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PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

E-7 ID#2423

ENERGY DIVISION **RESOLUTION E-3833**

July 10, 2003

R E S O L U T I O N

Resolution E-3833. Southern California Edison Company (SCE) requests approval of its proposed Gas Supply Plan for the State of California Department of Water Resources (DWR) Tolling Agreements. SCE's request is approved with modifications.

By Advice Letter 1701-E filed on April 18, 2003.

SUMMARY

This resolution approves with modifications Southern California Edison Company's (SCE) Gas Supply Plan filed with Advice Letter (AL) 1701-E.

SCE filed AL 1701-E on April 18, 2003, requesting Commission approval of a Gas Supply Plan (GSP) for its DWR Tolling Agreements Pursuant to Decision (D.) 03-04-029 and D.02-12-069. The proposed Gas Supply Plan[1] was confidentially filed as Appendix A to AL 1701-E because it contains Confidential Protected Material subject to the protections in the May 1, 2002, Protective Order issued in Order Instituting Rulemaking (OIR) 01-10-024, and pursuant to Public Utilities Code Section 583 and General Order 66C.

On May 21, 2003, SCE filed additional "Substitute Sheets for 1701-E" which amounted to a revised copy of the Gas Supply Plan from that submitted on April 18th and 21st. The May 21, 2003 version of the Gas Supply Plan includes certain "editorial corrections to the original Appendix A" which are itemized in the transmittal letter.

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[1] SCE's proposed Gas Supply Plan was slightly revised and resubmitted on both April 21, 2003 as a "Substitute Sheet for 1701-E" and on May 21, 2003 as additional "Substitute Sheets for 1701-E." The latter version represents SCE's most current proposed Gas Supply Plan.

SCE requested that its Gas Supply Plan become effective upon filing (April 18, 2003), subject to review and approval by the Commission's Energy Division. SCE's Gas Supply Plan is effective today.

AL 1701-E was protested on April 28, 2003 by the Office of Ratepayer Advocates (ORA), the Cogeneration Association of California (CAC), and DWR,[2] although DWR requested more review time. On May 2, 2003, SCE filed both a public and a confidential response to the three protests. Also on May 2, 2003, DWR submitted both a redacted and a confidential memo in which DWR set forth its "initial concerns" (DWR Supplemental Protest) with SCE's proposed Gas Supply Plan. On May 9, 2003, SCE filed both a redacted and a confidential response to DWR's May 2, 2003 memo.

Issues raised by ORA include disagreement over proposed gas transaction term limits, terms over which portfolio risk is calculated, and criteria used to evaluate individual contracts. CAC would have the Commission reject SCE's entire Gas Supply Plan because it was filed under seal. The redacted version of DWR's Supplemental Protest did not present any specific issues. However, DWR's confidential Supplemental Protest sets forth a number of specific concerns. DWR states its intent to develop and implement the "DWR Fuels Protocols in the form of instructions from principal to agent."[3] DWR considers SCE's proposed transaction strategy too vague and overly broad."[4] In addition, DWR lists some concerns with SCE's market assessment, and requests a consultation finding from the Commission per the Rate Agreement.[5]

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[2] DWR's April 28, 2003 protest addressed both the San Diego Gas & Electric Company & SCE Gas Supply Plans respectively submitted in SDG&E AL 1489-E and SCE AL 1701-E.

[3] DWR Supplemental Protest, Comment Item 1, page 1.

[4] Id., Comment Item 23, page 7.

[5] D.02-02-051 adopted a Rate Agreement between the Commission and DWR to facilitate DWR's issuance of the bonds to repay more than $10 billion of debt that DWR incurred to finance power purchases during the electricity crisis, including more than $6 billion owed to the State's General Fund. The Rate Agreement terminates when the bonds and associated financial obligations have been paid or otherwise provided for.

SCE's proposed Gas Supply Plan is modified with language proposed by DWR, as accepted by SCE, as set forth in SCE's May 9, 2003 public response to DWR's Supplemental Protest at pages 17-18.

The protests of CAC and ORA are denied.

We would like the utilities managing DWR contracts to file their proposed gas supply plans 45 days prior to the requested effective date. The next filing date will be August 15, 2003.

D.03-04-029 recommended that SCE circulate a proposed Gas Supply Plan to its Procurement Review Group (PRG) for review and comment. SCE circulated unredacted copies of its proposed Gas Supply Plan, and subsequent submittals, to its PRG concurrently with its filings to the Commission.

BACKGROUND

In D.02-09-053 (the Contract Allocation Order), the Commission allocated thirty-five long-term DWR contracts with twenty-four counterparties to SCE, Pacific Gas and Electric Company (PG&E), and San Diego Gas and Electric Company (SDG&E).[6] SCE was allocated nine of the thirty-five DWR contracts, four of which have gas tolling provisions and are the subject of SCE AL 1701-E.

The Contract Allocation Order determined that the three utilities shall assume operational responsibility for the contracts and are required to:

> "…perform all of the day-to-day scheduling, dispatch and administrative functions for the DWR contracts allocated to their portfolios, just as they will perform those functions for their existing resources and new procurements. Legal title, financial reporting and responsibility for the payment of contract-related bills will remain with DWR."
> (D.02-09-053, page 5)

[6] To view the public, redacted copies of all original, and renegotiated DWR contracts, see the DWR website, www.cers.water.ca.gov/contracts.html.

