BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Continue Implementation and Administration of California Renewables Portfolio Standard Program.	Rulemaking 11-05-005 (Filed May 5, 2011)

APPLICATION OF THE INDEPENDENT ENERGY PRODUCERS ASSOCIATION FOR REHEARING OF DECISION 12-11-016

INDEPENDENT ENERGY PRODUCERS ASSOCIATION
Steven Kelly, Policy Director
1215 K Street, Suite 900
Sacramento, CA 95814
Telephone: (916) 448-9499
Facsimile: (916) 448-0182
Email: steven@iepa.com

GOODIN, MACBRIDE, SQUERI, DAY & LAMPREY, LLP
Brian T. Cragg
Suzy Hong
505 Sansome Street, Suite 900
San Francisco, California 94111
Telephone: (415) 392-7900
Facsimile: (415) 398-4321
Email: bcragg@goodinmacbride.com

Attorneys for the Independent Energy Producers Association

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Pursuant to Public Utilities Code Section 1731(b)(1) and Rule 16.1 of the Commission's Rules of Practice and Procedure, the Independent Energy Producers Association (IEP) submits this Application for Rehearing of Decision (D.) 12-11-016 (Decision), issued on November 14, 2012.

The Decision conditionally accepts, with modifications, the 2012 Renewables Portfolio Standard (RPS) Procurement Plans filed by Pacific Gas and Electric Company (PG&E), Southern California Edison Company (SCE), and San Diego Gas & Electric Company (SDG&E). Among other things, the Decision requires the utilities to "incorporate terms into their respective pro forma agreements regarding termination rights and buy-down provisions in the event that the results of any interconnection study or agreement indicate that network upgrade costs will exceed a specific amount agreed to by the seller and the utility."[1] The stated rationale for requiring the pro forma agreements to include this termination right is to avoid

[1] D.12-11-016, p. 33.

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imposing increased costs on ratepayers.[2] The risk of increased interconnection or network upgrade costs, however, is placed entirely on the party with no ability to control those costs—the seller. The Commission's approval of this termination right is not supported by substantial evidence and is a product of arbitrary and capricious decision-making. Furthermore, the Decision is discriminatory. The termination provision applies to eligible renewable projects that participate in the utilities' RPS solicitation while identical projects that participate in the Renewable Auction Mechanism (RAM) program are not subject to this termination risk. Rehearing should be granted and the termination right based on transmission upgrade costs should be rejected.

I. INTRODUCTION

Rule 16.1 states that "[a]pplications for rehearing shall set forth specifically the grounds on which the applicant considers the order or decision of the Commission to be unlawful or erroneous, and must make specific references to the record or law. The purpose of the application for rehearing is to alert the Commission to a legal error, so that the Commission may correct it expeditiously."[3] Several varieties of legal error are listed in Public Utilities Code section 1757,[4] which sets forth the circumstances under which a Commission decision may be reviewed by a court. A Commission decision is subject to review by a court if, among other things, the findings in the decision are not supported by substantial evidence in light of the whole record or the Commission has abused its discretion or has not proceeded in the manner required by law.

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[2] *Id.*
[3] Also see Public Utilities Code section 1732, an "application for rehearing shall set forth specifically the ground or grounds on which the applicant considers the decision or order to be unlawful."
[4] All statutory references herein are to the California Public Utilities Code unless otherwise indicated.

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II. THE DECISION'S ALLOCATION OF THE RISK OF INCREASED NETWORK UPGRADE COSTS IS ARBITRARY AND CAPRICIOUS

The Decision states that the utilities' pro forma power purchase agreements (PPAs) shall include "termination rights and buy-down provisions in the event that the results of any interconnection study or agreement indicate that network upgrade costs will exceed a specific amount agreed to by the seller and the utility." There are several problems with this provision that individually and in combination constitute legal error.

Unnecessary and irrational interference in the parties' agreement. The seller/generator, the Participating Transmission Owner (often the utility purchasing the renewable energy) and the California Independent System Operator (CAISO) agree to allocate the estimated network upgrade costs in a project's interconnection agreement, pursuant to network upgrade cost allocation provisions in CAISO's tariff. The Decision interjects itself into these parties' agreement and arbitrarily assigns all of the risk of increased network upgrade costs to only one of the parties, the seller, without regard to the cost allocation that the parties had previously agreed to.

