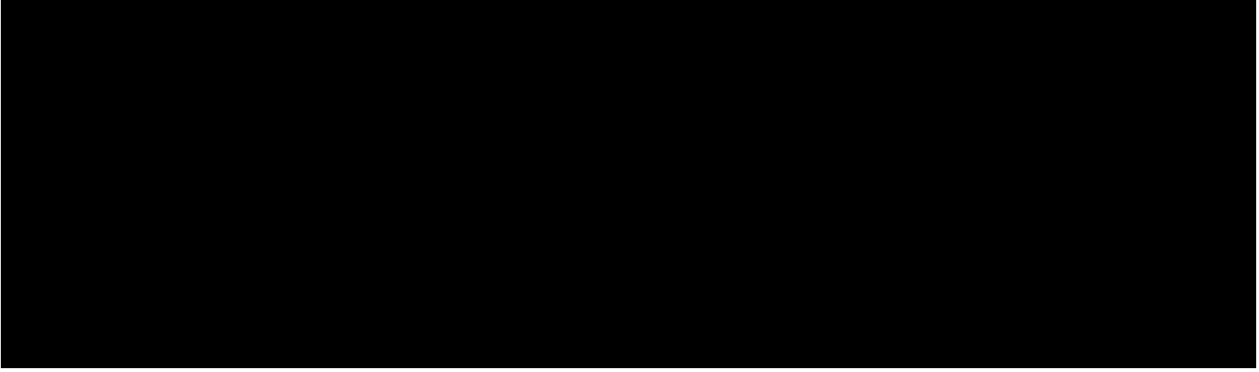
- The 90/10 load forecast was [REDACTED]
- The Category C (N-1 -1) is more constraining than the Category B (N-1/G-1) and its [REDACTED];
- The San Diego – IV area was defined as anticipated and a requirement established;
- [REDACTED]

The study estimated Total Load plus losses for 2013 to be 5,114 MW based on a 90/10 forecast. The study also identified 4,149 MW of total qualifying capacity in the area. Based on its interpretation of the study results and given existing contracted resources, SDG&E estimates [REDACTED].

Exhibit 1 below was prepared by SDG&E and presented to the PRG in April 2012 based on its interpretation of the study results and its existing contracted resources.

Exhibit 1: 2013 LCR Position








On April 30, 2012, the CAISO issued its 2013 Local Capacity Technical Analysis Final Report and Study Results (“LCT”) The objective of the LCT studies is to identify specific areas with in the CAISO Balancing Authority Area that have limited import capability and determine the minimum generation capacity in MW necessary to mitigate the local reliability problems in those areas.

The study confirmed that the San Diego local area has been expanded to include the Imperial Valley substation because the newly formed local area has higher requirements than the San Diego local area alone.

The report also provides the key assumptions for the analysis, the grid reliability and the performance criteria considered and utilized, and provides local capacity requirements study results by local area.

At the May 18, 2012 PRG meeting, SDG&E again provided an update of its 2013 Local Resource Adequacy position. SDG&E provided some of the major conclusions from the 2013 LCR study which was issued on April 30, 2012 by the CAISO and submitted to the CPUC shortly thereafter. These include:

1. The study formally created two requirement areas for San Diego; (a) San Diego-IV (Imperial Valley) area and (b) the San Diego sub-area;
2. The La Rosita plant (487 MW) and TDM (593 MW) satisfy the San Diego-IV area but not the San Diego sub-area. The Encina plant (965 MW), Cabrillo II (188 MW), Larkspur (92 MW), and Wellhead Chula Vista (36 MW) plants are eligible for the San Diego sub-area as well meet the San Diego-IV requirement;
3. The most constraining of the reliability scenarios proposed by CAISO (Category C), if implemented by CPUC would have SDG&E procure incremental San Diego sub-area RA in 2013, assuming Sunrise and SWPL are not online (N-1-1).

SDG&E stated its primary concern is 



[REDACTED]

SDG&E presented some preliminary cases associated with the ratepayer impacts from each procurement option, including cases [REDACTED].

At the June 15, 2012 PRG meeting, SDG&E summarized the results of the CPUC's Proposed Local Procurement Obligation ("LPO") Decision on May 22, 2012 and again raised its concern [REDACTED].