In D.02-12-069 (the Operating Order decision), the Commission adopted the Operating Order under which the three utilities "will perform the operational, dispatch, and administrative functions for the DWR Contracts as of January 1, 2003,"[7] given that the utilities and DWR were unable, at that point, to negotiate such an agreement on their own. The Operating Order decision found that the relationship[8] between the utilities and DWR is accurately characterized as that of principal (DWR) and limited agent (each utility), in which DWR has the following authority:

> "Assume legal and financial responsibility, and approve Utility's entering into transactions as DWR's limited agent, for the purchase (or sale, as the case may be) of gas, gas transmission services, gas storage services and financial hedges, and timely consent to Utility's performance of the operational and administrative responsibilities for such purchases under gas tolling provisions under the Allocated Contracts , including the review of fuel plans and consideration of alternative fuel supply, all as more specifically provided in the Fuel Management Protocols attached hereto as Exhibit B;" (D.02-12-069 , Attachment A, SCE Operating Order, Section 5.01b)

In addition, D.02-12-069 broadly outlined DWR's prospective responsibilities regarding the DWR contracts assigned to the utilities:

> "In sum, as of January 1, 2003, DWR will: 1) retain legal and financial responsibility for the DWR contracts, 2) remain responsible for calculating the DWR revenue requirement and for submitting revenue requirements to the Commission, and 3) continue to service the bonds as issuer. DWR's responsibilities do not extend to conducting a reasonableness review of the utilities' portfolio dispatch decisions. That responsibility rests with the Commission." (D.02-12-069, page 14)

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[7] D.02-12-069, page 2.

[8] "We find that the "limited agency" definition appropriately reflects the nature of the capacity in which the utilities will be operating under this order. It is reasonable to require the utilities to act as a "limited agent" of DWR for the purposes of complying with the Operating Order." (D.02-12-069, Finding of Fact 4)

The purpose of the Gas Supply Plan was set forth in D.02-12-069 (the Operating Order):

> "The utilities are responsible for preparing "Gas Supply Plans" detailing their strategies for procuring gas and proposed use of risk management instruments. These plans will set parameters under which the utilities will perform the various gas-related activities pursuant to the gas tolling provisions. The utilities shall file these plans for Commission approval through Advice Letter filings on a semi-annual basis. The Commission will review and approve these plans on an expedited basis. Following approval of the Gas Supply Plans, the utilities will negotiate with suppliers for gas supplies, transportation, and storage. Negotiated agreements will then be submitted to DWR for execution." (D.02-12-069, page 27)

On April 3, 2003, the Commission issued D.03-04-029 (the Operating Agreements decision) which, among other things, provided a concise overview of the operating agreement process between each of the three utilities and DWR:

> "In D.02-09-053, the Commission directed the utilities to negotiate an operating agreement addressing contract administration services with DWR and jointly file such agreement with the Commission. D.02-12-069 was issued by the Commission as an "Operating Order" after concluding that the utilities had not succeeded in reaching an agreement with DWR. D.02-12-069 allowed the utilities to continue negotiating with DWR to attempt to reach consensus on a mutually acceptable operating agreement, stating:
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> > "We understand that DWR believes there is a realistic possibility that such an Operating Agreement can be worked out with the utilities through continued negotiations and we continue to support these efforts. The utilities may continue to negotiate with DWR to attempt to reach consensus on a mutually acceptable Operating Agreement. If such an agreement is reached, the utilities should submit the agreement to the Commission for approval and request termination of the Operating Order. Assuming that the agreement is substantially similar to the Operating Order we adopt today, we anticipate that it could be approved on an

> expedited basis, after the necessary public review and comment."

PG&E and SDG&E have submitted Operating Agreements for Commission approval via advice letter.[9] However, SCE still opts to be governed by the Operating Order with respect to DWR contract administration.[10] With regard to the Gas Supply Plans, the Commission stated that it will attempt to resolve any conflicting Commission-DWR mandates. However, the Commission determined that the utilities are to operate within Commission-defined boundaries, yet also adhere to specific DWR requirements:

> "In response to SCE's concerns regarding how the Commission intends to resolve any conflicts between what the Commission approves and what DWR is willing to implement, we note that we expect the utilities to prepare and file comprehensive Gas Supply Plans describing their proposed methods of meeting gas supply needs. The Commission will approve or disapprove these methods and plans. We expect DWR to file comments on the utilities' Advice Letter filings as necessary to identify any concerns they may have regarding the plans. These concerns will be taken into account in the Commission's decision, however, <u>in the event that DWR only authorizes a subset of what the Commission has approved, the utilities must operate within the limitations of DWR's approval. Similarly, if the Commission rejects portions of the Gas Supply Plans that DWR would otherwise authorize, we expect the utilities to operate within the limitations of the Commission's decision.</u>
> (D.03-04-029, pages 24-25, emphasis added)

The Commission also noted the similar but differing objectives of the Commission and DWR:

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[9] Submission of Executed Operating Agreements for Commission review and approval: PG&E Advice Letter 2374-E filed on April 17, 2003, and SDG&E Advice Letter 1490-E filed on April 17, 2003.

