Decision **DRAFT DECISION OF ALJ ECONOME** (Mailed 3/4/2002)

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

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| In the Matter of the Application of San Diego Gas and Electric Company (U 902-E) for an Ex Parte Order Approving the Settlement Agreements between SDG&E and certain winning bidders in SDG&E's Biennial Resource Plan Update Auction | Application 97-10-081 (Filed October 30, 1997) |

# ORDER TERMINATING SAN DIEGO GAS & ELECTRIC COMPANY'S BIENNIAL RESOURCE PLAN UPDATE SOLICITATION

## I. Summary

This decision terminates San Diego Gas & Electric Company's (SDG&E) 1993 Biennial Resource Plan Update (Update) solicitation.

## II. Background

### A. The Application

SDG&E filed this application on October 30, 1997 seeking approval of a settlement package totaling $5.095 million containing settlements with three bidders that SDG&E stated may be "winning bidders" in the Update auction, subject to the outcome of certain judicial and regulatory proceedings challenging the legality of the Update ("winning bidders"). The total capacity of the "winning bidders" in SDG&E's solicitation is 501.5 megawatts (MW) of effective capacity, and the three settling bidders represented 108 MW of that effective capacity.

SDG&E's settlement package did not contain settlements with all of the bidders the utility designated as "winning bidders." SDG&E did not settle with PG&E National Energy Group (PG&E NEG)[1] and Kenetech Windpower, Inc. (Kenetech)[2] (nonsettling bidders), whose bids together represent 393.5 MW of effective capacity. SDG&E requested that the Commission approve the settlement package as reasonable and terminate SDG&E's Update solicitation because SDG&E had reached an impasse with PG&E NEG and Kenetech.

In December 1998, the Commission issued Decision (D.) 98-12-074 which approved the settlement package with respect to the three settling "winning bidders." We also deferred consideration of SDG&E's request to terminate its Update, and directed SDG&E and the nonsettling bidders to engage in further negotiation before we addressed the request, under the following rationale.

> "Because of the passage of time since the July [1995] ACR issued, and the uncertainty which exists until this Commission acts on Edison's settlement package, we believe it may be beneficial to give SDG&E and the nonsettling bidders that SDG&E has designated as "winning bidders" additional time to discuss settlement before we address SDG&E's request to terminate its Update solicitation. We, therefore, direct these parties to resume settlement discussions, as set forth in this decision.
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> "SDG&E and certain nonsettling bidders described above should continue to use the guidelines set forth in the July ACR,

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[1] PG&E NEG was formerly known first as U.S. Generating Company and then as PG&E Generating Company. Fellows Generating Company, L.P., the bidder in SDG&E's Update solicitation, was a subsidiary of U.S. Generating Company.

[2] The bidders were six wholly-owned subsidiaries of Kenetech.

> as modified and clarified by this decision, when they resume negotiations. The Commission will judge any remaining settlements presented by SDG&E as reasonable at the time they are entered into, and not at the time the July ACR issued." (D.98-12-074 at p. 21.)

After issuance of D.98-12-074, SDG&E and the nonsettling bidders engaged in further negotiations, which to date have proven unsuccessful. SDG&E does not believe that the nonsettling bidders are entitled to any compensation as a result of their participation in the Update solicitation. The two nonsettling bidders disagree. In March 1999, PG&E NEG declared negotiations with SDG&E to be at an impasse and requested that the Commission impose binding arbitration to define and quantify PG&E NEG's alleged "bid reliance costs." In July 1999, SDG&E declared its settlement discussions with Kenetech were at an impasse. At the March 28, 2000, prehearing conference, the Assigned Commissioner and Administrative Law Judge (ALJ) unsuccessfully explored whether Commission-assisted mediation might help break the impasse. The ALJ also denied the nonsettling bidders' requests that the Commission order binding arbitration. On July 13, 2001, the ALJ requested further briefing on the following issue which this decision addresses:

> Should the Commission grant SDG&E's request in this application to terminate the Update solicitation at this time? This question includes but is not limited to the following sub-issue: whether nonsettling Update bidders who were designated by SDG&E as "winning bidders" in the Update solicitation are entitled to any remuneration from SDG&E?

