BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Integrate and Refine Procurement Policies and Consider Long-Term Procurement Plans.	Rulemaking 10-05-006 (Filed May 6, 2010)

OPENING BRIEF OF SAN DIEGO GAS & ELECTRIC COMPANY (U 902 E) REGARDING TRACK I AND TRACK III ISSUES

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I. INTRODUCTION AND BACKGROUND

Pursuant to the August 15, 2011 ruling of Administrative Law Judge ("ALJ") Peter V. Allen and Rule 13.11 of the Rules of Practice and Procedure of the California Public Utilities Commission (the "Commission" or "CPUC"), San Diego Gas & Electric Company ("SDG&E") submits this Opening Brief regarding system plan issues addressed in Track I, as well as certain additional issues addressed in Track III of the above-captioned proceeding.

Prior to commencement of the evidentiary hearing held in August, 2011, several parties to the proceeding, including SDG&E, submitted a Settlement Agreement resolving all Track I issues except: (1) SDG&E's pending request for a need determination for new resources to meet Local Capacity Requirements ("LCR"); and (2) the possibility of need to procure currently uncontracted existing resources.[1/] As discussed below, SDG&E supports the Settlement Agreement and urges the Commission to adopt it.

In addition, SDG&E's requests in Track I that the Commission adopt a LCR need determination of 415 MW for the SDG&E service area. As discussed below, SDG&E's showing of need is based upon updates/corrections to the mandated assumptions included in the *Assigned*

1/ *See* Motion of PG&E, *et al*. for Expedited Suspension of Track 1 Schedule and for Approval of Settlement Agreement ("Motion"), filed August 3, 2011 in R.10-05-006.

Commissioner and Administrative Law Judge's Joint Scoping Memo and Ruling issued December 3, 2010 ("Scoping Memo").

In the *Administrative Law Judge's Ruling Addressing Motion for Reconsideration, Motion Regarding Track I Schedule, and Rules Track III Issues* issued June 13, 2010 ("ALJ Ruling"), the Commission provided direction concerning certain Rules Track III issues to be addressed concurrently with the System Track I schedule. The ALJ Ruling specifically identified five Rules Track III issues and invited parties to make proposals regarding each in testimony to be served concurrently with Track I testimony. The five Rules Track III issues enumerated in the ALJ Ruling are:

1) Procurement of greenhouse gas ("GHG") related products by investor-owned utilities ("IOUs");

2) Procurement rules relating to once-through cooling ("OTC") facilities;

3) Refinements to the bid evaluation process, particularly weighing competing bids between utility-owned generation ("UOG") and power purchase agreements ("PPAs");

4) Refinements to the existing timelines associated with the utilities' request for offers ("RFOs") for resource adequacy ("RA") products; and

5) Procurement oversight rules, including the oversight responsibilities and authority of various entities, including Independent Evaluators ("IEs") and the Procurement Review Group ("PRG"), and standards of conduct ("SOCs") applicable to the IOUs and their employees.[2/]

The ALJ Ruling directed parties to specify whether proposals related to these Rules Track III issues require resolution by the end of this calendar year.[3/] SDG&E addresses these five Rules Track III issues below and notes that that none of these issues require resolution by the end of 2011.

[2/] ALJ Ruling, p. 6.
[3/] *Id*. at pp. 6-7.

II.
SYSTEM TRACK I ISSUES

A. The Commission Should Approve the Settlement Agreement Proposing Resolution of Track I Issues

On August 3, 2011, most of the active parties to this proceeding, including SDG&E (together, the "Settling Parties"), submitted for Commission approval a Settlement Agreement resolving all Track I issues except: (1) SDG&E's pending request for a need determination for new resources to meet its LCR; and (2) the possibility of need to procure currently uncontracted existing resources. As is described in the motion submitting the Settlement Agreement for Commission review, the Settlement Agreement addresses the majority of issues in Track I of the instant proceeding, including the following:

- The Settling Parties agree not to dispute that the IOUs and the California Independent System Operator ("CAISO") have complied with Commission directions in Track 1 with respect to issues resolved by the Settlement Agreement.
- As set forth in substantially more detail in the Settlement Agreement, the Settling Parties recommend that the Commission, in conjunction with the CAISO's ongoing work on this subject, should further expeditiously examine the system resource need and the integration of intermittent renewable resources into the CAISO grid, either in the next Long-Tern Procurement Plan ("LTPP") cycle or in an extension of the current LTPP cycle. There is general agreement that further analysis is needed before any renewable integration resource need determination is made. The Settling Parties recommend that a final Commission assessment of need or a decision should be issued no later than December 31, 2012.
- The Commission does not need to authorize procurement authority relating to LCR for SCE's and PG&E's service areas at this time.

• The Settlement Agreement does not address SDG&E's request for local LCR procurement authority, and each Settling Party remains free to advocate its individual litigation position on this issue.

• The Settlement Agreement does not address the possibility of need to procure currently uncontracted existing resources, and each Settling Party remains free to advocate it individual litigation position on this issue.

• Those Settling Parties who are also parties to the qualifying facility/combined heat and power settlement, adopted by the Commission in D.10-12-035, agree that nothing in the Settlement Agreement qualifies, defers, or relaxes any obligation of any party under that settlement.[4/]

As the Settling Parties demonstrate in the Motion, the proposed Settlement Agreement is in the public interest and represents a fair and equitable resolution of the Track I issues covered in the Settlement Agreement. First, the Settlement Agreement is reasonable in light of the whole record.[5/] Second, the Settlement Agreement is fully consistent with the law and existing Commission precedent.[6/] Finally, approval of the Settlement Agreement is in the public interest.[7/] The Settling Parties complied with the procedural requirements set forth in Rule 12.1.[8/] Accordingly, the Commission should approve the Settlement Agreement without change.[9/]

4/ Motion, pp. 4-5.

5/ *Id*. at pp. 5-6.

6/ *Id*. at p. 6.

7/ *Id*. at pp. 6-7.

8/ *Id*. at p. 7.

9/ During the Track I/Track III evidentiary hearing, ALJ Allen observed, "[i]f the settlement is rejected, I'm going to have to come up with some sort of additional process." Tr. Vol. 3, p. 160. In the event the Commission elects not to adopt the Settlement Agreement, SDG&E reserves the right to participate in the additional process established to resolve Track I issues covered by the Settlement Agreement.

B. The Commission Should Approve SDG&E's Request for an LCR Need Determination of 415 MW

(i) <u>Summary of SDG&E's LCR Need Request</u>

SDG&E requests that the Commission adopt a LCR need determination of 415 MW for the SDG&E service area. SDG&E's showing of need is based upon updates/corrections to the mandated assumptions related to the need analysis included in the Scoping Memo, as discussed below.

(ii) <u>Overview of LCR Requirement</u>

In D.06-06-064, the Commission established a local procurement obligation as a component of the broader resource adequacy requirements ("RAR") program applicable to Commission-jurisdictional electric load-serving entities ("LSEs").[10/] The decision explains the distinction between "local" RAR and "system" RAR as follows:

> Under System RAR, each LSE is required to procure the capacity resources including reserves needed to serve its aggregate system load but is not required to account for local transmission constraints that could prevent the procured capacity from being available to the CAISO to serve load where the LSE's retail customers are located. <u>*Thus, under the current program, LSEs could be resource-adequate on an aggregate or system basis but transmission-constrained local load pockets could still be resource-deficient*</u>. It is this problem that Local RAR is intended to resolve.[11/]

Thus, even if system-wide studies do not identify a need for additional resources on a statewide basis, there may nevertheless still be a need for new resources to meet <u>local</u> resource adequacy criteria. The decision explains that "[l]ocal load pockets are defined by physical transmission constraints. If the transfer capability into a load pocket is less than the load demand within the area, then, depending on reliability criteria, additional generation capacity within the load pocket will be needed to satisfy the load demand. This amount of generation capacity is the

[10/] D.06-06-064, *mimeo*, p. 2.

[11/] *Id*. at p. 5 (emphasis added).