[10] "SCE has not yet negotiated an Operating Agreement with DWR so the Operating Order will continue to govern SCE's actions in administering the DWR contracts allocated to SCE by D.02-09-053." (D.03-04-029, page 19)

> "Although the Commission's and DWR's objectives are very closely aligned, it is not reasonable to expect their objectives to be perfectly aligned due to the fact that the Commission and DWR have differing jurisdictions and responsibilities. For example, DWR is in the best position to determine the level of credit support available for utility purchases under the gas tolling agreements, and the Commission will not second-guess DWR's determination in this regard. We request that DWR provide written notification to the Commission regarding its approval or rejection of the utilities' Gas Supply Plans. (D.03-04-029, pages 24-25)

D.03-04-029 required the three utilities the file their respective Gas Supply Plans on April 17, 2003. SCE requested, and was granted, a one-day extension and filed SCE AL 1701-E on April 18, 2003. On April 21, 2003, SCE filed a "Substitute Sheet for 1701-E" which contained a slightly revised copy of the Gas Supply Plan submitted on April 18, 2003. Both copies of the Gas Supply Plan are the same, except that the April 21, 2003 copy added "confidentiality language that was inadvertently omitted from Appendix A" when first filed on April 18, 2003. Also on April 21, 2003, SCE filed "Supporting Workpapers" for AL 1701-E. The workpapers, on computer diskette, consisted of hourly forecasts of power prices and gas prices for the period May 1, 2003 through December 31, 2007.

D.03-04-029 also directed the utilities to circulate unredacted copies of their proposed gas supply plans to their Procurement Review Groups (PRGs) for review and comment.[11] The Commission originally established PRGs in D.02-08-071 in order "to ensure that interim procurement contracts entered into by the utilities [were] subject to sufficient and expedited review and pre-approval" by the Commission.[12] Individual PRGs are not parties to any proceeding. Instead, PRGs are intended to act in an advisory fashion regarding the respective utilities' confidential procurement plans and activities.

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[11] "In addition, in the interest of minimizing protests on the initial Advice Letter filings, we recommend that the utilities provide advance, unredacted copies of the Gas Supply Plans to the "Procurement Review Groups" identified in D.02-08-071 for review and discussion. We also recommend that utilities file advance copies with DWR." (D.03-04-029, page 24)

[12] D.0-08-071, page 24.

NOTICE

Notice of AL 1701-E was made by publication in the Commission's Daily Calendar. Southern California Edison states that a copy of the Advice Letter was mailed and distributed in accordance with Section III-G of General Order 96-A.

PROTESTS

SCE's Advice Letter AL 1701-E was timely protested on April 28, 2003 by the Office of Ratepayer Advocates (ORA), the Cogeneration Association of California (CAC), and the California Department of Water Resources (DWR)[13] although DWR requested more review time. On May 2, 2003, SCE filed both a public and a confidential response to the three protests. Also on May 2, 2003, DWR submitted both a redacted and a confidential memo that set forth DWR's specific concerns ("DWR Supplemental Protest") with SCE's proposed Gas Supply Plan. On May 9, 2003, SCE filed both a redacted and a confidential response to DWR's May 2, 2003 memo. On May 21, 2003, SCE filed additional "Substitute Sheets for 1701-E" which amounted to a revised copy of the Gas Supply Plan from that submitted on April 18, 2003. The May 21, 2003 version of the Gas Supply Plan includes certain "editorial corrections to the original Appendix A" which are itemized in the transmittal letter.

The following is a more detailed summary of the major issues raised in the protests. CAC would have the Commission reject SCE's entire Gas Supply Plan because it was filed under seal. The redacted version of DWR's Supplemental Protest did not present any specific issues. However, DWR's confidential Supplemental Protest sets forth a number of specific concerns where DWR states its intent to develop and implement the "DWR Fuels Protocols in the form of instructions from principal to agent."[14] DWR considers SCE's proposed transaction strategy too general because it provides SCE with maximum flexibility. DWR would prefer, instead, to see more specific procurement

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[13] DWR's April 28, 2003 protest addressed both the San Diego Gas & Electric Company Gas Supply Plan submitted in SDG&E AL 1489-E and SCE AL 1701-E.

[14] DWR Supplemental Protest, Comment Item 1.

strategies.[15] In addition, DWR has some concerns with SCE's market assessment, and requests a consultation finding from the Commission per the Rate Agreement.

In the interest of clarity, and due to its brevity, ORA's protest is essentially shown here in its entirety:

> "Based on its review, ORA supports Commission approval of SCE's plan with the following modifications:
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> 1. "Natural gas transactions should not be subject to a five-year limit. Rather, they should be limited only be (sic) the length of the relevant CDWR contract."
> 2. "The calculation of portfolio risk should not be limited to a two-year period. Instead, portfolio risk should be calculated over the length of the longest DWR contract."
> 3. "Estimates of portfolio risk should not be used to evaluate individual contracts as SCE suggests. Instead, a less prospective approach should be used."
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> "SCE proposes (page iii) that it 'will perform an analysis that demonstrates that the prospective transaction reduces the risk of the combined SCE/DWR portfolio before recommending that DWR execute that transaction.' In other words, no contract will be recommended that does not reduce portfolio risk as measured by SCE."
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> "SCE's portfolio risk will be estimated with some error as will the effect on overall portfolio risk of a specific contract. Thus, a contract may be rejected because it increases the estimate of portfolio risk when the contract might actually decrease portfolio risk. Even if a given contract leads to an increase (on average) of portfolio risk, it might offer excellent protection during months in which natural gas prices are high even though it might offer poor protection in other months and on average increase portfolio risk." (ORA Protest, page 1)

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[15] Id., Comment Item 23.