### B. The Update

In order to set this application in context, we set forth a brief summary of the Update. In the late 1980s, the Commission reviewed the utilities' resource planning activities. On July 7, 1989, the Commission issued Order Instituting Investigation 89-07-004, which officially established the Update proceeding as the forum for reviewing the utilities' long-term resource plans during a designated planning period and addressing generic issues related to utility purchases of electricity from a broad class of nonutility energy producers called qualifying facilities or QFs.[3] (See D.92-04-045, 44 CPUC2d 6, 22.) For each utility, the Commission specified a certain amount of capacity and the benchmark prices for that capacity to be offered for possible deferral through QF bidding. This solicitation was known as the Final Standard Offer 4 (FSO4) auction process.

On August 11, 1993, SDG&E commenced its solicitation in the Update in compliance with our orders. On December 9, 1993, Southern California Edison Company (Edison) suspended its solicitation, informed the Commission of unanticipated bidding strategies, and reargued the wisdom of a number of policy implementation methods we had previously determined (*e.g.*, second price auction, renewable set-aside.) On December 21, SDG&E filed a Petition for Modification of certain Update decisions, which raised issues similar to Edison. In June 1994, the Commission issued D.94-06-047, 55 CPUC2d 274, which modified portions of the FSO4 to address unanticipated bidding strategies and

[3] A QF is a small power producer or cogenerator that meets federal guidelines and thereby qualifies to supply generating capacity and electric energy to electric utilities.

recommenced the solicitation schedule. The Commission later stayed D.94-06-047 on its own motion in D.94-10-039, 56 CPUC2d 620.

A number of parties, including SDG&E, filed applications for rehearing or petitions to modify the June 1994 decision. These pleadings culminated in D.94-12-051, 58 CPUC2d 300, in which the Commission denied, *inter alia*, SDG&E's application for rehearing of D.94-06-047, but granted a limited rehearing at the request of Flowind Corporation in order to review and determine the as-available wind bidders. The Commission also lifted the stay it issued in D.94-10-039, and required SDG&E to negotiate additional terms and to submit FSO4 contracts to the Commission for approval by advice letter filing. Under the then-applicable schedule, SDG&E was required to commence FSO4 contract negotiations with "winning bidders" after January 30, 1995, file contracts for Commission approval by May 28, 1995, and execute the FSO4 contracts by July 27, 1995.

Following issuance of D.94-12-051, SDG&E and Edison filed petitions for enforcement with the Federal Energy Regulatory Commission (FERC) that challenged the Commission's reinstatement of the solicitation and sought to enjoin the Commission from implementing its orders and to be relieved from having to enter into contracts with bidders designated as "winning bidders."

On February 23, 1995, FERC issued an *Order on Petitions for Enforcement Action Pursuant to Section 210(h) of PURPA* in Docket Nos. EL95-16-000 and EL95-19-000 (February 23 FERC Order).[4] FERC ruled that this Commission's

[4] 70 FERC ¶ 61,215. PURPA is the Public Utility Regulatory Policies Act of 1978. The utilities filed their petition for enforcement pursuant to Section 210 of PURPA, 16 U.S.C. § 824a-3(h) (1988).

implementation of the Update violated PURPA and FERC's implementing regulations because this Commission did not consider all sources of electric capacity in setting avoided cost prices. The FERC concluded:

> "Because the California Commission's procedure was unlawful under PURPA, Edison and SDG&E cannot lawfully be compelled to enter into contracts resulting from that procedure. At this juncture, there are no executed contracts. However, in order to avoid parties spending further time and resources in pursuing contracts that would be unlawful under PURPA, we believe it would be appropriate for the California Commission to stay its requirements directing Edison and San Diego to purchase pending the outcome of further administrative procedures in accordance with PURPA. We also encourage the utilities and QFs to reach a settlement that would be consistent with PURPA." (February 23 Order, 70 FERC ¶ 61,215 at 61,677-78.)

