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July 15, 2005

**Advice 2685-E**  
(Pacific Gas and Electric Company ID U 39 E)

Public Utilities Commission of the State of California

**Subject: Pacific Gas and Electric Company (PG&E)'s Electric Portfolio Gas Hedging Plan**

PG&E hereby submits for approval its electric portfolio gas hedging plan to the California Public Utilities Commission (Commission or CPUC). This filing provides the Commission with the strategy that PG&E will use to manage the gas open position associated with PG&E's electric procurement portfolio in a manner that is complementary to PG&E's approved procurement plan (Decision (D.) 04-12-048) and future California Department of Water Resources (CDWR) Gas Supply Plans. PG&E submits this plan as a result of increasing natural gas price exposure in its electric portfolio due to the transition from fixed energy to variable gas-indexed pricing for a substantial amount of its Qualifying Facility (QF) contracts. Therefore, PG&E requests that the Commission approve its strategy to manage the gas exposure identified in this advice letter by the end of September 2005 in order to allow for implementation in 2005.

### **Background and Purpose**

Decision 04-12-048 approved PG&E's procurement plan and authorized PG&E to request changes to its procurement plan through an advice letter.<sup>1</sup> While PG&E's currently approved procurement plan allows for flexibility to execute electricity and gas hedges out as far as five years, a more formal and detailed gas hedging framework and strategy is provided in this filing. This framework is necessary because the natural gas exposure in PG&E's electric portfolio is expected to increase with the expiration of QF contract amendments that are currently receiving fixed energy prices for five years at 5.37 cents per kilowatt-hour. A substantial amount of PG&E's Qualifying Facility (QF) contracts are covered by these amendments. Following expiration of the fixed energy prices, the QF contracts (including renewables) will revert to a variable priced structure

<sup>1</sup> Finding of Fact 106 of D.04-12-048 states that "...Updates or modifications to the [long-term] plans in between the biennial review will be filed with an advice letter." Ordering Paragraph 1 of the same decision permits PG&E to update its long-term procurement plan to reflect any material changes in its procurement activities. PG&E also notes that it would not be required to submit an expedited application seeking plan modifications unless PG&E's estimated risk exceeded 125% of the customer risk tolerance (p.16 of D.03-12-062).

where the energy price is tied to the index price of gas and a fixed heat rate. The size of this gas position component will dramatically increase from the current notional amount by summer 2006.

Thus, PG&E, through this advice letter, presents a strategy to manage the risks associated with gas price exposure in its electric portfolio.

### **PG&E's Gas Hedging Plan**

PG&E developed the gas hedging plan (further discussed in Confidential Attachment 1) to be consistent and easily integrated with PG&E's approved short-term and long-term procurement plans. In addition, the plan is strategically and methodologically consistent with PG&E's upcoming Gas Supply Plan (GSP) 6 for CDWR Tolling Agreements due to the Commission on August 1, 2005. PG&E also designed the plan to serve as a framework for CPUC compliance review in the quarterly and yearly Energy Resource Recovery Account (ERRA) filings. PG&E expects that its hedging activities found in compliance with this gas hedging plan and its procurement plans would be fully recovered through its ERRA account.

Similar to the electric operating targets already included in PG&E's Short-Term Procurement Plan approved by the Commission in December 2003 (D.03-12-062), PG&E proposes a set of gas financial operating targets intended to guide management of its gas open position. This plan should reduce the exposure of the portfolio to fluctuations in gas prices and manage To Expiration Value at Risk (TeVaR) within Procurement Review Group (PRG) and Commission notification levels. PG&E proposes a multi-year time horizon for these gas operating targets and a set of target percentages to guide hedge volumes. PG&E also proposes a mix of hedging products (forward and options) that will be set prior to each phase of gas hedging in consultation with PG&E's Procurement Review Group (PRG).

Finally, PG&E proposes a phased execution schedule where hedge volumes are adjusted, product mix is reviewed and set, and the major hedging phases are executed several times a year. In the periods between phases, PG&E will monitor its hedge positions and adjust them to stay within target ranges. While the Commission reviews this plan, PG&E is continuing to implement a second phase of the interim hedging strategy that it discussed with its PRG in February, March and April of this year (the CDWR portion of the strategy was submitted through GSP-5 Supplement in PG&E's Advice 2620-E-A on June 16, 2005).