In its May 2, 2003 response to protests, SCE stated that CAC's request (to reject SCE's entire GSP because it was filed under seal) exceeds the scope of this compliance filings review process, and that such concerns relating to QF contract costs could not legally be resolved through issuance of a resolution. With regard to ORA, SCE stated that it was willing to accept the first ORA recommendation on transaction term limits, but noted that to do so would exceed the term of the GSP. SCE did not accept the other two ORA recommendations regarding calculation of portfolio risk and contract evaluation.

In its May 9, 2003 response to DWR's Supplemental Protest, SCE proposed to accept a subset of DWR's recommendations. SCE accepts the proposed DWR Protocols, as long as they do not conflict with Commission decisions and orders.

DISCUSSION

In order to properly evaluate SCE's request for approval of its proposed Gas Supply Plan, the relationship between, and the scope of authority of, the Commission, DWR, and SCE must first be clearly understood. The Commission has the authority to review and approve SCE's Gas Supply Plan. DWR has the right, as the principal over SCE as its limited agent, to impose certain operational and administrative requirements associated with the tolling agreements. As noted above, the Commission has already determined in D.03-04-029 that SCE must operate within the subset approved by both the Commission and DWR.

We recognize that the SCE is bound by both the gas supply plan as well as the approval of DWR, and that DWR is at liberty to impose additional restrictions and requirements outside the scope of the gas supply plan.

With regard to conflicts, SCE stated its intent to seek guidance from the Commission and DWR as to how SCE should proceed in the event of a conflict between a Commission-approved GSP and specific DWR requirements.[16] SCE requests that the Commission clarify what course of conduct SCE should take during the interim period of time before the Commission and DWR resolve any conflict that may arise. SCE suggests two possibilities:

[16] SCE May 9, 2003 public response to DWR's Supplemental Protest, page 4.

1. SCE can perform under the conflicting DWR guidelines established in its Protocols, until the Commission resolves the conflict; or

2. SCE can refrain from acting at all until the Commission resolves the conflict, during which time DWR, as the principal, can act on its own behalf.

The Commission is not inclined to require either of the two exclusive possibilities at this time. In the event of a conflict, SCE shall consult with its PRG. If the conflict is not resolved, SCE may file an advice letter or application for expedited consideration.

DWR Protest

In its May 2, 2003 Supplemental Protest, DWR proposed a number of detailed modifications to SCE's gas supply plan. In response, SCE proposed to accept some of the DWR recommendations in its May 9, 2003 public filing while also countering certain DWR recommendations with alternative language. This sort of negotiation can be expected between principal (DWR) and agent (SCE) and may result in a number of back-and-forth exchanges on various issues. It is clear that SCE is willing to accept the DWR Protocols:

> "In its comments, DWR states that it intends to develop and provide Protocols to SCE at some unspecified later date. The Protocols will serve as instructions from DWR, as principal, to SCE, as its limited agent. The DWR Protocols, which DWR may from time to time in its sole discretion revise, will control all transactions of SCE as its limited agent, and will serve as the standard against which DWR will evaluate such transactions. SCE recognizes and accepts its legal and equitable obligations to DWR when it acts as its limited agent." (SCE May 9, 2003 Public Response to DWR Supplemental Protest, page 3)

However, DWR has expressed concern that SCE's proposed GSP procurement strategies are too general and inappropriately allow SCE "maximum flexibility." Instead, DWR would prefer more specific procurement strategies. SCE responds that a Commission-approved GSP should be sufficiently broad to encompass more restrictive conditions imposed by DWR through its Protocols. We are inclined to agree on this point and prefer to avoid having to issue subsequent

decisions or resolutions relaxing overly restrictive requirements that may unnecessarily conflict with DWR.

The Commission is not adopting DWR's Fuels Protocols as part of the utilities' Gas Supply Plan approval process. DWR has informed the Commission that it will provide the Commission a final copy of its Fuels Protocols once they are complete. To the extent that DWR's Fuels Protocols only authorize a subset of what the Commission has approved, the utilities must operate within the limitations of DWR's authorization.