LCR or Local Capacity Requirement."[12] The decision requires that LCRs be allocated to individual Commission-jurisdictional LSEs pursuant to a Commission-approved allocation methodology, and provides that such LSEs are subject to penalties for failure to meet local procurement obligations.[13]

SDG&E's service area has been treated as a single load pocket since the creation of the CAISO.[14] Accordingly, the CAISO determines on an annual basis if there are sufficient resources in the load pocket to meet grid reliability criteria, referred to as the G-1, N-1 criteria. These criteria require that SDG&E be capable of serving the entire load in its service area on a hot summer day – which is defined as a summer day that is expected once every ten years – while the largest transmission line and the largest generator are both out of service.[15] These criteria have been endorsed by the Commission, which has used them to set the LCR in its resource adequacy program.[16] The Commission also applied these criteria in determining the authorization for new resources approved in the 2006 LTPP proceeding.[17]

In terms of meeting the LCR procurement obligation, the Commission has made clear that it does not support "just in time" capacity procurement, and that planning for and procuring new resources must occur well in advance of the need for the resources. In D.07-12-052, for example, the Commission noted that "recent experience suggests that the time required to develop and carry out competitive long-term RFOs, then finance, permit and construct new generation resources – including a cushion to account for unanticipated delays – requires that these procurement decisions be made up to seven years in advance of when the resources are

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[12] *Id*. at pp. 12-13.
[13] *Id*. at pp. 3, 4, 24, 66-69.
[14] SDG&E/Anderson, Exh. 310, p. 2.
[15] *Id*.
[16] *See* R.09-10-032.
[17] *See* D.07-12-052, *mimeo*, p. 113.

needed."[18] Similarly, the Commission emphasized in D.09-01-008 the need to take proactive steps to prevent development of a reliability crisis in which there exists insufficient time to engage in additional procurement:

> We carefully reviewed and considered IEP and WPTF's comments and although we are approving MEF II, we are also admonishing SDG&E to have **adequate procedures in place to ensure that they do not again find themselves in a reliability crisis without sufficient time to follow the procurement protocols set forth in D.07-12-052**.[19]

To address the Commission's clear directive to avoid "just in time" resource additions, need authorizations must be made far enough in advance to allow sufficient time to carry out the Commission's procurement protocols, including the time needed to conduct a second round of procurement, to the extent it is necessary to do so.

(iii) SDG&E's LCR Showing

(a) LCR based upon Scoping Memo assumptions

In the Scoping Memo, the Commission directed the IOUs to consider four "required" scenarios (the "CPUC-Required Scenarios") using an analytic framework developed by the CAISO to prepare a system need determination in Track I.[20] In order to develop this system need determination, the Scoping Memo set forth standardized planning assumptions to be used for the CPUC-Required Scenarios.[21] A table with the loads and resources for SDG&E for the "Trajectory" Case is included in Attachment A to the Scoping Memo (the "Attachment A Table").[22] The table provides no information, however, regarding whether the LCR (as opposed to system capacity requirements) would be met in the SDG&E load pocket.

18/ *Id*. at p. 21.
19/ D.09-01-008, *mimeo*, p. 18 (emphasis added).
20/ Scoping Memo, p. 24.
21/ *Id.* at Attachment A.
22/ *Id.* at Attachment A, p. 19.

In Table 1 included in his Track I direct testimony, SDG&E witness, Robert Anderson, calculates the LCR for the San Diego load pocket based on the Scoping Memo assumptions for the Trajectory Case.[23/] As Mr. Anderson explained, Table 1 includes two components: 1) expected need for resources based on loads and changes to existing resources; and 2) a showing as to whether the assumed additions, including uncommitted energy efficiency ("EE") and demand response ("DR") would be sufficient to meet the LCR.[24/]

Mr. Anderson noted further that while the analysis in Table 1 is intended to reflect the assumptions included in the Attachment A Table, it was necessary to perform certain adjustments to the data in order to properly reflect the local SDG&E service area.[25/] Specifically, the Scoping Memo defined the SDG&E service area as including all resources in the SDG&E load pocket plus all the generation that would be connected to the Imperial Valley substation. This is inconsistent with the CAISO's current definition of the SDG&E local capacity area.[26/] Under CAISO's current definition, resources connected to the Imperial Valley substation and imports delivered to the SDG&E load pocket over the Sunrise Powerlink and the Southwest Powerlink are not located in the load pocket and therefore are not used to meet LCR. Thus to calculate SDG&E's LCR, these resources must be excluded from the supply.

The analysis set forth in Table 1 demonstrates that in the Trajectory Case, a local capacity need of 522 MW in 2017 growing to 722 MW in 2020 is identified after accounting for the retirement of the local OTC facilities. The Trajectory Case meets this need by assuming

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23/ *See* SDG&E/Anderson, Exh. 310, Table 1. Mr. Anderson notes that since most of the assumptions regarding loads and resources that are required in order to calculate the LCR are identical in all of the CPUC-Required Scenarios, SDG&E calculated the LCR only for the Trajectory Case. However, the other cases would produce similar results.

24/ *Id*. at p. 3.

25/ *Id*. at pp. 3-4.

26/ This analysis addresses SDG&E's current Local RA area. The CAISO may also create a new San Diego-Imperial Valley local area after the Sunrise Powerlink transmission line goes into service, which in some years might be more constraining and determine a given years LCR. Any capacity in the current SDG&E Local RA area will count towards meeting requirements for the new, larger area. *Id*. at p. 4, note 6.

substantial amounts of uncommitted EE, growth in DR, new local Renewable Portfolio Standard ("RPS") resources, and allocating a portion of a statewide combined heat and power ("CHP") goal to the SDG&E service area. The addition of these resources results in the Trajectory Case meeting SDG&E's LCR with a margin of approximately 300 MW. However, the Trajectory Case also includes incorrect assumptions regarding existing and future resources. As Mr. Anderson explained, the following two resources are likely not to be realized in the long term:

i. **Cabrillo II Peakers**: In all of the CPUC-Required cases, these peaker facilities are assumed to be in service for the entire planning period. It is anticipated, however, that these units will retire in 2013 when their current land leases expire. This will result in the elimination of 188 MW of supply.

ii. **Celerity Contract**: The Trajectory Case assumes as a "likely addition" 15 MW of new supply from the Celerity contract. This contract has not been able to obtain Resource Adequacy value, and ends in 2016. Thus it is not reasonable to expect that this resource will be available over the planning period.[27/]

With the removal of the 188 MW Cabrillo II peakers and the 15 MW "likely addition" of Celerity, SDG&E's LCR is met by only 112 MW in 2017 growing to about 190 MW in 2020. Thus, the Trajectory Case, as modeled, did meet the LCR; however it did so with substantial assumptions regarding new resources that may not be realized. In addition to relying erroneously on non-existent, or soon to be non-existent, resources, the Trajectory Case relies on Scoping Memo assumptions related to EE, DR, and CHP that produce a load growth forecast that is not realistic and that, if followed, will place reliability and/or the ability to retire once OTC units at risk. Further analysis of these assumptions is provided below.

27/ *Id*. at p. 7.

(b) LCR based upon SDG&E's corrected assumptions

As a supplement to the CPUC-Required Scenarios described above, SDG&E, Pacific Gas and Electric Company ("PG&E") and Southern California Edison Company ("SCE") developed three alternative scenarios (the "IOU Common Scenarios") and a sensitivity analysis using the same input databases used for the four CPUC-Required Scenarios. Certain variables in the input databases were modified to reflect alternative assumptions that align with the IOUs' expectations. The IOUs submitted joint testimony (the "Joint IOU Testimony") that provides modeling analysis and results of the CPUC-Required Scenarios and the IOU Common Scenarios and sensitivity (the "Joint Analysis").

All of the IOU Common Scenarios include new resources necessary to meet SDG&E's LCR for the planning period. The assumption for SDG&E's service area was the same for all three of the IOU Common Scenarios. To determine the LCR need for the IOU Common Scenarios, SDG&E developed assumptions and calculated an LCR table based upon its current outlook regarding loads and resources in its service area.[28/] It included updates to the load forecast, EE, DR, and existing resources, including the retirement of the Cabrillo II units.[29/] SDG&E's analysis uses the same method and calculations used by CAISO to determine the LCR.[30/] Table 2 of Mr. Anderson's Track I direct testimony shows the local capacity need and proposed solutions, as included in the IOU Joint Analysis.[31/] The analysis identifies a need for 573 MW in 2017, growing to 846 MW in 2020. Adding high probability additions adjusted for

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28/ SDG&E/Anderson, Exh. 310, p. 7.
29/ *Id.*; *see also* Joint IOU Testimony, Exh. 106, Ch. 5.
30/ SDG&E/Anderson, Exh. 314, p. 1.
31/ SDG&E/Anderson, Exh. 310, p. 8, Table 2.

contract end dates, uncommitted EE, DR, new CHP and local renewables (discussed below), the case shows a shortage of 41 MW growing to 180 MW in 2020.[32/]

Thus, the Joint Analysis establishes that there will be a substantial need for new resources in the SDG&E LCR area in order to meet key planning criteria. Accordingly, 300 MW of new resources were added to the Joint Analysis to address this shortage and add a reasonable margin.[33/] It is important to note, however, that in addition to the uncertainty reflected in the Joint Analysis surrounding how much of this resource need will be met through demand-side resources such as EE and DR, there also exists a concern regarding underestimation of the load growth rate in the Joint IOU Analysis. This concern is described in the testimony of Mr. Anderson and discussed in more detail below.[34/] Given the high likelihood that the load growth rate will be greater than the level assumed in the Joint Analysis, SDG&E requests that the Commission authorize a LCR need for SDG&E of 415 MW of new generation.[35/]

SDG&E's request for an LCR need determination of 415 MW is based upon updates/corrections to multiple assumptions included in the need determination analysis, including the following:

i. <u>Energy Efficiency ("EE")</u>: Public Utilities Code § 454.5 makes clear that the IOUs' procurement plans should include only those energy efficiency resources ". . . that are *cost*