The February 23 FERC Order precipitated the filing of various motions to stay the Update. On March 7, 1995, the Assigned Commissioner issued an interim stay of the Update solicitation and called for comments on four alternative actions that the Commission might take. On March 16, the full Commission on its own motion extended the interim stay, "in order to permit additional time to assess the impact of the FERC order on the Update proceeding and to review the Commission's legal and policy options. A stay will also suspend the deadlines for the signing of contracts by the utilities and will avoid what may be the needless expenditure of time and resources by the parties and the Commission in order to resolve the rehearing issues in this proceeding." (D.95-03-019, 59 CPUC2d 52, 53.)

The Commission and numerous parties filed requests for rehearing and clarification of the February 23 FERC Order. FERC issued a notice stating its intent to treat these requests for rehearing as motions for reconsideration. FERC

issued its *Order on Requests for Reconsideration* on June 2, 1995, upholding the February 23 FERC Order. (71 FERC ¶ 61,269.)

On July 5, 1995, the Assigned Commissioner issued an Assigned Commissioner's Ruling (July ACR) that memorialized the public discussion among Commissioners at the June 21, 1995 meeting, and stated that the Commission was unanimous in finding settlement the most appropriate next step in the Update proceeding, as long as ratepayer interests were advanced and protected by the settlements. (July ACR at p. 7.)[5] The July ACR set forth criteria by which the Commission would evaluate settlements with bidders, and directed each utility to file a single application containing all the settlement agreements it wished the Commission to approve. (*Id.* at p. 11.)

Subsequent to the issuance of the ACR, Edison submitted a settlement with its "winning bidders" that the Commission approved in D.98-12-072, and SDG&E reached a settlement with some of its "winning bidders" that the Commission approved in D.98-12-074. In order to seek closure of this proceeding, the ALJ issued the July 13, 2001 ruling requesting comment on whether or not the Commission should terminate SDG&E's Update.

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[5] The July ACR states that the Commission unanimously delegated to the Assigned Commissioner the task of memorializing the public discussion to provide guidance to the settling parties pursuant to the authority conferred by Article 12, Section 2 of the California Constitution. (July ACR at pp. 1-2.) First enacted in 1879, that portion of the Constitution provides that: "…Any commissioner as designated by the commission may hold a hearing or investigation or issue an order subject to commission approval."

### C. The Parties' Response to the ALJ's July 2001 Questions

SDG&E, PG&E NEG and Kenetech (jointly), as well as ORA, responded to the ALJ's ruling. SDG&E urges the Commission to (1) terminate its 1993 Update solicitation and (2) declare that PG&E NEG and Kenetech (the nonsettling bidders) are not entitled, either on legal or equitable grounds, to recover from SDG&E or its customers any bid development and reliance costs allegedly incurred in connection with the Update solicitation. SDG&E argues that the Commission should terminate the Update solicitation because FERC declared the solicitation invalid and the Commission should abide by this determination. SDG&E also argues that because the electric industry regulatory climate has changed dramatically since 1993, continuing the Update serves no public purpose and is not in the public interest.

According to SDG&E, Commission decisions as well as the request for bids (RFB) it issued in 1993 make clear that these nonsettling bidders are not entitled to any remuneration from SDG&E. SDG&E also argues that it has negotiated in good faith with PG&E NEG and Kenetech, and moves to strike a large portion of the bidders' opening brief, which SDG&E states violates Rule 51.9 and the parties' confidentiality agreements by disclosing to the Commission the alleged content of settlement negotiations.

ORA agrees with SDG&E that: (1) the bidders do not have a valid claim against SDG&E; (2) SDG&E is under no obligation to reach a settlement with the bidders; and (3) ratepayer interests are not advanced by settlement. ORA believes the Commission has authority to terminate the Update and urges it to do so.

PG&E NEG and Kenetech believe that no legal or equitable reason warrants the termination of SDG&E's Update solicitation at this time. If the Commission does so, PG&E NEG and Kenetech believe they would be wrongfully punished, arguing that they have complied with all relevant Commission Update-related decisions.