SCE's proposed Gas Supply Plan is modified with language proposed by DWR, as accepted by SCE in its May 9, 2003 public response to DWR's Supplemental Protest at pages 17-18, and as further modified as requested by DWR in its July 3, 2003 comments on the draft resolution:

- Modify DWR's Proposed Additional Language in Comment No. 1, Subsection 1(b) as follows:

  "Transactions made pursuant to the parameters set forth in the Protocols shall be reviewed by DWR for compliance with the Protocols. Further, confirmations of all gas transactions entered into on behalf of DWR shall continue to be presented to and signed by DWR."
- Delete DWR's Proposed Additional Subsection 1(g).
- Modify DWR's Proposed Additional Language in Comment No. 6 as follows:

  "SCE will conduct the reconciliation of gas invoices for DWR gas activities (e.g. purchases, sales, storage and transportation. All approved invoices and necessary verification documentation shall be forwarded to DWR in accordance with the provisions of the Operating Order no later than five (5) business days prior to the due date of the invoice. Further, all rejected invoices, along with explanation as to why SCE recommends rejecting the invoice shall be sent to DWR no later than five (5) business days prior to the due date of the invoice."

CAC and ORA Protests

The Cogeneration Association of California (CAC) would have the Commission reject SCE's entire Gas Supply Plan because it was filed under seal. In its response to protests, SCE states that CAC's request "exceeds the scope of a review process for compliance advice filings [and that] a protest to a compliance filing is not the appropriate forum for consideration of complex issues concerning QF contract costs which could not legally be resolved through issuance of a resolution." SCE also contends that it "properly filed its Gas Supply Plan as a confidential document[17] since the plan contains confidential information on gas procurement strategies that could be used by market participants to their advantage and to the disadvantage of ratepayers." (SCE Response to Protests, page 2).

While SDG&E filed both a confidential and a public, redacted version of its gas supply plan, SCE and PG&E filed confidential gas supply plans with the Commission.[18] Although it is appropriate to file certain information under seal, it is not necessary to redact the entire plan. Accordingly, we direct SCE in this resolution to file both confidential and redacted versions of its gas supply plan in future submittals. At this point in time, we will not adopt CAC's protest.

ORA made the following recommendations in its protest, which is shown almost in its entirety in the Protests section of this resolution:

1. "Natural gas transactions should not be subject to a five-year limit. Rather, they should be limited only be (sic) the length of the relevant CDWR contract."
2. "The calculation of portfolio risk should not be limited to a two-year period. Instead, portfolio risk should be calculated over the length of the longest DWR contract."
3. "Estimates of portfolio risk should not be used to evaluate individual contracts as SCE suggests. Instead, a less prospective approach should

[17] SCE's GSP Advice Letter contains Confidential Protected Material subject to the protections in the May 1, 2002, Protective Order issued in R.01-10-024, and pursuant to Public Utilities Code Section 583 and General Order 66C.

[18] PG&E filed AL 2359-E on March 25, 2003, and SDG&E filed AL on April 17, 2003.

be used." (ORA Protest, page 1)

Although SCE's response to ORA's protest was completely redacted, it can be stated that SCE is willing to accept ORA's first recommendation, but would reject the other two. ORA's first recommendation would effectively extend the term of SCE's gas supply plan well beyond its five-year term. SCE correctly noted that the liquidity for gas supply and hedging instruments is significantly less for products with a term greater than five years. Given such uncertainty, we see no compelling reason to extend the term of SCE's gas supply plan.

ORA's second recommendation, that "portfolio risk should be calculated over the length of the longest DWR contract," may not be practical for two reasons, as SCE notes in its response to protests: (1) the GSP has a five-year term, and (2) liquidity for gas supply and hedging instruments is significantly less for products with a term greater than five years. In addition, ORA does not provide a specific citation to SCE's GSP that sets forth such a two-year limit. SCE does not appear to propose it. For these reasons, we will not adopt ORA's recommendation.

ORA's third recommendation, that "a less prospective approach (something other than estimates of portfolio risk) should be used to evaluate individual contracts," is ambiguous. On this point, the ORA protest states:

> "SCE proposes (page iii) that it 'will perform an analysis that demonstrates that the prospective transaction reduces the risk of the combined SCE/DWR portfolio before recommending that DWR execute that transaction.' In other words, no contract will be recommended that does not reduce portfolio risk as measured by SCE."
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> "SCE's portfolio risk will be estimated with some error as will the effect on overall portfolio risk of a specific contract. Thus, a contract may be rejected because it increases the estimate of portfolio risk when the contract might actually decrease portfolio risk. Even if a given contract leads to an increase (on average) of portfolio risk, it might offer excellent protection during months in which natural gas prices are high even though it might offer poor protection in other months and on average increase portfolio risk." (ORA Protest, page 1)

As SCE notes in its response to protests, although ORA expresses concern with SCE's proposal on this point, ORA offers no alternative. Given ORA's incomplete recommendation, we will not adopt it at this time.

Gas Storage

Although filed under seal, it can be stated that SCE has arranged for some gas storage capacity on behalf of DWR as its limited agent. In future filings, we would like to see detailed cost data associated with the awarded storage.

The Commission is very concerned about the upward trend in natural gas prices, and the increasing volatility in natural gas prices. One of the reasons for these high prices and increasing volatility is the low level of natural gas in storage nationally. The lack of natural gas in storage by noncore customers was one of the contributing factors to high natural gas prices in California in 2000-2001. We believe that storage should be considered for use by the state's electric utilities as a hedge against high natural gas prices, particularly during the summer. The use of storage may be beneficial not only for a particular utility's customers, but for the state as a whole. It may help to lower the volume of flowing supplies that will be purchased during the summer, and thus help keep prices in check for the state as a whole.