32/ *Id*. at pp. 7-8.
33/ *Id*. at p. 8.
34/ *See id*. at pp. 9-10.
35/ SDG&E notes that its Application ("A.") 11-05-023, in which SDG&E requests approval of contracts with three new facilities located in the SDG&E load pocket, is currently pending before the Commission. These new facilities would, together, add 450 MW of local RA. If approved, these units would meet the anticipated need for local units in SDG&E's service area reflected in Table 2 and the IOU Joint Analysis. Although the capacity requested in A.11-05-023, is slightly greater the 300 MW shown in this filing, SDG&E believes it prudent to plan for a bit more margin above the minimum requirements, given the load and resource uncertainty discussed herein. Accordingly, the Commission should authorize in the instant LTPP proceeding the need of 415 MW of new generation, which will be met by the approval of A.11-05-023.

effective, reliable and feasible."[36] Thus, EE assumptions must not rely on "stretch" goals, but must instead reflect circumstances that are reasonably expected to occur. Nevertheless, the CPUC-Required Scenarios assume substantial new energy efficiency reductions, including reductions from programs that have not yet been defined or shown to be cost effective. As Mr. Anderson pointed out, a high degree of uncertainty continues to exist regarding whether these reductions will be achieved.[37] He noted that "[w]hile proposing stretch goals and aggressive new measures such as those reflected in the Energy Efficiency Strategic Plan's Big Bold Energy Efficiency Strategies ("BBEES") may be appropriate in certain non-LTPP contexts, the need to preserve system reliability makes it imperative that future uncommitted EE impacts not be overstated for purposes of resource planning."[38] Thus, BBEES are properly excluded from the EE assumption.

In addition, SDG&E adjusted the Scoping Memo's EE assumption to reflect a 70% realization rate and an 80% net to gross ratio. Mr. Anderson noted that this approach is consistent with the way committed energy efficiency was modeled in the California Energy Commission's ("CEC's") adopted 2009 Integrated Energy Policy Report ("IEPR") demand forecast; SDG&E applied the exact same factors that the CEC used to incorporate committed EE into its load models.[39] He explained that failure to make this adjustment would have resulted in double counting of naturally occurring savings that are already embedded in the CEC models, and would not account for the real world effects that evaluation, measurement and verification reports show occur. He noted further that the 70% realization rate is consistent with the EE realization rate used by both the Commission and the CEC:

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[36] Pub. Util. Code § 454.5(b)(9)(C) (emphasis added).
[37] SDG&E/Anderson, Exh. 310, p. 6.
[38] *Id*. at p. 6.
[39] SDG&E/Anderson, Exh. 314, p. 4.

> Q . . . Now, in San Diego's reduced assumptions for energy efficiency savings compared to the CPUC-required assumptions, almost half of San Diego's reduced assumptions is accounted for by reduction of savings from the IOU EE programs; is that right?
>
> A Yes. We did make some adjustments for realization rates, and we made assumptions -- also the CEC in their load forecasting, if you go back and read their discussion, their model, they believe their model already includes the free riders in the net to gross ratio. That their model, in essence, already includes some energy efficiency associated with that. So if you add 100 percent of the EE that the Commission has, you actually double in count in some. So part of this isn't what EE will really be, but what is the right way to adjust the EE when you are adding it to a load forecast.
>
> Q Well, in your calculations you use a projected realization rate of 70 percent for the IOU programs?
>
> A Yes, we did.
>
> Q And did you -- that 70 percent realization rate was based on the CPUC's measurement in evaluation studies of the 2006 to 2008 energy efficiency programs?
>
> A Yeah. Actually, we went back and the CEC was also using a 70 percent realization rate.[40/]

ii. Demand Response ("DR"): Mr. Anderson explained that the Scoping Memo DR assumptions were based on early estimates of the impact of future DR programs. Subsequent Commission filings made by SDG&E have forecasted peak reductions significantly lower than those included in the CPUC- scenarios.[41/]

iii. Combined Heat and Power ("CHP"): The incremental CHP assumption is based on a straight allocation across all the service areas rather than an analysis specific to the SDG&E service area. It also assumes 100% of the demand side capacity will be performing at the time of

40/ SDG&E/Anderson, Tr. Vol. 4, pp. 218-219; *see also* Exh. 314, p. 4.
41/ Joint IOU Testimony, Exh. 106, Ch. 5, p 8; *see also* SDG&E/Anderson, Tr. Vol. 4, pp. 228-230.

peak and the resource adequacy value of the supply side will be 100% of the installed capacity. This is wholly inconsistent with current projects and is not likely to occur with future projects.[42/]

iv. Load Growth Rate: As Mr. Anderson explained, the need shown in this filing is based on conservative demand forecasts. The expected peak load forecast, after EE and demand-side CHP, actually declines by 14 MW in the CPUC-Required Scenarios and increases at 1.1% annual growth for the years between 2011 and 2020 in the IOU Common Scenarios.[43/] The 1.1% growth rate reflected in the IOU Common Scenarios is very low when compared with historical peak load growth. Looking at the average growth rate for the ten-year periods ending in 2000 through 2010, the historical ten-year growth rate has been approximately 2%, or about twice as high as the IOU Common Scenarios forecast.[44/]

Mr. Anderson noted further that there was only one ten-year period – the period ending in 2001 – in which load growth was as low as 1.1% on average.[45/] This unusually low load growth was mainly driven by substantial load decreases due to the energy crisis in 2000 and 2001. Examination of load growth rates over 5-year periods for the periods ending in 2000 through 2010 produces a similar result – the growth rate averages 2%.[46/] It is important to note, however, that load growth does not typically occur in a steady pattern. SDG&E has observed 5-year growth rates as high as 5.5% (for the period ending in 2006).[47/] Given that the Commission expects reliability standards to be met in *every* year, not just on average, and that SDG&E is currently escalating the loads from the low point in an economic cycle, the load growth shown in both cases is very conservative. If load growth returns to historical averages, the need for

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[42/] SDG&E/Anderson, Exh. 310, pp. 6-7.
[43/] Mr. Anderson explained that the load after all demand-side reductions are taken into account is used since this is the best to compare to historical load, which also reflects reductions from the same demand-side resources, and that the load forecasts are also reduced for growth in roof top photovoltaics. SDG&E/Anderson, Exh. 314, p. 9, note 10.
[44/] SDG&E/Anderson, Exh. 310, p. 9.
[45/] *Id.*
[46/] *Id.*
[47/] *Id.* at pp. 9-10.

resources will be increased by over 900 MW in 2020 in the Trajectory Case, and by about 400 MW in the IOU Joint Analysis.[48]

As noted above, the Commission has emphasized that it does not support "just in time" capacity procurement.[49] Commission precedent makes clear that need authorizations must be made far enough in advance to allow sufficient time to carry out the Commission's procurement protocols, including the time needed to conduct a second round of procurement, to the extent it is necessary to do so. Given the long-lead time required to add new resources, it is essential that SDG&E's need for additional local resources be addressed in this LTPP proceeding. This will encourage prudent planning, and will help to protect system reliability – an obligation shared by the Commission and the IOUs – and will facilitate timely shut-down of OTC units in SDG&E's service area. Thus, taking into account future load growth, the uncertainty in the amount of demand-side resources, the lead-time required to add new plants and the State's OTC policy, it is clear that new resources must be added to SDG&E's local area in this LTPP planning cycle.

III.
RULES TRACK III ISSUES

A. The Commission Should Adopt SDG&E's Proposal Regarding Procurement of GHG-Related Products

(i) Overview

In Assembly Bill ("AB") 32, California established a goal of reducing its GHG emissions to 1990 levels by 2020.[50] The legislation designates the California Air Resources Board ("CARB") as the agency charged with developing GHG emission reduction regulations, and directs CARB to coordinate with the Commission and other stakeholders to design and

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[48] *Id*. at p. 10.
[49] *See* D.07-12-052, *mimeo*, p. 21.
[50] Assembly Bill (AB) 32, (Stats. 2006, Ch. 488).

implement California's GHG reduction program.[51/] As part of the "scoping plan" required under AB 32 for achieving the maximum technologically feasible and cost-effective GHG reductions by 2020,[52/] CARB has developed a proposal for a California GHG cap-and-trade program capable of linking with other programs to create a regional market system.[53/]

In October, 2010, CARB released its *Proposed Regulation to Implement the California Cap-and-Trade Program*, which was approved by its Board in December, 2010.[54/] Appendix A of that document contains CARB's Proposed Regulation Order.[55/] The regulations proposed by CARB would create a GHG emissions allowance cap-and-trade system, with compliance obligations in the electricity sector applicable to "first deliverers of electricity" (the "Cap-and-Trade Program"). Generally, "first deliverers of electricity" include (i) electricity generators located within California that emit more than 25,000 metric tons of GHGs; and (ii) importers of electricity from outside of California. The proposed regulations would require that first deliverers of electricity purchase all of the allowances and offsets required to meet their compliance obligations.[56/] The Cap-and-Trade Program was originally scheduled to become effective in January, 2012, but implementation has been delayed. CARB has indicated that it will hold two auctions at some point during 2012, with the first compliance obligation of the Cap-and-Trade Program occurring in 2013.[57/]

51/ *Id*. at §§ 38501, 38510, 38560.
52/ *Id*. at § 38561(a).
53/ CARB Resolution 10-42, p 3.
54/ The regulation has not yet been finalized or submitted to the Office of Administrative Law for approval.
55/ The CARB documents referenced are available at: http://www.arb.ca.gov/regact/2010/capandtrade10/capandtrade10.htm.
56/ This requirement would not apply to publicly-owned utilities.
57/ *See* http://www.arb.ca.gov/cc/capandtrade/capandtrade.htm.

