

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

Order Instituting Rulemaking to Promote
Consistency in Methodology and Input
Assumptions in Commission Applications of
Short-run and Long-run Avoided Costs,
Including Pricing for Qualifying Facilities.

Rulemaking 04-04-025
(Filed April 22, 2004)

**PRE-WORKSHOP REPLY COMMENTS OF
THE COGENERATION ASSOCIATION OF CALIFORNIA AND
THE ENERGY PRODUCERS AND USERS COALITION**

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Pursuant to the ruling issued April 22, 2004, the Cogeneration Association of California¹ and the Energy Producers and Users Coalition² (collectively, CAC/EPUC) submit these Pre-Workshop Reply Comments.

I. INTRODUCTION AND SUMMARY

Most opening workshop comments focused on the study prepared by Energy and Environmental Economics (E3 Report). The E3 Report proposed a comprehensive avoided cost methodology reflecting the calculation and various components of avoided cost; applicable components include generation, environmental, transmission, distribution, reliability, and line losses. The

¹ CAC represents the power generation, power marketing and cogeneration operation interests of the following entities: Coalinga Cogeneration Company, Mid-Set Cogeneration Company, Kern River Cogeneration Company, Sycamore Cogeneration Company, Sargent Canyon Cogeneration Company, Salinas River Cogeneration Company, Midway Sunset Cogeneration Company and Watson Cogeneration Company.

² EPUC is an ad hoc group representing the electric end use and customer generation interests of the following companies: Aera Energy LLC, BP America Inc. (including Atlantic Richfield Company), Chevron U.S.A. Inc., ConocoPhillips Company, Exxon Mobil Corporation, Shell Oil Products US, THUMS Long Beach Company, Occidental Elk Hills, Inc., and Valero Refining Company - California.

objective is to develop a consistent and comprehensive avoided cost methodology for evaluating the cost-effectiveness of conservation programs and establishing standard payment for purchases from qualifying facilities (QFs). A consistent and comprehensive avoided cost methodology is a worthy and achievable goal.

CAC/EPUC, in response to primarily the utilities' opening comments, make the following points in this reply:

- The current schedule may not include sufficient time to address QF issues; however, if phased approach is adopted, the Commission must ensure that the avoided cost methodology consistently includes all "adders" to comply with non-discrimination section of the Public Utility Regulatory Policies Act of 1978 (PURPA). Further, the Commission should make an actual avoided cost determination here and not defer such a determination.
- Public Utilities Code Section 390(b) governs SRAC energy payments and results in just and reasonable rates, thereby complying with federal law. SRAC as-available capacity payments should continue to equal 100% of a simple cycle combustion turbine (CT).
- The use of the all-in combined cycle combustion turbine (CCCT) cost remains the appropriate proxy for LRAC. Also, proposed alternate LRAC determinations based on market prices are premature. LRAC methodology should include all components detailed in the E3 Report.
- Pacific Gas & Electric Company's (PG&E) proposal regarding an alternate avoided cost methodology should be made available to parties prior to the workshop and parties should have the opportunity to conduct discovery on the proposal.
- Utility procurement data is required to calculate the utilities' avoided cost; therefore utility procurement data should be made available to all parties prior to the workshop.

II. QF ISSUES MAY NEED ADDITIONAL TIME TO BE ADEQUATELY ADDRESSED AND MUST BE TREATED CONSISTENTLY WITH OTHER RESOURCES.

CAC/EPUC share the concern of San Diego Gas & Electric Company (SDG&E) and Southern California Gas Company (SoCalGas) that the current schedule may not provide sufficient time to address QF issues. Accordingly, it may be more efficient to establish a separate phase of this proceeding to address QF issues. Any such phasing must not, however, result in inconsistent applications of the various avoided cost components comprising the overall comprehensive avoided cost methodology.

A separate QF track may only be established if it would continue to include all avoided cost components. CAC/EPUC accordingly strongly disagree with the PG&E and Edison positions that some adders in the E3 Report might not be included in QF pricing.³ A separate QF phase must not result in such discrimination against QFs. As the Independent Energy Producers Association (IEP) noted in their opening comments, PURPA forbids such discrimination. See Pre-workshop Comments of IEP, at 3. While a separate QF track may be adopted, implementation of a differential QF avoided cost methodology without including consideration of all “adders” provided for in other avoided cost methodologies must be avoided.

Moreover, the Commission should not defer the actual determination of the utilities’ avoided costs to another proceeding as suggested by Edison. Rather, the Commission should make such a determination in this proceeding.

³ See Pre-Workshop Comments of PG&E, at 11; see also Pre-Workshop Comments of Edison on Avoided Cost Methodologies (Edison Comments), at 11.

III. SECTION 390(B) RESULTS IN JUST AND REASONABLE SRAC ENERGY PAYMENTS, AND THE SRAC AS-AVAILABLE CAPACITY PAYMENT SHOULD REMAIN EQUAL TO 100% OF THE COSTS OF A SIMPLE CYCLE CT.

QF SRAC pricing applies to energy deliveries for most of the existing QF projects that are under Standard Offer contracts, including those QF projects for which the 5-year SO1 contract extension were authorized in D.04-01-050. QF SRAC pricing consists of an SRAC energy payment and an as-available capacity payment. The QF SRAC energy payment prescribed by Section 390(b) results in just and reasonable rates. QF SRAC as-available capacity payments should remain 100% of a simple cycle CT.

