



Memorandum

Date: September 24, 2015

To: Edward Randolph
Director of Energy Division

From: **Public Utilities Commission—
San Francisco**

Kayode Kajopaiye, Branch Chief
Division of Water and Audits

A handwritten signature in black ink, appearing to be "Kajopaiye".

Subject: Pacific Gas and Electric Company Advice Letter 4626-E
Quarterly Procurement Plan Compliance Report for the First Quarter of 2015

Based on the results of its audit, the Utility Audit, Finance and Compliance Branch (UAFCB), of the Division of Water and Audits, did not find any material reasons for Energy Division (ED) to deny the approval of Pacific Gas and Electric Company's (PG&E) Advice Letter No. (AL) 4626-E. The procurement transactions that PG&E executed during the first quarter of 2015 (Q1), that UAFCB examined, demonstrated, in all material respects, compliance with certain aspects of procurement-related state law and California Public Utilities Commission (Commission or CPUC) directives. The UAFCB assesses compliance in accordance with agreed-upon procedures with ED and does not assess compliance with all aspects of the procurement-related state law or those directives. In addition, PG&E's transactions conducted in the Integrated Forward Market (IFM) and the Residual Unit Commitment Market (RUC) are outside the scope of UAFCB's audits.

A. Summary of Negative Audit Findings:

UAFCB is unaware of any specific requirements established by the Commission regarding how PG&E should seek and obtain approval from the Commission for amendments to contracts that are originally approved through Quarterly Compliance Report (QCR) review processes, specifically an amendment to a Combined Heat and Power (CHP) contract that is less than five years in duration. In Q1, PG&E executed an amendment that made changes to a CHP contract without going through the QCR review process. The original contract was approved through the first quarter of 2014 QCR process. PG&E filed the executed amendment for information purposes only in its Q1 QCR and sought recovery for the costs associated with the executed amendment via its 2015 Energy Resource Recovery Account (ERRA) review proceeding.

B. Recommendation:

The Commission should provide guidance and establish procedures regarding how the Investor-Owned-Utilities (IOU) should seek approval from the Commission for contract amendments where the original agreements were approved through the QCR review process.

C. Background:

As required by D.02-10-062, Ordering Paragraph (OP) 8 and clarified in D.03-12-062, PG&E, San Diego Gas and Electric (SDG&E), and Southern California Edison (SCE) must each submit a QCR for all transactions of less than five years duration executed in the quarter. ED requested that the UAFCB conduct compliance audits of these utilities' QCR filings.

UAFCB conducts the quarterly procurement audits based on procedures specified by ED. As such these examinations are by design agreed-upon procedures. Per agreement with ED, UAFCB does not test all of the transactions that the utilities include in their QCR. In addition, ED specified which aspects of the utilities' Commission-approved procurement plans, AB 57 procurement rules and several procurement-related rulings and decisions to test for compliance. The decisions and rulings that ED chose directives from to test for compliance include, but are not limited to, D.02-10-062, D.03-06-076, D.03-12-062, D.04-12-048, D.07-12-052, D.08-11-008, and D.12-01-033.

D. Findings:

UAFCB is unaware of any specific guidelines and requirements established by the Commission regarding how PG&E should seek approval from the Commission for contract amendments where the original contracts were approved through the QCR review processes and where the amendments materially change the terms of the original contracts. If the Commission does not have a review and approval process for amendments to contracts approved through the QCR review process, it should establish guidelines and directives.

During Q1, without Commission review and approval, PG&E entered into an amendment to its Ripon Cogeneration, LLC (Ripon) Combined Heat and Power (CHP) contract. The original Ripon CHP contract was executed during the first quarter of 2014. Because the term of the Ripon CHP contract is less than five years, PG&E sought and acquired the Commission's approval for the original contract via PG&E's first quarter of 2014 QCR filing process.

Instead of following the Commission's directives applicable to the approval of contracts in accordance with Public Utilities Code (PUC) §454.5, PG&E reported the amendment to the Ripon CHP contract in its Q1 QCR as filed for information purposes only and is seeking a Commission finding that the amendment is reasonable for cost recovery after the fact via the 2015 ERRA proceeding.