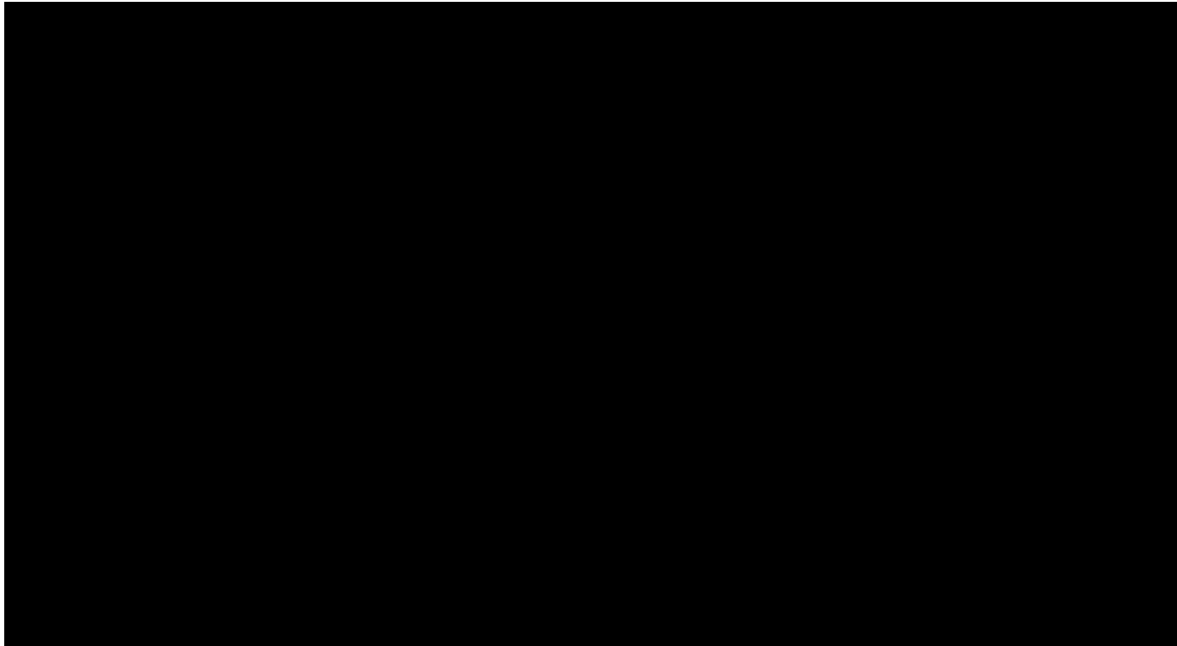
[REDACTED]

SDG&E also presented several cases which [REDACTED].

At the July 20, 2012 PRG meeting, SDG&E presented the results of an analysis of the potential costs of various scenarios associated with the costs of procurement [REDACTED].

[REDACTED]

[REDACTED]



IV. Economic Analysis Supporting Decision

Throughout the presentations to the PRG, SDG&E presented several of the potential ratepayer impacts associated with various procurement options designed to meet load requirements in the two areas. [REDACTED]

[REDACTED] The economics of the various options are dependent on a number of factors including the following:

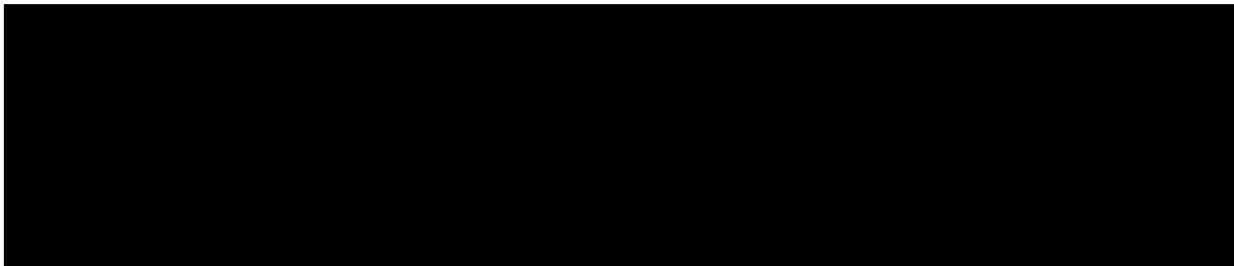
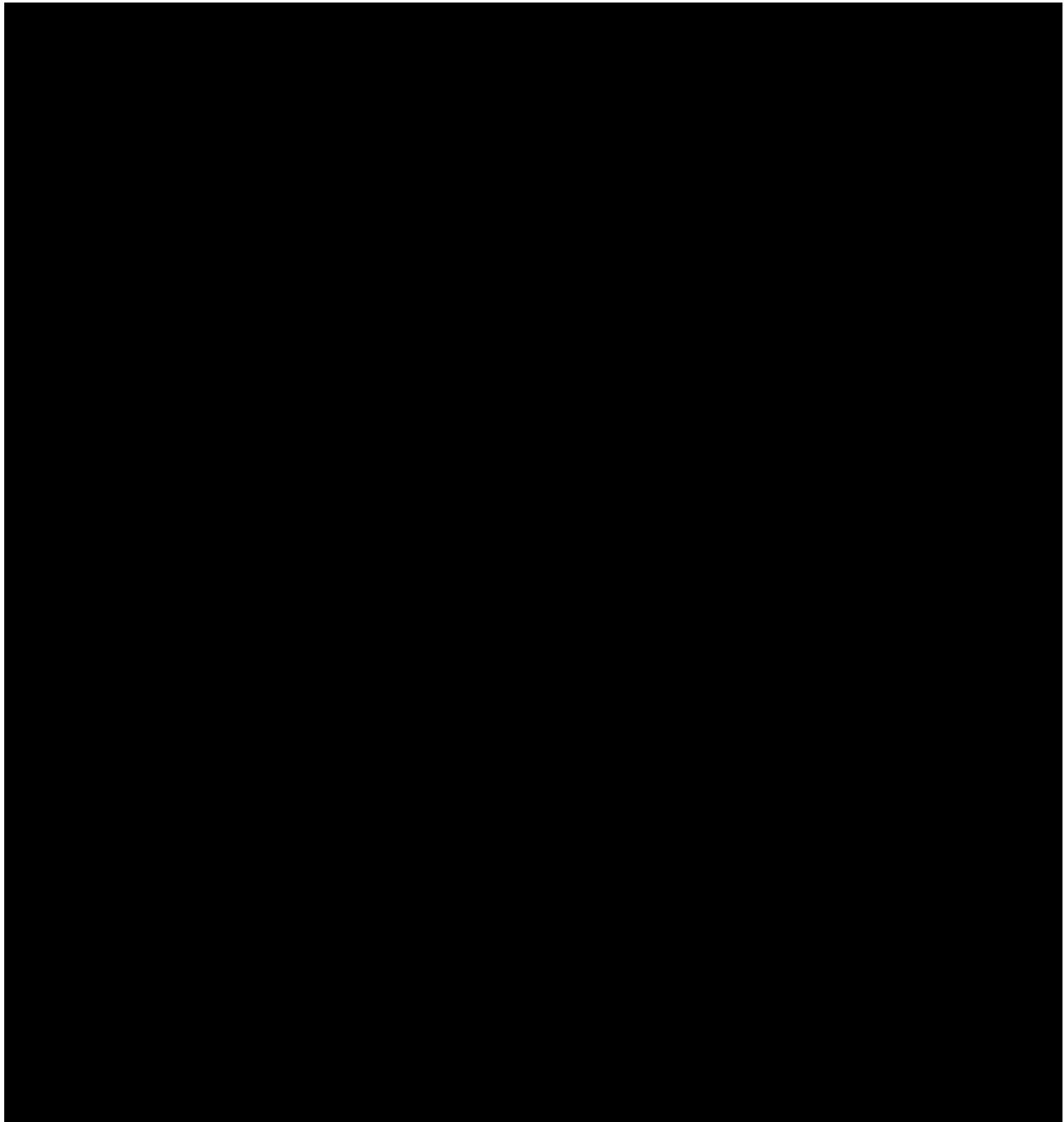


Exhibit 2: Analysis of Ratepayer Costs Under Various Market Scenarios



- _____
- _____
- _____
- _____

[REDACTED]

- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

VI. Contract Negotiations Process

As noted, during the contract negotiation process Merrimack Energy had the opportunity to review several mark-ups of the contract and participated in negotiation sessions between SDG&E and NRG. [REDACTED]

[REDACTED]

Several of the initial discussions between the two parties focused on the implications of the new challenge of the CAISO's yet to be completed (and filed) tariff revisions regarding Replacement Requirements for Scheduled Generation Outages. The parties both felt that they had to come to a general understanding as to what the implications of the new rules might be prior to launching into negotiations of the contract. The parties also discussed the challenges associated with attempting to incorporate, to the best of the counterparties' ability, the expected changes with regard to RA counting and replacement requirements for scheduled generation outages in the contract for RA capacity. Since the CAISO has not yet filed tariff revisions at FERC to implement the new rules and requirements, the counterparties were only able to speculate at this point in crafting contract provisions. [REDACTED]

[REDACTED]

The parties had to discuss the resource's outage schedule or unit availability as both parties were concerned with who had the obligation to provide replacement capacity for an approved maintenance outage. SDG&E initially felt that NRG should provide replacement capacity since the owner controls the operations of the resource. NRG felt that SDG&E should provide replacement capacity because the utility had more RA resources in its portfolio. SDG&E assessed the risk of the Encina outages as part of its own portfolio. SDG&E requested a change in Encina's proposed outage schedule to minimize the risk of replacement, but NRG identified several reasons as to why it did not

⁸ The CPUC Resource Adequacy Replacement rule will no longer be in effect as of January 1, 2013. Accordingly, the CAISO is endeavoring to create rules for replacement that are designed to improve incentives and promote grid reliability.

agree with this request, based on the implications on unit operations. SDG&E agreed with NRG's rationale and decided to drop this issue.

Once negotiations began, SDG&E provided an initial contract draft which was updated from the 2012 RA Confirm. Most of the changes to the contracts after the first draft addressed two issues: (1) how the parties were concentrating on finalizing the Planned Outage dates and the language which allowed for Seller-initiated changes to planned outages after the initial dates were chosen; [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Contract Summary

[REDACTED]

PRINCIPAL TERMS AND CONDITIONS

[REDACTED]

[REDACTED]

[REDACTED]

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[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Overall, the IE found that SDG&E 's team was well prepared for contract negotiations and negotiated aggressively but fairly. There were no outstanding terms or conditions that were of concern to the IE.

VII Safeguards to Compare Affiliate Bids or Utility Owned Generation Options

This section is not applicable since this is a third-party non-affiliate transaction.

VIII. Recommendation For Contract Approval

SDG&E is seeking approval of a Confirmation for Resource Adequacy Capacity Product for CAISO Resources with NRG Power Marketing for [REDACTED] Resource Adequacy from the Encina units for a one year term in 2013 to meet a portion of SDG&E's Local Capacity Requirements. SDG&E has executed this Agreement with NRG for the Encina units at time of uncertainty with regard to CAISO requirements and tariff revisions. SDG&E supports its decision to enter into the Agreement [REDACTED]

[REDACTED]

[REDACTED] As a result, the IE views the decision of SDG&E to execute the Encina contract

based on the provisions contained in the contract to mitigate risk to be a reasonable decision to meet a portion of 2013 RA requirements.

San Diego Gas & Electric Advice Letter 2390-E
July 31, 2012

ATTACHMENT D
CONFIDENTIALITY DECLARATION

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

**DECLARATION OF THOMAS C. SAILE REGARDING CONFIDENTIALITY OF
CERTAIN DATA**

I, Thomas C. Saile, do declare as follows:

1. I am an Energy Contracts Originator for San Diego Gas & Electric Company (“SDG&E”). I have reviewed Advice Letter 2390-E, requesting approval of a Resource Adequacy Confirmation with NRG Power Marketing, LLC for the Encina Power Station (with attached confidential and public appendices), dated July 31, 2012 (“Advice Letter”). I am personally familiar with the facts and representations in this Declaration and, if called upon to testify, I could and would testify to the following based upon my personal knowledge and/or belief.