As SDG&E witness, Ryan Miller, explained, implementation of the Cap-and-Trade Program will impose costs on SDG&E's bundled customers. Specifically, SDG&E's bundled customers will be exposed to GHG-related costs for: (i) SDG&E UOG, including the Palomar and El Dorado combined cycle generation facilities and the peaking generation located at the Miramar facility; (ii) imported electricity purchased under existing long-term contracts and spot market purchases; and (iii) contractual obligations for GHG compliance responsibility for certain bilateral contracts.[58/] Accordingly, it will be necessary for SDG&E to procure GHG products in order to comply, on behalf of its bundled customers, with Cap-and-Trade Program requirements, and to manage the price risk to bundled customers associated with such compliance.

SDG&E's GHG product procurement plan ("GPPP") is set forth in detail in the testimony of Mr. Miller.[59/] The GPPP, when approved, will be incorporated into SDG&E's authorized LTPP[60/] and will constitute the "upfront standards and criteria" envisioned in Assembly Bill ("AB") 57 that will guide SDG&E's future procurement of GHG products and determine the eligibility of GHG product procurement costs for rate recovery.[61/] While SDG&E originally requested approval of its GPPP by the end of 2011,[62/] it has revised its requested approval date in light of the above-referenced delay in CARB's implementation of the Cap-and-Trade Program. Specifically, SDG&E now requests approval of its GPPP no later than the first quarter of 2012.[63/]

Approval in early 2012 is necessary in order to ensure that SDG&E is able to participate in the Cap-and-Trade Program as soon as it commences. As discussed above, CARB has indicated that offsets will become available in 2012, and secondary markets have *already* begun

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58/ SDG&E/Miller, Exh. 313, p. 4.
59/ *See* SDG&E/Miller, Exh. 313, pp. 3-17.
60/ SDG&E's draft LTPP was filed for Commission approval on March 25, 2011.
61/ *See* Assembly Bill ("AB") 57, Sec. 2, §§ 454.5(c)(3) and 454.5(d)(2) (Stats. 2002, Ch. 835).
62/ SDG&E/Miller, Exh. 313, p. 4.
63/ SDG&E/Miller, Exh. 315, p. 2.

trading for GHG products.[64] The ability to take advantage of GHG market opportunities that may arise before the compliance obligation of the Cap-and-Trade Program starts in 2013 would benefit SDG&E ratepayers. As Mr. Miller explained, CARB's delay in implementation of the compliance obligation of the Cap-and-Trade program will not cause a material change in SDG&E's proposed GPPP.[65] Thus, there is no need for the Commission to significantly delay approval of SDG&E's GPPP. Likewise, it is not necessary to delay approval of SDG&E's GPPP pending finalization by CARB of Cap-and-Trade and/or other GHG-related regulations. While the regulations ultimately adopted by CARB may impact the *amount* of GHG allowances or offsets SDG&E is required to procure on behalf of its bundled customers, SDG&E does not expect to modify its strategy or methodology for GHG procurement.[66] Accordingly, SDG&E's GPPP should be approved no later than the first quarter of 2012.

(ii) <u>Cost Recovery</u>

Section 454.5 (d)(3) requires the Commission to "[e]nsure timely recovery of prospective procurement costs incurred pursuant to an approved procurement plan." The provision further directs the Commission to establish rates based on forecasts of procurement costs, actual procurement costs incurred, or a combination thereof, and to establish "power procurement balancing accounts to track the differences between recorded revenues and costs incurred pursuant to an approved procurement plan." In accordance with this direction, the Commission established the Energy Resource Recovery Account ("ERRA") balancing account mechanism to track procurement-related revenues against actual recorded costs.[67]

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[64] *Id*. at p. 1.
[65] *Id*. at p. 2.
[66] SDG&E/Miller, Exh. 315, p. 5.
[67] *See*, D.02-10-062; D.02-12-074; D.03-06-067; D.04-01-050.

SDG&E's GPPP provides that "[a]ll cost associated with SDG&E's compliance with GHG requirements will be included and recovered in SDG&E's Energy Resource Recovery Account ("ERRA") in a manner identical to other procurement costs."[68/] It notes further that "[a]s with other procurement-related costs, forecasts of SDG&E's GHG compliance costs will be included in SDG&E's annual ERRA forecast filing with actual compliance cost tracked in comparison to the approved forecast costs on a monthly basis."[69/] As Mr. Miller explained, "[o]nce the cap-and-trade program is implemented, GHG-related procurement obligations will become a variable cost for generating electricity, much like natural gas is now."[70/]

In its Track III testimony, Pacific Environment ("PE") argues that "given the novelty, uncertainty, and complexity of the proposed Cap-and-Trade program, the ratepayers should not bear all of the risks associated with the carbon market."[71/] PE ignores the fact that the Cap-and-Trade Program to be implemented by CARB is a mandatory program adopted in accordance with California's policy in favor of GHG reduction. As such, costs associated with the risks of such program are fairly borne by California ratepayers. Because GHG-related procurement obligations are identical in nature to current Commission-authorized products associated with generating electricity, GHG costs should be fully recoverable in a manner identical to other electricity procurement costs.[72/]

(iii) Ratepayer Protection

SDG&E's GPPP establishes ratepayer protection measures that are identical to those in place for energy procurement. As explained by Mr. Miller, these measures include: (i) consultation with SDG&E's PRG on GHG product procurement issues; (ii) inclusion of GHG

68/ SDG&E/Miller, Exh. 313, p. 5.
69/ *Id*. at pp. 5-6.
70/ SDG&E/Miller, Exh. 315, p. 2; Tr. Vol. 7, p. 807.
71/ Pacific Environment, Exh. 505, p. 36.
72/ SDG&E/Miller, Exh. 315, p. 2.

transactions in SDG&E's Quarterly Compliance Reports ("QCRs"), which are reviewed by the Commission's Energy Division; and (iii) adherence to the principles of least-cost dispatch, which apply for decisions regarding GHG.[73] Mr. Miller further noted that "as part of SDG&E's GHG procurement plan, SDG&E intends to purchase GHG products more or less ratably over time, thereby minimizing the impacts of short-term market swings on prices to effect reasonable overall cost for compliance with GHG requirements."[74] In addition, SDG&E has indicated that it is willing to provide its PRG with information concerning bid curves for the allowance auctions and GHG forward curves in advance of the scheduled auctions.[75]

Notwithstanding the robust ratepayer protection measures included in SDG&E's GPPP, PE asserts that the Commission must strengthen oversight procedures.[76] It proposes, for example, that the utilities should be required to file advice letters for offset transactions. Imposition of this requirement would likely *harm* ratepayers, however, since the resulting delay would cause SDG&E to miss out on opportunities to purchase cost-effective offsets, which would result in increased costs for SDG&E ratepayers.[77] As Mr. Miller explained, "SDG&E expects that ARB cap-and-trade regulations will be designed so that offsets are developed as standard products that can be traded quickly. Requiring the utilities to seek Commission approval for each offset transaction would inject unworkable delay into the process, and would create an unfair competitive advantage for entities not subject to Commission jurisdiction."[78] Accordingly, the Commission should approve the ratepayer protection measures included in SDG&E's proposed GPPP, which balance the need to avoid imposition of excessive costs on

[73] *Id*. at p. 4.
[74] *Id*. at p. 4.
[75] *Id*. at p. 3.
[76] Pacific Environment/Track III, Exh. 505, p. 37.
[77] SDG&E/Miller, Exh. 315, p. 2.
[78] *Id*.

ratepayers with the need to ensure that the IOUs have adequate flexibility to compete effectively in the market for GHG products.