Irrational assignment of risk. Singling out the seller to bear all of the risk of increased costs of network upgrades may achieve the Decision's short-term goal of shifting the risk of increased costs away from ratepayers, but it is otherwise irrational. Of the three parties involved in interconnection arrangements and network upgrades, the seller is the party with no involvement in the construction of the interconnection or the upgrades and no ability to ensure that the estimated upgrade costs will not be exceeded. Singling out the seller/generator to bear the risk of increased costs is irrational. In addition to the fact that the generator has no control over the costs of network upgrades, the generator faces the prospect of losing its entire investment if excess network upgrade costs result in termination of the PPA. The Decision

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makes no effort to explain why assigning sole responsibility for the costs of network upgrades to the party with the most at stake and the least ability to control costs is a rational outcome.

No limitation on the duration of seller's risk. To make matters worse, the language in the Decision puts absolutely no limits on the duration of the termination right. Pursuant to the language in the Decision, any interconnection study, even an interconnection study completed after construction of a project, could conceivably still result in termination of the project's PPA. This is an absurd result. The open-ended termination right subjects generators to indefinite uncertainty with regard to the costs of network upgrades. The termination provision could lead to the termination of PPAs for projects that are completed or substantially underway, unless the generator exercises the buy-down provision. There is no reason (at least none stated in the Decision) to subject completed projects, or projects that are substantially underway, to an enduring risk of termination based on subsequent unanticipated increases in network upgrade costs.

No remedy for errors or revisions. Moreover, the Decision does not consider the possibility for revisions to an interconnection study that triggered the termination right, even if such revisions were for the purpose of correcting erroneous or faulty study assumptions or contingencies. Thus, if the termination right is triggered by an interconnection study (even one that is later determined to be flawed) and the PPA is terminated, it may not be possible to "un-terminate" the PPA if the study is later revised such that the transmission upgrade costs no longer exceed the cost cap. After losing its PPA due to termination, the project may no longer be in operation and may be beyond resuscitation.[5]

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[5] For example, see PG&E's Final 2012 Renewable Energy Procurement Plan, Attachment 2 (2012 Solicitation Protocol), Attachment H1 (Form of Power Purchase Agreement), section 3.9(d)(i), which states that the termination right is "irrespective of any subsequent amendments of such Interconnection

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The risk of termination will impede financing. In addition, the Decision gives no consideration to how lenders will react to the utility's unbounded termination right. If a PPA can be terminated due to unpredictable events outside of the seller's control, few lenders will be willing to invest in the project. While some developers have access to other sources of financing, most projects will fail if they are unable to get access to conventional financing.

Conclusion on risk allocation. For the reasons stated above, the Commission's determination to allow the transmission upgrade costs termination right to be triggered by <u>any</u> interconnection study that indicates that network upgrade costs will exceed the cost cap is arbitrary and capricious. The Decision subjects generators to indefinite and unreasonable uncertainty with regard to a project's network upgrade costs. At the very least, the termination right should be limited so that it cannot be exercised after the execution of a project's interconnection agreement.

III. THE NETWORK UPGRADE COSTS BUY-DOWN PROVISION IS NOT SUPPORTED BY SUBSTANTIAL EVIDENCE IN LIGHT OF THE WHOLE RECORD

According to termination provision the Decision requires, once a utility exercises its termination right, the generator may avoid termination by buying-down the costs above the cap amount. There are several significant legal and practical problems with this provision.

No consideration of the benefits of network upgrades. The requirement for generators to bear <u>all</u> of the risk of network upgrade costs above the cap amount, either by buying down the excess costs or enduring a termination of the PPA, irrationally assumes that all of the benefits of the excess cost of the network upgrades accrue to sellers. This assumption is in direct conflict with the alignment of benefits and cost responsibility for the investment in the

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Study or GIA or any contingencies or assumptions upon which such Interconnection Study or GIA is based."

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network upgrades below the cap. For the costs of network upgrades below the cap, the Federal Energy Regulatory Commission (FERC) has determined that retail ratepayers' reimbursement to sellers should generally occur over a five-year period for the costs the sellers incur for network upgrades because retail customers are the primary beneficiaries of the network upgrades and an improved or expanded transmission system. The Decision lacks any explanation of why cost responsibility and the benefits of network upgrades swing so suddenly when the agreed-on level of network upgrade costs is reached. Despite the fact that generators have no control over network upgrade costs and that network upgrades benefit the entire system, the Decision puts all the risk and cost of unexpected cost increases on generators. The Decision also fails to acknowledge that the allocation of cost responsibility for network upgrade costs is governed by the CAISO's tariff and FERC.