2. I hereby provide this Declaration in accordance with D.06-06-066, as modified by D.07-05-032, and D.08-04-023, to demonstrate that the confidential information (“Protected Information”) provided in the Advice Letter submitted concurrently herewith, falls within the scope of data protected pursuant to the IOU Matrix attached to D.06-06-066 (the “IOU Matrix”).^{1/} In addition, the Commission has made clear that information must be protected where “it matches a Matrix category exactly or consists of information from which that

^{1/} The Matrix is derived from the statutory protections extended to non-public market sensitive and trade secret information. (See D.06-06-066, *mimeo*, note 1, Ordering Paragraph 1). The Commission is obligated to act in a manner consistent with applicable law. The analysis of protection afforded under the Matrix must always produce a result that is consistent with the relevant underlying statutes; if information is eligible for statutory protection, it must be protected under the Matrix. (See *Southern California Edison Co. v. Public Utilities Comm.* 2000 Cal. App. LEXIS 995, *38-39) Thus, by claiming applicability of the Matrix, SDG&E relies upon and simultaneously claims the protection of Public Utilities Code §§ 454.5(g) and 583, Govt. Code § 6254(k) and General Order 66-C.

information may be easily derived.”^{2/}

3. I address below each of the following five features of Ordering Paragraph 2 in

D.06-06-066:

- That the material constitutes a particular type of data listed in the Matrix,
- The category or categories in the Matrix to which the data corresponds,
- That it is complying with the limitations on confidentiality specified in the Matrix for that type of data,
- That the information is not already public, and
- That the data cannot be aggregated, redacted, summarized, masked or otherwise protected in a way that allows partial disclosure.^{3/}

4. SDG&E’s Protected Information: As directed by the Commission, SDG&E

demonstrates in table form below that the instant confidentiality request satisfies the requirements of D.06-06-066:^{4/}

Data at issue	D.06-06-066 Matrix Requirements	How moving party meets requirements
1. Confidential Attachment A -Substance of negotiations and pricing analysis 2. Confidential Attachment C -Independent Evaluator Report	Demonstrate that the material submitted constitutes a particular type of data listed in the IOU Matrix	The data provided is non-public bid data from SDG&E’s bilateral negotiation evaluation and contract terms
	Identify the Matrix category or categories to which the data corresponds	This information is protected under IOU Matrix category VIII B. and VII.B.
	Affirm that the IOU is complying with the limitations on	In accordance with the limitations on confidentiality set forth

^{2/} See, *Administrative Law Judge’s Ruling on San Diego Gas & Electric Company’s April 3, 2007 Motion to File Data Under Seal*, issued May 4, 2007 in R.06-05-027, p. 2 (emphasis added).

^{3/} D.06-06-066, as amended by D.07-05-032, *mimeo*, p. 81, Ordering Paragraph 2.

^{4/} See, *Administrative Law Judge’s Ruling on San Diego Gas & Electric Company’s Motions to File Data Under Seal*, issued April 30 in R.06-05-027, p. 7, Ordering Paragraph 3 (“In all future filings, SDG&E shall include with any request for confidentiality a table that lists the five D.06-06-066 Matrix requirements, and explains how each item of data meets the matrix”).

Data at issue	D.06-06-066 Matrix Requirements	How moving party meets requirements
	confidentiality specified in the Matrix for that type of data	in the IOU Matrix, SDG&E requests that this information be kept confidential until one year following the expiration of the confirmation.
	Affirm that the information is not already public	SDG&E has not publicly disclosed this information and is not aware that it has been disclosed by any other party.
	Affirm that the data cannot be aggregated, redacted, summarized, masked or otherwise protected in a way that allows partial disclosure.	SDG&E cannot summarize or aggregate the bid data while still providing project-specific details. SDG&E cannot provide redacted or masked versions of these data points while maintaining the format requested by the CPUC.
3. Confidential Attachment B -Confirmation	Demonstrate that the material submitted constitutes a particular type of data listed in the IOU Matrix	The data provided is non-public bid data from SDG&E's contract terms
	Identify the Matrix category or categories to which the data corresponds	This information is protected under IOU Matrix category VII.B.
	Affirm that the IOU is complying with the limitations on confidentiality specified in the Matrix for that type of data	In accordance with the limitations on confidentiality set forth in the IOU Matrix, SDG&E requests that this information be kept confidential until one year following the expiration of the confirmation.