B. The Commission Should Reject the Staff Proposal Concerning Procurement Rules Relating to Once-Through Cooling

In May, 2010, the State Water Resources Control Board (the "SWRCB") adopted its statewide *Water Quality Control Policy on the Use of Coastal and Estuarine Waters for Power Plant Cooling*, which applies to power plants located along the California coast that rely on "once-through cooling" technology (the "OTC Policy").[79/] The OTC Policy implements § 316(b) of the federal Clean Water Act, which seeks to minimize the adverse environmental impacts of cooling water intake structures. In adopting the new regulations, the SWRCB made clear that the OTC Policy is intended, *inter alia*, to protect State's coastal and estuarine waters, "while also ensuring that the electrical power needs essential for the welfare of the citizens of the State are met."[80/] The SWRCB observed further that it "recognizes that it is necessary to develop replacement infrastructure to maintain electric reliability in order to implement this Policy."[81/]

The Commission's Energy Division Staff have developed proposed rules related to IOU contracting with generating facilities subject to the OTC Policy (the "Staff OTC Proposal").[82/] The Staff OTC Proposal would (i) prohibit the IOUs from entering into contracts for longer than one year with any generating facility identified in the OTC Policy; and (ii) prohibit the IOUs from entering into contracts with any OTC facility that requires operation of that facility beyond the compliance date identified in the OTC Policy, except under certain specified

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79/ *See* Resolution No. 2010-0020. The Policy was approved by the Office of Administrative Law on September 27, 2010, and became fully effective on October 1, 2010.
80/ *Id.* at ¶ 10.
81/ *Id.*
82/ Staff's OTC Proposal is attached to the ALJ Ruling as Appendix A.

circumstances.[83] While SDG&E does not oppose the proposal to limit the IOUs' ability to enter into contracts that would require operation of an OTC facility beyond the compliance date identified in the OTC Policy, it strongly objects to the proposal to mandate that IOUs enter only into one-year contracts with OTC facilities.

As SDG&E witness, Mr. Anderson observed, the Staff OTC Proposal is misguided in its focus and fails to address the key concerns related to the OTC Policy.[84] He explained that the uncertainty surrounding the future viability of OTC facilities creates a number of resource planning issues for the IOUs, with the difficulty presented by potential retirement of OTC facilities being particularly evident where such facilities are located in areas with local capacity constraints, such as in the SDG&E service territory.[85] In the event OTC facilities in a local capacity constrained area must shut down, the only option for replacement of the lost capacity is building new facilities. Plainly, procuring new capacity is a time-consuming proposition; in most, if not all, cases, the time required to solicit, approve, and build new generation will exceed the period of time that remains once it is known whether an existing OTC plant can meet new requirements or must be shut down. Thus, the challenge presented by the OTC Policy is one of timing, or as Mr. Anderson explained it, "the need for [the Commission] to issue determinations regarding authorization of new capacity in the absence of perfect information."[86] As a practical matter, failure to approve new capacity to be located in constrained areas in a timely manner will result in OTC facilities being retained beyond the dates in the OTC Policy due to reliability concerns. The Staff OTC Proposal fails, however, to address this fundamental issue, or to address the OTC Policy's impact on reliability.

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[83] ALJ Ruling, Appendix A, p. 1.
[84] *See* SDG&E/Anderson, Exh. 313, pp. 17-19.
[85] *Id*. at p. 17.
[86] *Id*. at pp. 17-18.

As a practical matter, the one-year contracting limitation included in the Staff OTC Proposal would have little effect beyond creating administrative burden for the IOUs. While the Staff OTC Proposal appears to be aimed at ensuring that the IOUs' respective procurement strategies do not rely on OTC facilities beyond the compliance period, until the facilities have shown that they are able to meet the regulation, it is clear, as Mr. Anderson explained, that "reliance on OTC facilities such as those located in SDG&E's service area will not be driven by the length of contract with the existing facilities, but rather by whether new plants have been built so that a procurement option other than contracting with existing OTC facilities exists."[87/] Mr. Anderson noted, for example, that the compliance date for the remaining OTC facility located in SDG&E service area is the end of 2017. He pointed out that "[l]imiting SDG&E's ability to contract with this OTC plant to one-year contracts in 2012, 2013 and so on serves no discernable purpose. It does not lower the costs borne by SDG&E ratepayers; indeed, such a limitation might actually *increase* transaction costs for customers as new agreements will need to be negotiated for each year."[88/]

The concern that the one-year contracting requirement would potentially be detrimental to ratepayers was echoed by the Division of Ratepayer Advocates ("DRA"), which opposes the proposed limitation.[89/] DRA pointed out that "the Staff Proposal unnecessarily restricts the IOUs' options for procuring capacity and adds additional risk to their short-to- mid-term procurement efforts."[90/] It noted further that "since the proposed one-year contracting limitation would apply only to the investor-owned utilities, this policy would not be applied equally to all Load Serving Entities ("LSEs") in California. This puts the IOUs at a competitive

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87/ *Id*. at p. 18.
88/ *Id*. (emphasis added).
89/ DRA, Exh. 405, pp. 19-22.
90/ *Id*. at p. 20.

disadvantage."[91] It explained that "LSEs not affected by this policy could sign lower priced, longer term contracts with OTC units and this, in turn, would give the OTC facility the upper hand in pricing future contracts with the IOUs."[92]

Likewise, SCE points out the ratepayer risk created by the one-year contracting policy. SCE witness, Mr. Buerkle, noted that the one-year contracting policy "does not allow IOUs to hedge a large portion of their customers' capacity needs on a multi-year basis, although they have the authority to do so in their Assembly Bill (AB) 57 bundled procurement plans."[93] He explained that "IOUs are then forced to procure thousands of megawatts of capacity, much of it in critical local reliability areas, under a very tight timeline (to meet year-ahead local RA showings) and without the ability to manage costs over multiple years."[94]

Thus, the focus of the Commission's OTC Policy implementation should be on addressing the need for replacement capacity, rather than on limiting contracts with OTC units to one-year. As Western Power Trading Forum ("WPTF") witness, Mr. Ackerman, noted, "[t]he Staff OTC proposal would lead to inefficient outcomes that would increase costs and jeopardize reliability."[95] Accordingly, the Commission should reject the one-year contracting limitation proposed in the Staff OTC Proposal.

C. The Commission's Approach to Evaluating Competing Bids Between UOG and PPAs does not Require Modification

The Commission has long recognized that UOG and PPA resources both offer benefits to ratepayers, and has established a preference for a hybrid market that includes both UOG and PPAs.[96] In the 2004 LTPP decision, it rejected the notion that UOG and PPAs cannot compete

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[91] *Id.*
[92] *Id.*
[93] SCE/ Buerkle, Exh. 211, p. 9.
[94] *Id.*
[95] WPTF/Ackerman, Exh. 2300, p. 6.
[96] D.04-12-048, *mimeo*, p. 217, Finding of Fact ("FOF") No. 85.

head-to-head, concluding that "PPAs and utility-owned resources need to participate in the same all-source open solicitations to ensure [least-cost, best fit ("LCBF")], not in separate PPA and utility-owned specific solicitations . . ."[97] The Commission was not persuaded by the argument that the IOUs may not conduct an all-source open RFO without a unique UOG/PPA bid evaluation methodology, finding instead that "[t]he IOUs will employ the LCBF methodology when evaluating PPAs and utility-owned bids in an all-source open RFO, taking into account the qualitative and quantitative attributes associated with each bid . . . In addition, when seeking Commission approval for the proposed contracts the IOUs will need to demonstrate that they employed LCBF principles."[98]

The Commission has considered several applications for approval of both UOG and PPAs filed since 2005 and has, as Mr. Anderson noted, "demonstrated that it is fully capable of weighing the entire record presented and applying judgment to render a decision as to what resources are in ratepayers' best interests."[99] Thus, the Commission is currently in possession of the tools necessary to analyze the attributes of proposed UOG and PPAs, and to evaluate the differences between the two. In addition, as Mr. Anderson explained, there are a number of checks on the IOU evaluation process that provide fair evaluation to all bidders. These include:

a. The Commission-adopted SOCs;

b. IE involvement and expertise regarding how to compare UOG and PPA projects; and

c. Full access to the evaluation process by the PRG and Energy Division.[100]

Since the Commission already has the ability to effectively evaluate competing UOG and PPAs bids, additional "refinements" to the bid evaluation process in the form of a strict,

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[97] *Id*. at p. 139.
[98] *Id*. at p. 140.
[99] SDG&E/Anderson, Exh. 313, p. 19.
[100] *Id*. at pp. 19-20.

structured set of rules for comparing UOG and PPAs are not necessary. As Mr. Anderson observed, "[a]ny such rules or mechanisms adopted in this proceeding are unlikely to fit all circumstances or the unique characteristics of all potential projects."[101] The existing evaluation approach, which requires that any hybrid product evaluation employ the LCBF guiding principle with oversight from an IE and PRG to ensure that each project's unique circumstances and attributes are captured, should be maintained.[102]

Despite the clear lack of any compelling evidence to support the claim that the current process requires modification, IEP proposes several revisions to the existing UOG/PPA bid evaluation approach.[103] As Mr. Anderson explained, however, IEP's proposed modifications to the bid evaluation process are contrary to Commission policy, unfairly burden the utilities and are premised on a flawed analysis.[104] IEP proposes, for example, that IOUs be required to provide detailed bid evaluation information to bidders.[105] While IEP suggests that adoption of its information disclosure proposal will result in more bids and lower prices, it admits that past utility solicitations have produced offers that "far exceeded" the capacity needed.[106] As Mr. Anderson pointed out, "if the utilities are receiving bids that exceed the need by up to ten times, increasing the response so that the utilities receive bids that exceed the need by eleven times, or more, will not have much impact on pricing."[107]

IEP proposes that if production cost models are used by the IOUs to evaluate bids, the modeling assumptions should be provided to prospective bidders.[108] However, the utility models often include data concerning existing contracts, which is protected under the

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[101] *Id*. at p. 20.
[102] D.04-12-048, *mimeo*, pp. 217-218, FOF No. 86, 93, 95.
[103] *See* IEP/Monsen, Exh. 2000, pp. 3-48.
[104] SDG&E/Anderson, Exh. 315, pp. 6-10.
[105] *See* IEP/Monsen, Exh. 2000, pp. 8-15.
[106] *Id*. at p. 10.
[107] SDG&E/Anderson, Exh. 315, pp. 6-7.
[108] IEP/Monsen, Exh. 2000, p. 15.