The Decision's rationale for this requirement is to protect ratepayers by maintaining the value of contracts as they were originally evaluated.[6] IEP certainly understands and agrees with the principle of protecting ratepayers from unwarranted costs. However, the Decision fails to justify why network upgrade costs above the cap amount must automatically be paid for in their entirety by the generator, the party with the least ability to control those costs, regardless of how network upgrade costs are allocated under CAISO's tariff. In its effort to protect ratepayers from cost increases, the Decision fails to recognize that ratepayers are the primary beneficiaries of network upgrades that improve system reliability and increase the supply of cost-effective renewable energy. If the Commission applied the principle that those who benefit should bear the costs, it would have considered allocating at least a portion of any unexpected increased costs in network upgrades to ratepayers. Allocating all of the increased

[6] D.12-11-016, p. 32.

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costs to sellers, while benefiting customers who are not asked to bear any portion of the cost increases, is arbitrary and capricious.

Incentives should be directed to the parties that can control costs and avoid unexpected cost increases. The Decision also fails to acknowledge that excusing PTOs from any responsibility for unexpected cost increases dampens the incentive for PTOs to prevent or control cost overruns, and may be inconsistent with network upgrade cost allocation under CAISO's tariff. Under the Decision's allocation of cost responsibility, PTOs will be highly motivated to avoid cost responsibility by aggressively negotiating for a low network upgrade costs cap. This will shift a greater portion of the risk of cost overruns to generators, who have no control over upgrade costs. Once the low cap amount is exceeded, the PTO has little incentive to keep costs down since any upgrade costs above the cap amount must be paid for by the generator, unless the PPA is terminated. The upgrades paid for by the generator will be owned by the PTO. Under the provision the Decision requires, the PTO has an incentive to "gold-plate" its system since it will reap the rewards of a more reliable system and increased ratebase while avoiding any responsibility for the costs of upgrades.

Thus, the Decision's cost allocation approach may not accomplish its intended purpose of protecting ratepayers from excessive costs. If the PTOs who construct the network upgrades have no incentive to control costs once the cost cap is exceeded, it is unclear how this approach ultimately protects ratepayers. Although ratepayers may be protected from network upgrade costs above the cap amount in the short term, the Decision's approach will ultimately increase the overall costs of renewable generation.

Conclusion on the buy-down option. The Commission's adoption of the network upgrade cost buy-down provision makes generators entirely responsible for network

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upgrade costs above the cap amount. In requiring this provision for the pro forma PPAs, the Commission fails to acknowledge provisions in CAISO's FERC-approved tariff regarding reimbursement for network upgrade costs and fails to acknowledge and address how network upgrades benefit PTOs and ratepayers by improving the system and increasing the supply of cost-effective renewable energy. Furthermore, the Commission fails to acknowledge and address how the buy-down provision will ultimately increase ratepayer costs associated with renewable generation by burdening renewable generators with increased transmission costs that are outside of their control. For these reasons, the Decision commits legal error because it is not supported by substantial evidence in light of the whole record.

IV. IT IS ARBITRARY, CAPRICIOUS, AND DISCRIMINATORY FOR THE COMMISSION TO ADOPT A TRANSMISSION UPGRADE COST TERMINATION RIGHT FOR THE RPS PROGRAM AND NOT THE RAM

On the same day the Commission adopted the Decision, the Commission also adopted Resolution E-4546, making changes to the utilities' RAM program. In Resolution E-4546, the Commission also considered a transmission upgrade costs termination right if network upgrade costs exceeded estimates by the lesser of $100,000 or 25%. The Commission decided not to adopt the termination right for the RAM program due to parties' opposition, which included the contention that the Commission should impose a clear sunset date on a utility's ability to exercise this right.[7]

The RAM resolution was adopted only after the RAM termination clause was deleted from the proposed Resolution, but the Decision includes a similar termination/buy-down provision. The Commission has provided no explanation for why projects that participate in the RPS solicitation face a transmission upgrade cost termination clause, while similarly situated projects in the RAM avoid this risk. This is especially relevant for projects that are 20 MW or

[7] Resolution E-4546, p. 11.

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less, but cannot participate in the RAM because they are not located in one of the utilities' service territories. As a result of these two decisions, the Commission discriminates between similarly situated eligible renewable projects for no reason that is explained in the Decision.

If the purpose of the termination right is to protect ratepayers from transmission upgrade costs in excess of estimated costs, it is unclear why the termination right should apply to PPAs resulting from the utilities' RPS Procurement Plans, but not to PPAs resulting from the utilities' RAM program. The RAM, like the RPS program, involves the utilities' procurement of renewable generation to comply with the RPS. The underlying issue is the same in both contexts—renewable generators should not be subject to indefinite uncertainty regarding their network upgrade costs or to a continuing risk of termination.