With respect to SRAC energy payments, CAC/EPUC concur with parties that recognize that Section 390(b) defines how SRAC energy prices are to be determined.⁴ In part, Section 390(b) states:

. . . Short run avoided cost energy payments paid to nonutility power generators by an electrical corporation shall be based on a formula that reflects a starting energy price, adjusted monthly to reflect changes in a starting gas index price in relation to an average of current California natural gas border price indices. The starting energy price shall be based on 12-month averages of recent, pre-January 1, 1996, short-run avoided energy prices paid by each public utility electrical corporation to nonutility power generators. The starting gas index price shall be established as an average of index gas prices for the same annual periods.

P.U. Code §390(b). CAC/EPUC further agree with IEP and SDG&E, SoCalGas that this determination complies with federal law and that no reason has been put

⁴ See Pre-workshop Comments of IEP, at 10; see also Edison Comments, at 14-15; see also Comments of SDG&E and SoCalGas on Energy and Environmental Economics, Inc. Report Entitled A Forecast of Cost Effectiveness Avoided Costs And Externality Adders And Pre-Workshop Comments On Avoided Costs (SDG&E/SoCalGas Comments), at 10.

forth to change Section 390(b).⁵ There has been no evidence presented that Section 390(b) SRAC energy prices result in unjust and unreasonable rates. The SCE claim that 390(b) is “stale” offers no substantiation beyond superficial reference to purported changes in the energy market, utility procurement practices and technology to support its assertion.⁶

CAC/EPUC agree with IEP and the California Wind Energy Association that a simple-cycle CT should remain the proxy for the SRAC as-available capacity payment.⁷ Indeed, the Commission’s position on marginal cost electric rate design requires the continued the use of this proxy. Moreover, consistent with the utilities’ procurement efforts related to new capacity, the value of the as-available capacity payment must be set at 100% of the annualized cost of the CT. CAC/EPUC further support IEP’s statements regarding the apparent misconceptions of this Commission regarding the function of the as-available capacity payments. See Pre-workshop Comments of IEP, at 8-9. When the utilities have achieved their target reserve margins, the as-available capacity payment should be re-evaluated.

IV. LRAC METHODOLOGY SHOULD USE THE “ALL-IN” CCCT COST, NOT MARKET PRICES, AND MUST INCLUDE ALL E3 REPORT COMPONENTS.

The use of the “all-in” cost of a CCCT to establish the generation component of the avoided cost applicable to new long-term QF contracts remains the best indicator for QF LRAC pricing. Additionally, the proposed use of current

⁵ See Pre-workshop Comments of IEP, at 2, 9-10; see *also* SDG&E/SoCalGas Comments, at 10.

⁶ See Edison Comments, at 14.

⁷ See Pre-workshop Comments of IEP, at 8-9; see *also* Pre-Workshop Comments of the California Wind Energy Association, at 4-5.

public electric future prices to establish avoided generation costs and the assumption that these prices include a combined energy and capacity value are not substantiated and should be rejected. Moreover, each individual component of a comprehensive avoided cost methodology must be consistently applied to QF LRAC pricing (e.g., generation, environmental, transmission, distribution, reliability, and line-loss components).

The generation component of the LRAC should reflect the long-run costs associated with the capacity and energy procurement of the investor owned utilities (IOUs). Moreover, the payments to supplying QF resources should reflect the same avoided cost as those used to evaluate demand-side programs. The Workshop should focus on identifying and quantifying those LRAC components that are consistent with the Commission's overall energy policies. The "all-in" cost of a CCCT (applicable in 2004 and for the life of the resource) has been offered by some parties as the appropriate "generation" component of the comprehensive avoided cost methodology. This approach is consistent with the avoided cost pricing in other Commission proceedings.

Utility proposals to shift to an electric market price alternative for QF pricing purposes⁸ ignores the reality of current energy markets; these markets are not sufficiently robust to provide accurate proxies for utility avoided costs. Further, there has been no demonstration that the proper value for capacity would be included in the market price for energy. While at some future point such proposals may be reconsidered, these proposals should be rejected now.

⁸ See Edison Comments, at 11; see also Pre-Workshop Comments of PG&E, at 4.

Additionally, the LRAC for QF pricing should include the same avoided cost components applicable to demand-side management programs when a QF provides consistent benefits. For example, QF cogeneration projects reduced the consumption of natural gas by efficiently utilizing natural gas to produce both electrical and thermal energy. Thus, cogeneration reduces emissions that would otherwise be emitted and an avoided cost emission component should be applicable to cogeneration pricing. This principle should apply to all of the avoided cost components reflected in the adopted comprehensive avoided cost methodology that results from the Workshop.

IV. PG&E'S PROPOSAL AND UTILITY PROCUREMENT DATA SHOULD BE MADE AVAILABLE TO PARTIES PRIOR TO THE WORKSHOP.

PG&E states it is prepared to present “*a proposal to reform QF pricing in a manner consistent with Section 390 and that yields just and reasonable rates*” at the workshop. Pre-Workshop Comments of PG&E, at 11. Any PG&E proposal regarding an alternate QF pricing avoided cost methodology should be made available to parties prior to the workshop. Moreover, parties should have the opportunity to conduct discovery on the proposal. The ability to review the proposal in advance and examine through discovery the underlying assumptions will lead to more focused and productive workshop debate.

Similarly, pre-workshop availability of utility procurement data required to calculate the utilities' avoided cost would further promote a more thorough workshop discussion. As SDG&E and SoCalGas noted, “*the E3 Report appears to lack short- and long-term utility procurement data **needed to develop utility avoided costs for generators.***” SDG&E/SoCalGas Opening Comments, at 10

(emphasis added). Therefore utility procurement data should also be made available to all parties prior to the workshop.

V. CONCLUSION

CAC and EPUC thank the Commission for the opportunity to provide these comments and urge the Commission to act upon the recommendations herein to encourage a productive workshop discussion.

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