PG&E's Response:

PG&E indicated:

PG&E disagrees with the assertion that the Ripon Cogeneration, LLC ("Ripon") routine amendment was improperly submitted as an "Informational Purposes Only" transaction in the QCR with approval to be sought through the 2015 ERRA Compliance Filing. PG&E believes that this assertion is in direct contravention with D.02-10-062 and D.06-12-009, which will be described more fully below. Based on this, PG&E does not believe that it is necessary to amend Attachment H to request approval of the Ripon routine amendment through the QCR.

D.02-10-062 established the basic parameters for the QCR. Appendix B, "Adopted Master Data Request for Monthly Advice Letters," lists the material to be included in the QCR and this material is listed in the current QCR filing. The list, however, does not make any mention of amendments or the necessity of their inclusion in the QCR. PG&E disagrees that it is out of compliance with D.02-10-062 Appendix B, when D.02-10-062 Appendix B does not address amendments.

Moreover, Commission rules require that PG&E seek approval for amendments in a forum other than the QCR. In D.06-12-009, the Commission ordered, "PG&E shall file a

separate advice letter, or include in that annual ERRA reasonableness applications, an approval request for contract amendments and modifications.” Ordering Paragraph 3, p. 13

In its discussion section of D.06-12-009 the Commission expanded on its order. The Commission stated:

“However, the PTQCR is not the appropriate vehicle for requesting approval of contract amendments and modifications. The PTQCR is a compliance filing that explains a why and how a utility enters into a contract. As such, the PTQCR is not an appropriate vehicle for an approval request. The PTQCR serves a specific purpose as defined in D.04-10-062, Conclusion of Law 7. That purpose is not compatible with a request for contract modifications. PG&E should file a separate advice letter when seeking Commission approval for contract amendments and modifications. The requirement that PG&E not use the PTQCR for contract approval request is not intended to limit or hinder PG&E’s management from exercising their discretion in managing the procurement contracts on a day-to-day basis. Nor is PG&E prevented from filing pre-approval requests via an application or a separate advice letter as deemed appropriate by PG&E management.”

“Previously, the annual ERRA reasonableness application process was used to seek approval of contract amendments and modifications, and we do not object to its continued use for such purpose. (D.06-12-009 at pp. 8-9)”

The auditors have asserted that this language only applies to Qualifying Facility (“QF”) contracts. This belief appears to be centered around the fact that the amendments in question related to D.06-12-009 were all QF amendments, but nowhere in the language above is there language that restricts the decision to QF amendments. Also, at the time this decision was issued, PG&E’s portfolio contained a much higher percentage of QF contracts than it does today, which explains why the amendments were related to QF contracts, but it does not limit the applicability of this language. Further, the Commission appeared to contemplate that this requirement is not solely related to QF contracts when it stated that “the requirement ... is not intended to limit or hinder PG&E ... in managing the procurement contracts on a day-to-day basis.” If the intent were to limit the applicability to QF contracts, the Commission would not have referenced “procurement” contracts.

PG&E has been submitting contracts for approval through the QCR since 2002. In compliance with the Commission’s direction in D.06-12-009, PG&E has not submitted an amendment for approval through the QCR, even when the initial contract was filed for approval through the QCR. PG&E believes that it is still in compliance with D.06-12-009 and that the approval for amendments is properly sought through Advice Letter or the ERRA Compliance filing. PG&E also has concerns that this change in filing requirement is out of scope for the QCR, that other parties who would normally review PG&E’s ERRA Compliance filing are not included in this discussion, and that this is not the appropriate forum in which to address this issue.

UAFCB's Rebuttal:

The Commission should establish specific and effective procedures requiring PG&E, SCE and SDG&E to seek approval for contract amendments where the original contracts were reviewed and approved via QCR review processes.

UAFCB believes that:

1. Contract amendments, where the original contracts are approved via a QCR process, should be reviewed for compliance with the utilities' bundled procurement plan (BPP) approved by the Commission.
2. Consistency of the review and approval processes between the original contracts and any associated amendments can increase the Commission's oversight effectiveness for energy procurement.

E. Conclusion:

Except for the item noted in Section D above, PG&E's AL 4626-E and its Q1 procurement transactions for electricity and natural gas that the UAFCB examined were, in material respects, in compliance with the aspects of PG&E's Commission-approved procurement plan and relevant Commission decisions that the UAFCB tested compliance with. PG&E's Q1 transactions that the UAFCB examined, in material respects, appear to be complete, accurate and properly authorized by its management.

If you have any questions on UAFCB's audit, please contact Tracy Fok at (415) 703-3122.

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