PG&E NEG and Kenetech state that the Commission cannot terminate SDG&E's Update solicitation because no settlements have been reached. These bidders argue that the Commission can only terminate SDG&E's solicitation upon making specific findings that: (1) SDG&E has complied fully with the July 1995 ACR and D.98-12-074; and (2) the failure to settle is directly attributable to PG&E NEG and Kenetech's unreasonable demands. PG&E NEG and Kenetech believe that the Commission should employ its resources to further facilitate a settlement of this matter, and urge that the Commission or a mediator review these bidders' costs for reasonableness. The bidders also believe the Commission should deny SDG&E's motion to strike, arguing that most of the settlement references made are either permissible broad generalities or public information.

## III. Discussion

### A. The July ACR Did Not Mandate Settlement

The July ACR encouraged, but did not mandate, settlements. Ruling paragraph 1 of the ACR stated:

> "Settlement between winning bidders and the respondent utilities conducting the auction, and wind bidders and those utilities, that meet each party's needs given this climate of uncertainty and are in the public interest are encouraged."

The July ACR memorialized the goals and objectives of the settlement process, as well as a number of settlement options such as "the option," "the

buyout," and "the contract." (*Id.* at p. 8.) The July ACR recognized that FERC also encouraged the utilities and the QFs to achieve settlements consistent with PURPA. However, it cautioned that the Commission did not encourage settlements at all costs:

> "The surest way to achieve settlement would be to assure parties that any costs of settlement would be fully recovered from ratepayers so that QFs merely needed to tell utilities how large a check to write. We are decidedly not encouraging such settlement, nor are we preapproving recovery of settlement costs. Commissioner Conlon said it best during our public discussion: we want to see value received for payment given. We recognize that settlements that are in the ratepayer' interest may not be achievable with every winning bidder, but we expect the utilities to make the effort, and we expect settlements in the ratepayers' interest when we review them as a package. " (*Id.* at p. 9.)

Thus, the July ACR did not mandate that the utility settle with each "winning bidder", nor did it require that the utilities' settlement package contain a settlement with all "winning bidders."

### B. D.98-12-074 Did Not Mandate Settlement

D.98-12-074, which approved as reasonable SDG&E's package of settlements with three "winning bidders", did not add a new requirement to the July ACR mandating the utility settle with all "winning bidders." In reviewing the ACR and endorsing its goals and objectives, the Commission stated its agreement with SDG&E and ORA "that the July ACR did not mandate settlement with every bidder no matter what the cost, and did not mandate that we find a settlement package which eliminates all potential litigation reasonable, no matter what the cost." (D.98-12-074 at p. 20.)

In D.98-12-074, the Commission directed SDG&E and certain nonsettling bidders to recommence settlement negotiations based on the rationale set forth in the decision, and to report to the Commission within 45 days as to the status of the negotiations. The Commission did so under the assumption that the passage of time since the July ACR issued, and the uncertainty which existed until the Commission acted on Edison's settlement package, might have influenced settlement negotiations.

However, the Commission did not mandate that the parties reach settlement. In fact, in reaffirming footnote 4 of the July ACR[6], the Commission stated that its affirmation

> "does not mean that, in our assessment of litigation risk, we believe that all bidders designated by SDG&E as 'winning bidders' are somehow legally entitled to receive their reliance interest. Rather, we view such payment as equitable, in light of the time and resources these particular bidders have committed to the lengthy and contentious Update proceeding, which has not yet terminated, as well as their cooperation in engaging in this settlement process as directed by the July ACR." (D.98-12-074 at pp. 16-17.)

The Commission made clear in D.98-12-074 that no bidder is entitled, either legally or equitably, to receive remuneration. It found SDG&E's offered settlement package reasonable on equitable grounds. Thus, equitable considerations permitted us to find SDG&E's settlement package reasonable, but do not mandate remuneration for other nonsettling bidders.

### C. Termination of SDG&E's Update Solicitation is in the Public Interest

The regulatory climate has changed substantially since 1993, as have the figures and assumptions underlying SDG&E's Update solicitation. The time has come to reach finality in this proceeding so that the Commission and parties'

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[6] The July ACR defined the settlement outcome of a "buyout" as "a settlement which makes an otherwise winning bidder whole for reasonable bid preparation costs or reliance costs." (July ACR at p. 8.) The Assigned Commissioner elaborated in footnote 4 that he would personally view with disfavor buyout contracts that pay QFs more than their bid preparation or reliance interest by approximating their expectation interest. (July ACR at p. 9.)

efforts can be spent on the much broader issues of current capacity and resource needs. (See *e.g.* Rulemaking 01-10-024.)