Data at issue	D.06-06-066 Matrix Requirements	How moving party meets requirements
	Affirm that the information is not already public	SDG&E has not publicly disclosed this information and is not aware that it has been disclosed by any other party.
	Affirm that the data cannot be aggregated, redacted, summarized, masked or otherwise protected in a way that allows partial disclosure.	SDG&E cannot summarize or aggregate the bid data while still providing project-specific details. SDG&E cannot provide redacted or masked versions of these data points while maintaining the format requested by the CPUC.

5. As an alternative basis for requesting confidential treatment, SDG&E submits that the Power Purchase Agreement enclosed in the Advice Letter is material, market sensitive, electric procurement-related information protected under §§ 454.5(g) and 583, as well as trade secret information protected under Govt. Code § 6254(k). Disclosure of this information would place SDG&E at an unfair business disadvantage, thus triggering the protection of G.O. 66-C.^{111/}

6. Public Utilities Code § 454.5(g) provides:

The commission shall adopt appropriate procedures to ensure the confidentiality of any market sensitive information submitted in an electrical corporation’s proposed procurement plan or resulting from or related to its approved procurement plan, including, but not limited to, proposed or executed power purchase agreements, data request responses, or consultant reports,

^{111/} This argument is offered in the alternative, not as a supplement to the claim that the data is protected under the IOU Matrix. California law supports the offering of arguments in the alternative. See, *Brandolino v. Lindsay*, 269 Cal. App. 2d 319, 324 (1969) (concluding that a plaintiff may plead inconsistent, mutually exclusive remedies, such as breach of contract and specific performance, in the same complaint); *Tanforan v. Tanforan*, 173 Cal. 270, 274 (1916) (“Since . . . inconsistent causes of action may be pleaded, it is not proper for the judge to force upon the plaintiff an election between those causes which he has a right to plead.”)

or any combination, provided that the Office of Ratepayer Advocates and other consumer groups that are nonmarket participants shall be provided access to this information under confidentiality procedures authorized by the commission.

7. General Order 66-C protects “[r]eports, records and information requested or required by the Commission which, if revealed, would place the regulated company at an unfair business disadvantage.”

8. Under the Public Records Act, Govt. Code § 6254(k), records subject to the privileges established in the Evidence Code are not required to be disclosed.^{5/} Evidence Code § 1060 provides a privilege for trade secrets, which Civil Code § 3426.1 defines, in pertinent part, as information that derives independent economic value from not being generally known to the public or to other persons who could obtain value from its disclosure.

9. Public Utilities Code § 583 establishes a right to confidential treatment of information otherwise protected by law.^{6/}

10. If disclosed, the Protected Information could provide parties, with whom SDG&E is currently negotiating, insight into SDG&E’s procurement needs, which would unfairly undermine SDG&E’s negotiation position and could ultimately result in increased cost to ratepayers. In addition, if developers mistakenly perceive that SDG&E is not committed to assisting their projects, disclosure of the Protected Information could act as a disincentive to developers. Accordingly, pursuant to P.U. Code § 583, SDG&E seeks confidential treatment of this data, which falls within the scope of P.U. Code § 454.5(g), Evidence Code § 1060 and General Order 66-C.

^{5/} See also Govt. Code § 6254.7(d).


^{6/} See, D.06-06-066, *mimeo*, pp. 26-28.

11. Developers' Protected Information: The Protected Information also constitutes confidential trade secret information of the developer listed therein. SDG&E is required pursuant to the terms of its Resource Adequacy Confirmation to protect non-public information. Some of the Protected Information in the Resource Adequacy Confirmation (including confidential attachments) and my supporting declaration, relates directly to commercial aspects of the respective transaction. Disclosure of this extremely sensitive information could harm the counterparty's ability to negotiate necessary contracts and/or could invite interference from competitors.

12. In accordance with its obligations under its Resource Adequacy Confirmation and pursuant to the relevant statutory provisions described herein, SDG&E hereby requests that the Protected Information be protected from public disclosure.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Executed this 31st day of July, 2012, at San Diego, California.


Thomas C. Sille
Energy Contracts Originator
Electric and Fuel Procurement
San Diego Gas & Electric