At this point in time, we are already well into the summer, and we do not have an adequate record to determine in this resolution what would be an appropriate amount of storage for this summer. Nor do we have adequate information to say exactly how much storage capacity should be obtained. However, we will order SCE and the other electric utilities to prepare a proposal for their next Gas Supply Plans, due August 15, 2003, for possibly obtaining natural gas storage capacity as of April 1, 2004. This should include a proposal for minimum storage targets as of May 31, 2004.

Consumer Risk Tolerance (CRT)

In D.02-12-074, the Commission introduced the concept of the Consumer Risk Tolerance (CRT). On June 19, 2003, the Commission issued D.03-06-067 which clarified the application of the CRT which gave "SCE the flexibility to enter longer term forward energy, gas, and other procurement hedges that are necessary to serve expected load, mitigate anticipated power conditions, and/or take advantage of cost-effective market opportunities" (D.03-06-067, page 17).

In its proposed gas supply plan, SCE states that it does not intend to apply the CRT to its GSP. As we understand it, PG&E and SDG&E will, in contrast, apply the CRT to their respective GSPs. We see no compelling reason to allow SCE different treatment on this point. Accordingly, the CRT is applicable to SCE's gas supply plan. More precisely, gas supply plans should meet all standards in adopted procurement plans.

With regard to SCE's gas supply plan and the CRT, we would like to see a comparison of the countervailing risks of being caught short if the market price skyrockets, and the risks of being caught long if the market price plummets. The concept of the CRT introduced by the Commission addresses only one of these risk types. The CRT is designed to ensure a highly predictable payment stream, and to protect the utility and its customers from price spikes. If this were the only concern, then the utility could meet its obligations by purchasing all of its supplies through forward contracts, with some storage to adapt to the daily and seasonal peaks and valleys in demand. However, utilities and their customers are also concerned about being stuck with a fixed long term purchase obligation in the event that the market price drops and they will be precluded from taking advantage of cheaper supplies. The GSP contains no discussion of the tradeoffs between these kinds of risks, and we would like to see this analysis better developed in future GSP filings.

Gas Supply Plans Filed

SCE filed three versions of its proposed Gas Supply Plan, all substantively the same. The most current plan was submitted on May 21, 2003. On April 21, 2003, SCE filed a "Substitute Sheet for 1701-E" which contained a slightly revised copy of the Gas Supply Plan submitted on April 18, 2003. Both copies of the Gas Supply Plan are the same, except that the April 21, 2003 copy added "confidentiality language that was inadvertently omitted from Appendix A" when first filed on April 18, 2003. Also on April 21, 2003, SCE filed "Supporting Workpapers" for AL 1701-E. The workpapers, on computer diskette, consisted of hourly forecasts of power prices and gas prices for the period May 1, 2003 through December 31, 2007. On May 21, 2003, SCE filed additional "Substitute Sheets for 1701-E" which amounted to a revised copy of the Gas Supply Plan from that submitted on April 18, 2003. The May 21, 2003 version of the Gas Supply Plan includes certain "editorial corrections to the original Appendix A" which are itemized in the transmittal letter.

It should be noted that when filing clarifications or modifications to an advice letter (as opposed to tariff sheets), utilities must submit supplemental advice letters per General Order 96-A, Part III, Section I, given that substitute sheets are specific to certain types of tariff sheet modifications, not modifications to advice letters, as specified in General Order 96-A, Part III, Section J.

Commission and DWR Consultation

DWR requests that Commission approval of SCE's Gas Supply Plan constitute "prior consultation"[19] between DWR and the Commission for purposes of complying with D.02-02-051, Appendix C, the Rate Agreement, Article 1, Section 1.1, Definitions, "Priority Long Term Power Contracts[20] (PLTPCs)." Finding of Fact 35 of D.02-02-051 states that "DWR shall consult with the Commission prior to entering into any additional contract for the purpose of securing fuel if that contract contains such a provision." We find DWR's request reasonable and will make the requested finding.

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[19] Id., Comment Item 7.

[20] *"Priority Long Term Power Contracts"* shall mean (i) those long-term electric power contracts identified in Appendix A, and shall not include any electric power contracts entered into after August 14, 2001; provided, however, that such term shall include any priority long term electric power contract entered into after August 14, 2001, as an amendment or novation of any Priority Long Term Power Contract and (ii) any contracts entered into for the purpose of securing fuel for use at generating facilities being operated pursuant to such Priority Long Term Power Contracts, if that fuel supply contract contains a provision to the general effect that payments by the Department under the contract are to be paid or payable prior to bonds, notes, or other indebtedness of the Department secured by a pledge or assignment of the revenues of the Department under the Act and other amounts in the Fund. The Department shall consult with the Commission prior to entering into any additional contract for the purpose of securing fuel if that contract contains such a provision. Contracts shall cease to be treated as Priority Long Term Power Contracts under the circumstances described in Section 7.8. (emphasis added)

Procurement Review Group (PRG) Review

D.03-04-029 recommended that SCE circulate a proposed Gas Supply Plan to its Procurement Review Group (PRG) for review and comment. SCE circulated unredacted copies of its proposed Gas Supply Plan, and subsequent submittals, to its PRG concurrently with its filings to the Commission.