It would not be in the public interest nor would it benefit ratepayers to direct SDG&E to negotiate a settlement with the nonsettling bidders to meet California's current energy needs at this time. For example, because FERC declared that the Commission's implementation of the Update violated PURPA,[7] and also because the Commission directed the utilities to renegotiate contracts to address unanticipated bidding strategies and ordered further hearings with respect to the wind bidders, the process of renegotiating a FSO4 contract might be necessarily lengthy, create uncertainty, and might never reach conclusion. Assuming a successful renegotiation, it is unclear that any prices resulting therefrom would be competitive in today's market.

We decline to adopt PG&E NEG and Kenetech's recommendation that we interject ourselves into the settlement process by engaging in fact-finding to determine the bidders' reasonable bid preparation or reliance costs, and then mandate that SDG&E settle for these costs. PG&E NEG and Kenetech are not entitled to such remuneration. If the parties are unable to voluntarily resolve their differences in a timely manner, we decline to adopt new rules and

[7] In D.95-03-018, 59 CPUC2d at 53, we stated our understanding that the FERC order was advisory, citing *Industrial Cogenerators v. FERC*, 47 F.3d 1231, 1235. (D.C. Cir. 1995). *Industrial Cogenerators v. FERC* also analogized that such an order was much like a memorandum of law prepared by the FERC staff in anticipation of a possible enforcement action, and could play a role in a subsequent enforcement action brought in district court. (*Id.*)

procedures to force them to do so.[8] In fact, the July ACR anticipated voluntary settlements within a reasonable period of time when it recognized that settlements in the ratepayers' interest may not be achievable with every wining bidder.

The Commission has not adopted the criteria advanced by PG&E NEG and Kenetech and we reject the invitation to do so here. Furthermore, assuming for the sake of argument that such an inquiry is relevant, Kenetech's claim that SDG&E failed to negotiate in good faith is belied by the fact that Kenetech states that it is now willing to accept a number of settlement offers that SDG&E made prior to the issuance of D.98-12-074, and which, in exercise of its business judgment, Kenetech did not timely accept. (See Joint Reply Brief of Kenetech and PG&E NEG at p.p. 4-5.) That statement is an admission that SDG&E has in fact negotiated in good faith, because it made settlement offers which are now acceptable to Kenetech. In D.98-12-074, we did not require that SDG&E resume negotiations by renewing its prior offers and the fact that the utility did not do so does not demonstrate that SDG&E resumed negotiations in bad faith. For example, the utility could have believed that renewing such an offer would not

[8] We also affirm the ALJ's ruling denying PG&E NEG and Kenetech's motion that the Commission mandate the parties to engage in binding arbitration. The Update solicitation did not contain such an arbitration procedure to address claims of these "winning bidders" and we decline to impose one after the fact. We do not mandate mediation because mediation requires that both parties to submit to the process voluntarily.

be in the utility or ratepayers' best interest under the criteria we established in D.98-12-074.[9]

PG&E NEG and Kenetech also urge the Commission to interject itself in the settlement process because terminating SDG&E's Update solicitation now could engender litigation both against SDG&E and the Commission. The July ACR recognized the value to ratepayers of settlements that eliminate the potential for litigation flowing from the Update proceeding. In D.98-12-074, we found SDG&E's settlements reasonable, in part, because it achieved this goal with respect to the settling bidders. (*Id.* at p. 17.)

However, as stated above, the July ACR recognized that settlements in the ratepayers' interest may not be achievable with every "wining bidder", and neither PG&E NEG nor Kenetech demonstrate how merely being designated as a "winning bidder" granted them a FSO4 contract or afforded them the right to compel SDG&E to enter into such a contract in the wake of the Commission's stay of the solicitation. In fact, SDG&E points out the Commission decisions and its own RFB limited the extent to which bidders reasonably could rely on preliminary rankings, preliminary final rankings, and final rankings.[10]

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[9] For instance, in D.98-12-074, we stated that we will judge any remaining settlements presented by SDG&E as reasonable at the time they are entered into, and not at the time the July ACR issued. (*Id.* at p. 21.)