The Commission's adoption of a transmission upgrade costs termination right for the RPS Procurement Plans, but not for the RAM, is arbitrary, capricious, and discriminatory. The Commission's rationale that the termination right is necessary for ratepayer protection because it preserves the value of contracts as they were originally evaluated applies equally to both the RPS and the RAM. But the termination right was only adopted for the RPS Procurement Plans. Moreover, because the RPS solicitations are open to renewable generators of all sizes, it would be possible for two identical projects to be treated very differently depending on which program they participated in.

V. THE TERMINATION RIGHT THREATENS ACHIEVEMENT OF THE RENEWABLES PORTFOLIO STANDARD GOALS

Section 399.15 sets compliance obligations for the procurement of renewable generation. Generally, these obligations require retail sellers to procure of 20% retail load from renewable sources by 2013, 25% by 2016 and 33% by 2020. As discussed above, the transmission upgrade costs termination right imposes on generators unknown and unknowable

risks associated with unexpected interconnection cost increases. A likely result of this risk allocation is that developers will delay construction as long as possible until all transmission costs are known (perhaps even until interconnection facilities are fully built), which could result in RPS compliance being delayed. This result is inconsistent with the goals and requirements of the RPS program.

VI. OTHER MEASURES CAN PROTECT RATEPAYERS FROM PAYING EXCESS TRANSMISSION UPGRADE COSTS.

The transmission upgrade costs termination right will adversely affect large-scale renewable generation interconnected at the transmission level by impacting projects' ability to receive financing. To secure financing for projects built in California, a project generally must first obtain a PPA. However, if a PPA is terminable indefinitely (unless the generator bears the risk of buying down unknown network upgrade costs) and for reasons outside of a generator's control, the private capital necessary to construct the resources to meet the RPS goals will flow elsewhere to investments that are perceived to be less risky. This risk placed on renewable generation projects by the termination right is not justified because other measures can protect ratepayers from transmission upgrade cost overruns.

First, under the CAISO's generator interconnection process, a Phase 2 interconnection study is required before the generator, the PTO and the CAISO enter into an interconnection agreement. The interconnection agreement allocates the anticipated cost of network upgrades among the three parties. The Phase 2 study includes the best available information on the cost of reliably interconnecting the generator to the electric grid. Thus, the Commission could reasonably order that the termination provision cannot be exercised after the execution of a project's interconnection agreement.

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Second, the CAISO has gone to great effort to revise the approach to interconnection studies to minimize projects' interconnection costs. Also, the Commission-approved Least-Cost/Best-Fit (LCBF) bid evaluation methodology, which the utilities use to select renewable projects, already considers interconnection and transmission upgrade costs in the selection algorithm. Under the LCBF methodology, the utilities should be selecting projects with the lowest risk of cost overruns for network upgrades.

In light of the significant risk placed on project financing by the inclusion of the termination right in RPS PPAs, and the availability of other measures to protect ratepayers against network upgrade cost overruns, the rationale for the transmission upgrade costs termination right is not supported by substantial evidence in light of the whole record.

VII. CONCLUSION

For all the reasons stated in this application, IEP respectfully requests that the Commission grant this application, rehear this issue, and, upon rehearing, reject the inclusion of the transmission upgrade costs termination right and associated buy-down provision in RPS PPAs.

Respectfully submitted this 14th day of December, 2012, at San Francisco, California.

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GOODIN, MACBRIDE, SQUERI,
DAY & LAMPREY, LLP
Brian T. Cragg
Suzy Hong
505 Sansome Street, Suite 900
San Francisco, California 94111
Telephone: (415) 392-7900
Facsimile: (415) 398-4321
Email: bcragg@goodinmacbride.com

By */s/ Brian T. Cragg*
Brian T. Cragg

Attorneys for the Independent Energy
Producers Association

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VERIFICATION

I am the attorney for the Independent Energy Producers Association (IEP) in this matter. IEP is absent from the City and County of San Francisco, where my office is located, and under Rule 1.11(d) of the Commission's Rules of Practice and Procedure, I am submitting this verification on behalf of IEP for that reason. I have read the attached "Application of the Independent Energy Producers Association for Rehearing of Decision 12-11-016," dated December 14, 2012. I am informed and believe, and on that ground allege, that the matters stated in this document are true.

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

Executed on this 14th day of December, 2012, at San Francisco, California.

/s/ Brian T. Cragg
Brian T. Cragg

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