The PRG for SCE comprises the California Energy Commission (CEC), California Utility Employees (CUE), Department of Water Resources (DWR), Energy Division, Office of Ratepayer Advocates (ORA), Natural Resources Defense Council (NRDC), and The Utility Reform Network (TURN).

The PRG met a number of times via conference call to discuss SCE's Short-Term Procurement Plans for 2003 and 2004, during which time SCE also discussed DWR contract gas supply plan issues. In particular, SCE's PRG convened on April 25, 2003.

COMMENTS

PU Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission.

Commission Rule 77.7 implements provisions of Public Utilities Code Section 311(g) for public review and comment by parties on Commission decisions and alternates. In the interest of public necessity[21] as set forth in Rule 77.7(f)(9), the Commission may reduce or waive the 30-day period for public review and comment for draft decisions (and resolutions) and may

[21] "Public necessity" includes, without limitation, circumstances where failure to adopt a decision before expiration of the 30-day review and comment period would place the Commission or a Commission regulatee in violation of applicable law, or where such failure would cause significant harm to public health or welfare. When acting pursuant to this subsection, the Commission will provide such reduced period for public review and comment as is consistent with the public necessity requiring reduction or waiver. Rule 77.7(f)(9), in part.

reduce, but not waive, the public review and comment period for alternates.

In D.03-04-029, the Commission found that the "initial Utility Gas Supply Plans should be subject to expedited Commission review and approval."

Comment Period on Draft Resolution E-3833

On June 24, 2003, the Energy Division circulated draft resolution E-3833 for public comment to parties in SCE AL 1701-E. The draft resolution was also circulated via email on June 25, 2003 to SCE's Procurement Review Group (PRG). Comments were due on Thursday, July 3, 2003. Reply comments were due on Tuesday, July 8, 2003. Comments were filed by SCE and DWR. Reply comments were filed only by DWR.

On July 2, 2003, DWR emailed separate draft Fuels Protocols for SCE, PG&E, and SDG&E to the Energy Division. DWR indicated that these were non-public documents. The same day, Energy Division circulated draft Fuels Protocols specific to SCE via email to the SCE PRG. No feedback was received on the draft Fuels Protocols specific to SCE from the SCE PRG.

SCE had two comments on draft Resolution E-3833:

- "The Commission should clarify what course of conduct SCE should take during the interim period of time before the Commission and DWR resolve any conflict that may arise between the Commission-approved GSP and specific DWR requirements."
- "The Commission should require SCE to file its next GSP on October 17, 2003, and not on August 15, 2003." (SCE Comments, page 2)

In its comments on the draft resolution,[22] DWR suggested that the Commission should consider "adopting uniform language in the Resolutions adopting the GSPs" (DWR Comments, page 1). In its July 8, 2003 reply comments regarding

[22] The DWR comments addressed all three draft Gas Supply Plan (GSP) resolutions: E-3825 on the PG&E GSP, E-3833 on the SCE GSP, and E-3838 on the SDG&E GSP.

draft resolution E-3833, DWR essentially reiterated points already made in its comments.

The draft resolution has been modified in response to comments and reply comment, specifically, (1) to recognize that the SCE is bound by both the gas supply plan as well as the approval of DWR, and that DWR is at liberty to impose additional restrictions and requirements outside the scope of the gas supply plan; (2) to adopt DWR's proposed language regarding the Fuels Protocols as shown below, and (3) to require five business days to validate gas invoices, instead of two.

The following language in the draft resolution at page 11 as circulated on June 24, 2003 has been deleted:

> "We recommend that DWR file any draft and final "Fuel Protocols" as further supplemental comments to SCE AL 1701-E and provide, at least via email, a redacted copy on the R.01-10-024 service list, and an unredacted copy to the SCE PRG. Alternatively, DWR and SCE could opt to include the Fuel Protocols in the next gas supply plan filing."

DWR's proposed language regarding the Fuels Protocols has been added to the resolution as noted above:

> "The Commission is not adopting DWR's Fuels Protocols as part of the utilities' Gas Supply Plan approval process. DWR has informed the Commission that it will provide the Commission a final copy of its Fuels Protocols once they are complete. To the extent that DWR's Fuels Protocols only authorize a subset of what the Commission has approved, the utilities must operate within the limitations of DWR's authorization." (DWR Comments, page 2)

The draft resolution has also been modified to require that all gas supply plans meet all standards in adopted procurement plans. Findings 10, 12, 13, and 19 are added, along with Order 5.

FINDINGS

1. D.03-04-029 directed PG&E, SDG&E, and SCE to file initial Gas Supply Plans on April 17, 2003 and subsequent gas supply plans every six months thereafter for the term of the Operating Agreements / Order.

2. SCE filed AL 1701-E on April 18, 2003 requesting approval of its proposed Gas Supply Plan for the State of California Department of Water Resources (DWR) Tolling Agreements, pursuant to D.03-04-029 and D.02-12-069.

3. On April 21, 2003, SCE filed a "Substitute Sheet for 1701-E" which contained a slightly revised copy of the Gas Supply Plan submitted on April 18, 2003. Both copies of the Gas Supply Plan are the same, except that the April 21, 2003 copy added "confidentiality language that was inadvertently omitted from Appendix A" when first filed on April 18, 2003.