Commission's confidentiality rules.[109] Moreover, development of modeling assumptions used for production cost modeling involves analysis and application of professional judgment. IEP fails to explain the basis for its expectation that the IOUs assume the burden of providing this service to market participants. As Mr. Anderson pointed out, "consultants that run production cost models, including models of the California Independent System Operator (CAISO) system, are widely available . . . Also substantial historical data regarding the CAISO market prices are publicly available to bidders."[110] Thus, any market participant that believes that it can enhance its bid by running production cost models is free to retain a consultant to do so, and should not demand that the IOU perform this service at its behest.

Mr. Anderson also addressed in his rebuttal testimony several errors contained in the analysis offered by of IEP witness, Mr. Monsen. He pointed out, for example, that in proposing adders related to capital, Operations & Maintenance ("O&M") and heat rate for UOG projects, Mr. Monsen incorrectly assumes that, for Independent Power Producer ("IPP") projects, the capacity, heat rate and O&M are fully specified, and therefore that there is little or no uncertainty in those factors.[111] He noted further that in making this assumption, IEP ignores equivalent costs and risks faced by ratepayers in connection with IPP projects. He observed that "IEP conducted no analysis and provided no calculations regarding the delta between the 'initial cost estimates' of IPP project and the final cost ratepayers are paying today."[112] Omission of this data is significant, and inexplicable, given the number of re-priced PPAs submitted for Commission approval. IEP fails, however, to propose any adjustments or adders related to IPP projects equivalent to those proposed for UOG to account for this situation.

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[109] *See* D.06-06-066, *et seq*.
[110] SDG&E/Anderson, Exh. 315, p. 7.
[111] *Id*.
[112] *Id*. at pp. 7-8.

In addition, the capital cost adder proposed by IEP appears to be based upon erroneous data.[113] Mr. Anderson explained, that "[Mr. Monsen's] work papers show SDG&E's Palomar Plant dropping from 550 MW in the initial application to 500 MW as actual. However, Palomar has a CAISO net qualifying capacity (NQC) rating of 565 MW. If the 500 MW used by IEP is replaced with the correct 565 MW value, then the IEP worksheet goes from showing Palomar at being 12% over on a $/kw basis to 1% under."[114] Similarly, Mr. Monsen's conclusion that the heat rate adder is necessary, and that it should be added only to UOG bids, makes little sense. As Mr. Anderson explained, while a plant's heat rate may degrade slightly over time, the degradation will be minimal (assuming the plant is performing major maintenance in accordance with the schedule set by the original equipment manufacturer).[115] Thus, IEP greatly overstates the need for a heat rate adder. In addition, the degradation potential exists equally for UOG and IPP plants. As Mr. Anderson pointed out, "there is no reason that a UOG plant would experience more or less degradation than an independently-owned plant, so long as they are carrying out the required maintenance. Thus, the idea that an adder should be applied only to UOG plants does not make sense."[116] Mr. Anderson also noted that it appeared that IEP relied on irrelevant data in develop its heat rate adder proposal.[117]

IEP's proposal to adopt an O&M cost adder is similarly flawed. Specifically, IEP's claim that ratepayers are at risk for direct pass-through of "unexpected" O&M costs is incorrect. As Mr. Anderson explained, the Commission reviews both historical and forecasted UOG O&M costs in each SDG&E general rate cases ("GRCs"); if SDG&E were to propose a change in O&M costs, the Commission has the ability to fully review that request to determine whether it

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[113] IEP/Monsen, Exh. 2000, p. 41.
[114] SDG&E/Anderson, Exh. 315, p. 8.
[115] *Id*. at p. 9.
[116] *Id*.
[117] *Id*.

is reasonable.[118/] To the extent SDG&E experiences an "unexpected" O&M cost increase that was not forecasted in its last GRC, SDG&E would be able to pass that cost increase on to ratepayers only with specific Commission approval. In short, as the Commission noted in the 2004 LTPP decision, the utilities are held accountable for cost-overruns and project delays:

> Putting shareholders – not ratepayers – at risk for cost overruns will put IOU-owned projects and PPAs on equal footing (at least with respect to the allocation of risk), impose some measure of market discipline on IOUs when formulating their bids, and better ensure that the resource solicitation process is fair and competitive.' Consequently, IOUs will not be allowed to recover initial capital costs in excess of its final bid price for utility-owned resources.[119/]

It is plain that there exists no need to modify the existing approach for evaluating UOG versus PPA bids. The current policy requiring that any hybrid product evaluation employ the LCBF guiding principle, with IE oversight in accordance with Commission guidelines, is adequate to protect ratepayers and promote competition, and should therefore remain in place.

D. The Utilities' Current Approach to Sale of Excess RA Products does not Require Modification

As discussed above, in D.06-06-064 the Commission established a local procurement obligation as a component of the broader resource adequacy requirements program applicable to Commission-jurisdictional LSEs.[120/] The decision requires that LCRs be allocated to individual Commission-jurisdictional LSEs pursuant to a Commission-approved allocation methodology, and provides that such LSEs are subject to penalties for failure to meet local procurement obligations. The decision encourages the IOUs to sell contracted RA resources that are not required to meet customer need, to the extent doing so is consistent with the LCBF procurement

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[118/] *Id*. at p. 10.
[119] D.04-12-048, *mimeo*, p. 218, FOF No. 87.
[120/] D.06-06-064, *mimeo*, p. 2.

principle.[121] The decision expressly declines, however, to mandate the timing or terms of the IOUs' sale of excess RA capacity:

> AReM suggests that IOUs should be required to sell off any long capacity to other LSEs at reasonable prices. This requirement, AReM maintains, would prevent IOUS from using an administrative allocation to sell their excess local capacity. TURN has suggested the mandatory sales of the local attribute of resources. We will not adopt such proposed requirements. *There may be reasons for a long LSE to hold on to capacity even though it does not need the capacity to meet its own local procurement obligations.* However, while we do not mandate such sales, we join the staff in calling upon IOUs to carefully consider whether holding on to capacity that is not needed for Local RAR is in line with the "least-cost/best-fit" procurement principle. IOUs may wish to hold Requests for Offers (RFOs) for System RAR capacity concurrently with RFOs for their excess RAR capacity that satisfies local requirements so that they can better determine the "least cost/best fit" mix of RAR resources.[122]

SDG&E witness, Mr. Miller, explained that when SDG&E anticipates that it may have excess RA that it can make available to other market participants, it must first evaluate how certain it is that its RA position will not change.[123] He noted that "SDG&E strives to avoid situations where it over-sold and would be forced to buy RA back, or where it purchased too much RA and would have to sell the excess or allow the RA to go unused."[124] To avoid these undesirable outcomes, SDG&E does not issue RFOs for RA until it has a fairly clear view of its RA position, including availability and amount of RA resources and demand position. Mr. Miller observed that "in the absence of certainty regarding its RA position, it would be unwise for SDG&E to issue an RFO to either buy or sell RA."[125] In addition, SDG&E typically maintains a small amount of RA supply above required minimums to protect against variances to

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[121] *Id*. at p. 65.
[122] *Id*.
[123] SDG&E/Miller, Exh. 313, p. 23.
[124] *Id*.
[125] *Id*.

SDG&E's supply position or RA requirement in order to ensure it has met its RA obligations at the time RA-related filings are made to the CAISO and CPUC.[126]

No evidence that would justify a departure from the current process and timeline for the IOUs' RFOs for RA has been offered into the record of this proceeding. Under the existing process, the IOUs have been able to procure RA when needed, and to make excess RA available when appropriate.[127] Accordingly, the Commission should find that changes to the current process and timeline for the IOUs' RFOs for RA are not warranted.