[10] Ordering Paragraph 4(k) of D.93-06-099, 50 CPUC2d 264, 303 modified D.93-03-020 Conclusion of Law 18 to provide: "As part of the QF's acceptance of binding arbitration, the QF should agree to hold the utilities harmless from liability for any reliance a bidder places on a preliminary ranking." [The Commission approved arbitration process was not available to "winning bidders."] When SDG&E published its preliminary rankings and preliminary final rankings, it warned bidders not to take actions in reliance on the ranking results, and that the notices did not create a contract. SDG&E's January 30, 1995 Final Ranking included similar warnings.

*Footnote continued on next page*

Furthermore, SDG&E's RFB Section V.G.2(a) at p. 22, provides that bidders "who are both preliminary Final Winning Bidders and Final Winning Bidders … have no right to raise any claim against SDG&E … in any forum," and specifically prohibits a third party from raising a claim on behalf of a bidder, as PG&E NEG does here on behalf of Fellows. (*Id.*)

In summary, we grant SDG&E's request to terminate its 1993 Update solicitation as being in the public interest. We deny SDG&E's motion to strike portions of PG&E NEG and Kenetech's brief.

## IV. Comments to the Draft Decision

The draft decision of ALJ Econome in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7.

## Findings of Fact

1. The July ACR encouraged, but did mandate, settlements. The ACR did not require that the utilities' settlement package contain a settlement with all "winning bidders."

2. D.98-12-074, which approved as reasonable SDG&E's package of settlements with three "winning bidders" did not add a new requirement to the July ACR mandating the utility settle with all "winning bidders." In D.98-12-074, the Commission stated its agreement with ORA and SDG&E that the July ACR did not mandate settlement with every bidder no matter what the cost.

3. Equitable considerations permitted us to find SDG&E's settlement package reasonable, but do not mandate remuneration for other nonsettling bidders.

4. The regulatory climate has changed substantially since 1993, as have the figures and assumptions underlying SDG&E's Update solicitation.

5. It would not be in the public interest nor would it benefit ratepayers to direct SDG&E to negotiate a settlement with the nonsettling bidders to meet California's current energy needs at this time.

6. If the parties are unable to voluntarily resolve their differences in a timely manner, we decline to adopt new rules and procedures to force them to do so.

7. The July ACR anticipated voluntary settlements within a reasonable period of time when it recognized that settlements in the ratepayers' interest may not be achievable with every winning bidder.

8. Commission decisions and SDG&E's own RFB limited the extent to which bidders reasonably could rely on preliminary rankings, preliminary final rankings, and final rankings. SDG&E's RFB Section V.G.2(a) at p. 22, provides that bidders "who are both preliminary Final Winning Bidders and Final Winning Bidders … have no right to raise any claim against SDG&E … in any forum," and specifically prohibits a third party from raising a claim on behalf of a bidder, as PG&E NEG does here on behalf of Fellows.

## Conclusions of Law

1. SDG&E's request to terminate its 1993 Update solicitation should be granted as being in the public interest.

2. SDG&E's motion to strike portions of PG&E NEG and Kenetech's brief is denied.

3. The ALJ's ruling denying PG&E NEG and Kenetech's motion that the Commission mandate the parties to engage in binding arbitration should be affirmed.

4. In light of the determinations made in this decision, the limited rehearing ordered in D.94-12-051 should be cancelled with respect to SDG&E and all effective megawatts in SDG&E's Update solicitation.

5. This order should be effective immediately in order to bring finality to SDG&E's Update solicitation.

## O R D E R

**IT IS ORDERED** that:

1. San Diego Gas & Electric Company's (SDG&E) request to terminate its 1993 Update solicitation is granted.

2. In light of the determinations made in this decision, the limited rehearing ordered in Decision 94-12-051 is cancelled with respect to SDG&E and all effective megawatts in SDG&E's solicitation.

3. This proceeding is closed.

This order is effective today.

Dated _____, at San Francisco, California.