4. Also on April 21, 2003, SCE filed "Supporting Workpapers" for AL 1701-E. The workpapers, on computer diskette, consisted of hourly forecasts of power prices and gas prices for the period May 1, 2003 through December 31, 2007.

5. AL 1701-E was timely protested by ORA, CAC, and DWR on April 28, 2003, although DWR requested more review time.

6. On May 2, 2003, SCE filed both a public and a confidential response to the protests of ORA, CAC, and DWR.

7. Also on May 2, 2003, DWR submitted both a redacted and a confidential memo which set forth DWR's specific concerns ("DWR Supplemental Protest") with SCE's proposed Gas Supply Plan.

8. On May 9, 2003, SCE filed both a redacted and a confidential response to DWR's May 2, 2003 memo regarding SCE's proposed Gas Supply Plan.

9. On May 21, 2003, SCE filed additional "Substitute Sheets for 1701-E" which amounted to a revised copy of the Gas Supply Plan from that submitted on April 18, 2003. The May 21, 2003 version of the Gas Supply Plan includes certain "editorial corrections to the original Appendix A" which are itemized in the transmittal letter.

10. On July 2, 2003, DWR emailed separate draft Fuels Protocols for SCE, PG&E, and SDG&E to the Energy Division. DWR indicated that these were non-public documents.

11. D.03-04-029 found that "…in the event that DWR only authorizes a subset of what the Commission has approved, the utilities must operate within the limitations of DWR's approval. Similarly, if the Commission rejects portions of the Gas Supply Plans that DWR would otherwise authorize, we expect the utilities to operate within the limitations of the Commission's decision."

12. We recognize that the SCE is bound by both the gas supply plan as well as the approval of DWR, and that DWR is at liberty to impose additional restrictions and requirements outside the scope of the gas supply plan.

13. The Commission is not adopting DWR's Fuels Protocols as part of the utilities' Gas Supply Plan approval process. DWR has informed the Commission that it will provide the Commission a final copy of its Fuels Protocols once they are complete. To the extent that DWR's Fuels Protocols only authorize a subset of what the Commission has approved, the utilities must operate within the limitations of DWR's authorization.

14. SCE's proposed Gas Supply Plan should be modified with language proposed by DWR, as accepted by SCE in SCE's May 9, 2003 public response to DWR's Supplemental Protest at pages 17-18.

15. We decline to accept any provisions of either the CAC or the ORA protests.

16. D.03-04-029 recommended that SCE circulate a proposed Gas Supply Plan to its Procurement Review Group (PRG) for review and comment, which SCE did do.

17. We require SCE to file cost data associated with awarded storage in future gas supply plan filings.

18. The Consumer Risk Tolerance (CRT) is applicable to SCE's gas supply plan.

19. Gas supply plans should meet all standards in adopted procurement plans.

20. With regard to the Consumer Risk Tolerance (CRT) and future gas supply plan filings, we require SCE to present a comparison of the countervailing risks presented by short positions with skyrocketing market prices in relation to the CRT, as compared with the risks of long positions with plummeting market prices in relation to the CRT, specifically, discussing the tradeoffs between these two general risks scenarios.

21. When filing clarifications or modifications to an advice letter (as opposed to tariff sheets), utilities must submit supplemental advice letters per General Order 96-A, Part III, Section I, given that substitute sheets are specific to certain types of tariff sheet modifications, not modifications to advice letters, as specified in General Order 96-A, Part III, Section J.

22. DWR requests that Commission approval of SCE's Gas Supply Plan constitutes "prior consultation" between DWR and the Commission for purposes of complying with D.02-02-051, Appendix C, the Rate Agreement, Article 1, Section 1.1, Definitions, "Priority Long Term Power Contracts."

23. SCE should file its next Gas Supply Plan on August 15, 2003, for the period October 2003 through March 2004.

THEREFORE IT IS ORDERED THAT:

1. The request of Southern California Edison Company for approval of the proposed Gas Supply Plan for the State of California Department of Water Resources (DWR) Tolling Agreements, pursuant to D.03-04-029 and D.02-12-069 as submitted in Advice Letter 1701-E, is approved, as modified.

2. SCE's proposed Gas Supply Plan is modified with language proposed by DWR, as accepted by SCE, as set forth in SCE's May 9, 2003 public response to DWR's Supplemental Protest at pages 17-18.

3. Commission approval of SCE's Gas Supply Plan constitutes "prior consultation" between DWR and the Commission for purposes of complying with D.02-02-051, Appendix C, the Rate Agreement, Article 1, Section 1.1, Definitions, "Priority Long Term Power Contracts."

4. The protests of CAC and ORA are denied.

5. Gas supply plans shall meet all standards in adopted procurement plans.

6. SCE shall re-file its modified Gas Supply Plan with a supplemental advice letter within 10 days.

7. SCE shall file its next Gas Supply Plan on August 15, 2003, for the period October 2003 through March 2004.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on July 10, 2003; the following Commissioners voting favorably thereon:

_____
WILLIAM AHERN
Executive Director