E. *The Commission Should Not Adopt the Staff Proposal Regarding Procurement Oversight Rules*

The ALJ Ruling directed parties to address a Staff proposal (the "Staff Proposal") regarding procurement oversight rules that is based upon Section O of the draft *Procurement Manual* ("Rulebook"). The rules included in the Staff Proposal address oversight responsibilities and authority by the IEs, the PRGs, the Cost Allocation Mechanism ("CAM") groups, and the Energy Division. The Staff Proposal would also establish SOCs governing the procurement activities of the utilities and their employees.[128] Although the Scoping Memo contemplated that the "Rulebook" would include only *existing* rules,[129] the Staff Proposal deviates markedly from this approach. Staff claims that the proposed rules "clarify and elaborate on" existing rules, and that the proposed rules include "minor" changes to existing rules.[130] Staff further observes that the proposed rules differ from prior Commission decisions due to undefined "operational and legal" considerations.[131]

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[126] *Id*. at p. 24.
[127] *Id*. at p. 22.
[128] ALJ Ruling, Appendix B, p. 3.
[129] *See* Scoping Memo, p. 43 (emphasis added).
[130] ALJ Ruling, Attachment B, p. 3.
[131] *Id*.

The procurement oversight rules proposed by Staff are clearly not consistent with the existing rules approved by the Commission. Nor are the changes to the procurement rules proposed by Staff "minor"; rather, the Staff Proposal includes significant modifications to existing Commission decisions and newly-created rules. As SDG&E witness, James Magill, observed, "it is improper for Staff to make unilateral changes to Commission-adopted reporting requirements and procedures without input from the IOUs, who will be required to comply with the adopted rules, and market participants that must function within the rules."[132/] Moreover, conducting review of the Rulebook in the piecemeal fashion proposed by Staff is counter-productive and inefficient. The proper forum for addressing the proposed Rulebook is in a workshop environment that involves collaboration by all stakeholders rather than through unilateral action by Staff.

The evidentiary record of the instant proceeding is inadequate to support the modifications to prior Commission decisions proposed in the Staff Proposal or the addition of new rules that, as discussed below, could be detrimental. In the absence of an adequate factual record, the Commission should not adopt any substantive modifications to existing decisions; nor should it adopt new rules without permitting sufficient time for meaningful stakeholder review and comment. The Commission originally intended to consider the proposed Rulebook in 2012 in the 2nd phase of Track III.[133/] The Commission should return to this timeline and should conduct workshops in a manner that allows for meaningful stakeholder review and input.

132/ SDG&E/Magill, Exh. 313, p. 27.
133/ Scoping Memo, p. 43.

As discussed below, SDG&E has several concerns, both procedural and substantive, related to the Staff Proposal. It details elements of the proposed Rulebook that it views as particularly problematic, but notes that additional concerns may exist. It reserves the right to raise additional issues related to the Rulebook in the future.

(i) <u>The Rulebook Should Operate as a Compendium</u>

SDG&E believes that the Rulebook offers value as a compendium of the various Commission requirements related to electric procurement, but should not be adopted as an enforceable document. As Mr. Magill observed, "if the Rulebook is envisioned as being akin to a General Order that would supersede prior Commission orders, it would be necessary to closely review each and every provision contained in the Rulebook in order to ensure consistency with prior Commission decisions and that relevant rules from such prior Commission decisions had not been omitted or improperly modified."[134/]

Certainly, this degree of scrutiny is not possible in the instant case given the scope of the issues currently before the Commission in this proceeding and the truncated procedural schedule. It would also be necessary to establish a process for updating the Rulebook to accurately reflect new requirements adopted by the Commission. As a practical matter, however, given the Commission's limited resources, it may not be feasible for it to assume the burden of immediately updating the Rulebook upon issuance of future Commission decisions. Thus, if the Commission elects to adopt the rules proposed in the Staff Proposal, it should deem the Rulebook to be a non-binding compendium available as a reference (updated periodically rather than immediately) for parties involved in electric procurement.

[134/] SDG&E/Magill, Exh. 313, p. 27.

(ii) Certain Rules Proposed by Staff Related to PRG Review Should Not be Adopted

As Mr. Magill observed, Staff's proposed rules governing the PRG's review of the overall procurement process generally comport with previous Commission decisions, which established the rules currently in effect.[135/] He noted, however, that in some instances, Staff deviates from the current rules by either adding to or omitting certain aspects of the rules.[136/] For example, the Staff Proposal would introduce a new requirement to report on fuel forecasts.[137/] The proposed fuel forecast requirement does not exist under current Commission decisions, thus it is not appropriate for inclusion in the Rulebook, which is intended to reflect only "*existing*" procurement rules.[138/] Moreover, because it is not a well-developed requirement adopted on the basis of a factual record, the fuel forecast requirement inserted into the Rulebook lacks necessary definition. It is not at all clear what information SDG&E would be required to report to the PRG.[139/]

The Staff Proposal also improperly eliminates the existing rule that grants the IOUs the option to conduct PRG meetings via teleconference.[140/] Elimination of the conference call option for PRG meetings makes little sense and is not in the public interest. As Mr. Magill explained, requiring every PRG meeting participant to travel to the meeting location to appear in-person would be highly unproductive.[141/] PRG meetings typically require input from a number of different individuals, often on limited topics. A utility subject matter expert may, for example, participate in a PRG meeting to discuss the key aspects of a specific procurement contract or the IOU's procurement and hedging strategies. Requiring these individuals to travel for only a small

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135/ *Id*. at p. 28.
136/ *Id*. at p. 29.
137/ ALJ Ruling, Appendix B, p. 13.
138/ *See* Scoping Memo, p. 43 (emphasis added).
139/ SDG&E/Magill, Exh. 313, p. 29.
140/ *See* D.03-12-062, *mimeo*, p. 47.
141/ SDG&E/Magill, Exh. 313, p. 29.

portion of the actual meeting would be an inefficient use of resources. In addition, non-utility PRG members may have limited travel budgets that preclude in-person attendance at PRG meetings.

Mr. Magill also noted that elimination of the teleconference option would make it extremely difficult for SDG&E to consult with its PRG in instances in which its estimated portfolio risk exceeds the Customer Risk Tolerance ("CRT") threshold, as required by D.03-12-062.[142/] He expressed further concern related to the CRT threshold, noting that the Staff Proposal includes the requirement that "[t]he IOU will consult with their PRGs on instances in which its estimated portfolio risk exceeds the Customer Risk Threshold by 25%."[143/] He explained that SDG&E supports consulting with its PRG in instances in which its estimated portfolio risk (VaR-to-Expiration at a 95% confidence interval) exceeds the CRT threshold by 25%.[144/] However, Staff's proposal omits a critical component by not incorporating the current Commission adopted 95% confidence interval.[145/] Nor does it incorporate any discussion of the VaR-to-Expiration ("VtE") component.[146/] Staff's proposal as written would be inconsistent with the Commission's approved risk metric. As a result of this omission, PRG meetings would not be held until after the risk metric was already exceeded.[147/]

142/ *Id.*
143/ ALJ Ruling, Appendix B, p. 14.
144/ SDG&E/Magill, Exh. 313, p. 30.
145/ D.07-12-052, *mimeo*, p. 175.
146 SDG&E uses the term VtE synonymously with TeVaR (Terminal VaR). VtE/TeVaR presumes that all positions are held to expiration. "Value at Risk" refers to the statistical dollar amount that can be lost on the net open position of a portfolio over a specific time horizon and with a given confidence interval. TeVaR accounts for the increasing potential distribution of prices as time passes, as well as the expiration of the positions in the portfolio with the passage of time. The result is the estimation of loss, at the specified confidence level, assuming that the portfolio remains constant over time until all positions within it have expired. SDG&E/Magill, Exh. 313, p. 30.
147/ *Id.*

Finally, Staff seeks to impose a new rule that would require each IOU to confer with the PRG if "material" barriers to hedging arise.[148] The IOUs would be required to file modifications to its hedging strategy in an expedited application within fifteen days of the PRG meeting.[149] This requirement does not exist under the Commission's existing rules and should not be adopted. As Mr. Magill explained, the proposed rule is poorly defined and, in any event, is unnecessary.[150] Because the proposed rule includes no definition of what constitutes a "material" barrier to hedging, it is not clear when the requirement to confer with the PRG on these issues would arise. Moreover, Staff's proposed requirement would serve little purpose since SDG&E is already required to consult with the PRG on a quarterly basis to review the company's hedging strategy, at which time any other issues impacting SDG&E's hedging strategy (*i.e*. material barriers) can be discussed. Also, in those instances where SDG&E proposes to make changes to its Commission-adopted LTPP, it can do so through an Advice Letter process.[151] To require instead that the IOUs file an expedited application imposes unnecessary burden and delay, which would be highly problematic given the time-sensitive nature of the changes.[152]

(iii) <u>Certain Rules Proposed by Staff Related to PRG Meeting Protocols Should Not be Adopted</u>

In addition to concerns regarding the issues subject to PRG review discussed above, SDG&E notes that certain of the proposed PRG meeting protocols are ill-advised and are likely to impose unnecessary burden. For example, the proposal that PRG members be allowed to request a delay of the PRG meeting if they believe there is inadequate time to review corrected

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[148] ALJ Ruling, Appendix B, p. 14.
[149] *Id*.
[150] SDG&E/Magill, Exh. 313, pp. 30-31.
[151] Consistent with Staff's proposal, under the Advice Letter process, SDG&E continues to operate under the existing LTPP until a resolution is adopted by the Commission.
[152] SDG&E/Magill, Exh. 313, p. 31.

materials provided by the IOU is, as SDG&E witness, Juancho Eekhout, pointed out "more troublesome than beneficial."[153/] Mr. Eekhout explained that while SDG&E agrees that it is crucial that PRG members receive notice of mistakes in presentation materials as soon as possible, the challenge inherent in coordinating the schedules of PRG members, Energy Division Staff and IOU representatives makes it extremely difficult to re-schedule meetings. Instead, SDG&E proposes that if PRG members believe that inadequate time exists for review of corrected materials, such materials should be presented at the following PRG meeting. In the alternative, a special PRG meeting could be called to address corrected materials if such materials are time sensitive.[154/]

In addition, the proposal that IOUs provide confidential meeting summaries and a list of information requested or offered to be supplied to PRG members within 14 days of PRG meetings is unnecessary and burdensome.[155/] SDG&E's current practice is to provide a list of attending PRG members, their organizations and an agenda of meeting topics on its PRG calendar, which can be accessed at any time.[156/] SDG&E also provides detailed presentation materials prior to each meeting.[157/] This process provides an efficient way for PRG members to keep track of the details of each meeting by referring to the calendar and/or the relevant presentation materials at their convenience. SDG&E also takes notes of any information requested or offered to be supplied during a PRG meeting, and ensures that issues requiring follow-up are addressed at the next meeting.[158/] SDG&E believes that this method has provided PRG members with the information they require in a timely fashion. SDG&E also notes that

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153/ SDG&E/Eekhout, Tr. Vol. 6, p. 717. *See* ALJ Ruling, Appendix B, p. 16.
154/ SDG&E/Eekhout, Exh. 313, p. 31; *see also* Tr. Vol. 6, p. 719.
155/ *See* ALJ Ruling, Appendix B, p. 16.
156/ SDG&E/Eekhout, Exh. 313, p. 31.
157/ *Id.*
158/ *Id.* at p. 32.

PRG members may request, if the circumstances merit, that follow-up materials be provided more quickly.[159/] Hence, imposing an arbitrary 14-day limit on these procedures adds unnecessary administrative burden to the PRG process without providing any additional benefit. Accordingly, the proposed rule should be rejected.

(iv) <u>Certain Rules Proposed by Staff Related to IE Oversight Should Not be Adopted</u>

The Staff Proposal includes certain revisions to the IE rules that are problematic or require further definition. For example, the proposal that IE reports for solicitations of products five years or greater in length be filed with the Energy Division and the PRG at least 7 calendar days before any IOU application is filed with the Commission gives rise to concerns regarding unnecessary delay.[160/] Mr. Eekhout explained that the IE's solicitation report cannot be completed until the IOU's analysis and negotiations are complete; thus, the IE report is a long lead-time item in preparation of applications or advice letters.[161/] The IOU's application or advice letter is typically nearly complete by the time the IE report is ready to be filed. Requiring a 7-day lag in the filing of the advice/letter application after the IE report is filed would result in needless and potentially harmful delay.[162/] Accordingly, the current practice of filing the IE report concurrently with the application or advice letter should be maintained.

In addition, the proposal that the Energy Division have the right to final approval of the use of a particular IE for each RFO should not be adopted.[163/] As Mr. Eekhout explained, while the Energy Division's involvement in the IE selection process is beneficial, the IOUs work closely with each of their approved IEs and are in the best position to determine which IEs are

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159/ *Id.*
160/ *See* ALJ Ruling, Appendix B, p. 15.
161/ SDG&E/Eekhout, Exh. 313, p. 33.
162/ *Id.*
163/ *See* ALJ Ruling, Appendix B, p. 11.

most qualified for evaluating certain types of solicitations.[164] He noted, for example, that "certain IEs may have a wealth of experience with renewable procurement, but less experience with Resource Adequacy products."[165] Accordingly, SDG&E proposes that once the PRG and Energy Division select IEs to be part of the IOU's pool, the IOU should be able to determine which IE has the skills most relevant to a specific solicitation.

SDG&E is also concerned that the proposal to allocate costs associated with the Commission's use of IE services to each IOU on a pro rata basis (*i.e.* 33% to each IOU) unless the IE performs work related to only one specific utility unfairly burdens SDG&E.[166] Although this approach was established through D.08-11-008, it places disproportionate burden on SDG&E's ratepayers. SDG&E proposes that the costs instead be allocated on a proportional bases as is common in other proceedings.[167]

Finally, the proposal that communications between the IE and the Energy Division or PRG be permitted without any involvement or knowledge of the IOU must be modified slightly in order to ensure accurate billing by IEs. As Mr. Eekhout explained, "[w]hile SDG&E agrees that these parties should communicate freely and independently, the IOUs must have enough information regarding such communications to be able to verify the amounts billed to SDG&E by the IE."[168] Accordingly, SDG&E proposes that the Energy Division or PRG provide a monthly report to the IOUs indicating the time spent in communications with the IOUs'p respective IEs. Mr. Eekhout noted that the intent of this proposed requirement "was not to try to

[164] SDG&E/Eekhout, Exh. 313, p. 33.
[165] *Id.*
[166] *See* ALJ Ruling, Appendix B, p. 8.
[167] *See, e.g.,* D.06-10-050, *mimeo*, Ordering Paragraph 8, as modified by D.11-01-016 ("The Executive Director may hire and manage one or more contractors to perform tasks described in this order for the purpose of advancing RPS Program goals. Such costs, if any, shall not exceed a total annual amount of $400,000, **and the total shall be paid by PG&E, SCE and SDG&E on a proportional basis in relationship to retail sales** reported each year in the March 1 RPS compliance report [or other first report each year as directed by the Executive Director.") (Emphasis added).
[168] SDG&E/Eekhout, Exh. 313, p. 32.

second guess or get a clue of what the discussion was about, [but] just to make sure that the meeting did take place and how many hours it took."[169] The report should indicate (i) the duration of the communication that occurred; and (ii) if the Energy Division or PRG requested that the IE perform follow-up work that will be billed to the IOU. This will allow each IOU to verify billed costs when it receives invoices from its IEs.

(v) Staff's Proposed Rule Regarding Provision of Data to the PRG to Support Procurement of Congestion Revenue Rights Should be Rejected

Staff recommends that when proposed or completed Congestion Revenue Rights ("CRR") procurement is reported to the PRG, the IOU be required to present specific information on (i) the contribution of congestion risk to the TeVaR (terminal VaR)[170] value; and (ii) the reduction or increase in TeVaR due to CRR procurement.[171] As Mr. Magill explained, however, SDG&E does not currently have the modeling capability to produce this information. Modeling the potential impact of CRRs on the portfolio would require complex modeling capability to capture the pricing differentials and potential congestion at numerous generation nodes both inside and outside SDG&E's service territory as the prices relate to SDG&E's load aggregation point.[172] This is not a currently a Commission requirement, and should not be adopted here.

(vi) Staff's Proposal to Make QCR Audit Reports Public Should be Modified

Staff proposes to modify existing procurement rules to make QCR audit reports public.[173] In order to do so, Staff proposes to: (i) redact market-sensitive information from the audit reports; (ii) provide an opportunity for the IOUs to comment on audit reports; (iii) work

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[169] SDG&E/Eekhout, Tr. Vol 6, p. 742.
[170] SDG&E uses VtE as a proxy for calculating TeVaR. SDG&E/Magill, Exh. 313, p. 34, note 35.
[171] ALJ Ruling, Appendix B, p. 16.
[172] SDG&E/Magill, Exh. 313, p. 34.
[173] ALJ Ruling, Appendix B, pp. 6-7.

with the IOUs to resolve any discrepancies in the audit report; and (iv) *make available the IOU rebuttals in those instances where discrepancies persist*.[174/]

While SDG&E does not oppose making QCR audit reports public, it recommends that the Energy Division be required to include in the body of the QCR audit report the IOU's comments in response to the findings set forth in such audit report – this should be required in *all* instances, not merely when discrepancies exist. This requirement would impose little or no additional burden on Staff, and will ensure that the IOU's position on all findings included in a QCR audit report are available, thereby avoiding creation of the perception that the IOU endorses a particular finding due to its inability to address it.

IV.
CONCLUSION

For the reasons set forth above, the Commission should approve the Track I Settlement Agreement submitted on August 3, 2011, and adopt an LCR need determination of 415 MW for the SDG&E service area. In addition, the Commission should resolve the Track III issues enumerated above in a manner consistent with the discussion included herein.

Respectfully submitted this 16th day of September, 2011.

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174/ *Id*. at p.7 (emphasis added).