Upon Commission approval of this plan, PG&E, in consultation with its PRG regarding hedging strategies, will implement the gas hedging framework, the operating targets, and other strategies as described in this plan. Therefore, PG&E requests CPUC approval of this electric portfolio gas hedging plan for incorporation with PG&E's short-term and long-term generation procurement plans by the end of September 2005 so that PG&E can begin implementing the plan.

**Protest Period**

Anyone wishing to protest this filing may do so by sending a letter by **August 4, 2005**, which is 20 days from the date of this filing. The protest must state the grounds upon which it is based, including such items as financial and service impact, and should be submitted expeditiously. Protests should be mailed to:

IMC Branch Chief – Energy Division  
California Public Utilities Commission  
505 Van Ness Avenue, 4<sup>th</sup> Floor  
San Francisco, California 94102  
Facsimile: (415) 703-2200  
E-mail: [jjr@cpuc.ca.gov](mailto:jjr@cpuc.ca.gov) and [jnj@cpuc.ca.gov](mailto:jnj@cpuc.ca.gov)

Protests also should be sent by e-mail and facsimile to Mr. Jerry Royer, Energy Division, as shown above, and by U.S. mail to Mr. Royer at the above address. The protest should be sent via both e-mail and facsimile to PG&E on the same date it is mailed or delivered to the Commission at the address shown below.

Pacific Gas and Electric Company  
Attention: Brian K. Cherry  
Director, Regulatory Relations  
77 Beale Street, Mail Code B10C  
P.O. Box 770000  
San Francisco, California 94177  
Facsimile: (415) 973-7226  
E-mail: [PGETariffs@pge.com](mailto:PGETariffs@pge.com)

**Effective Date**

PG&E is requesting that the Commission approve this advice letter through a resolution **on or prior to the CPUC's September 22, 2005, business meeting** so that PG&E can begin implementing the plan in 2005.

**Notice**

In accordance with General Order 96-A, Section III, Paragraph G, a copy of this advice letter excluding the confidential appendices is being sent electronically and via U.S. mail to parties shown on the attached list and the service list for Rulemaking (R.) 01-10-024, R. 04-04-003. Address change requests should be directed to Rose De La Torre at (415) 973-4716 (RxDd@pge.com). Advice letter filings can also be accessed electronically at:

<http://www.pge.com/tariffs/>

Handwritten signature of Brian K. Cheng in black ink.

Director - Regulatory Relations

cc: Service List - R. 01-10-024, R.04-04-003

**Attachments**

Confidential Attachment 1 – PG&E Electric Portfolio Gas Hedging Plan

# CALIFORNIA PUBLIC UTILITIES COMMISSION

## ADVICE LETTER FILING SUMMARY ENERGY UTILITY

**MUST BE COMPLETED BY UTILITY (Attach additional pages as needed)**

Company name/CPUC Utility No. **Pacific Gas and Electric Company (ID U39)**

Utility type:

ELC       GAS  
 PLC       HEAT     WATER

Contact Person: Bernard Lam

Phone #: (415) 973-4878

E-mail: bxlc@pge.com

### EXPLANATION OF UTILITY TYPE

ELC = Electric      GAS = Gas  
PLC = Pipeline     HEAT = Heat      WATER = Water

(Date Filed/ Received Stamp by CPUC)

Advice Letter (AL) #: **2685-E**

Subject of AL: PG&E's Electric Portfolio Gas Hedging Plan

Keywords (choose from CPUC listing): Procurement, Portfolio

AL filing type:  Monthly  Quarterly  Annual  One-Time  Other \_\_\_\_\_

If AL filed in compliance with a Commission order, indicate relevant Decision/Resolution #:

Decision 04-12-048

Does AL replace a withdrawn or rejected AL? If so, identify the prior AL: N/A

Summarize differences between the AL and the prior withdrawn or rejected AL<sup>1</sup>: \_\_\_\_\_

Resolution Required?  Yes  No

Requested effective date: 09/22/2005 or prior

No. of tariff sheets: 0

Estimated system annual revenue effect: (%):

Estimated system average rate effect (%):

When rates are affected by AL, include attachment in AL showing average rate effects on customer classes (residential, small commercial, large C/I, agricultural, lighting).

Tariff schedules affected: N/A

Service affected and changes proposed<sup>1</sup>: N/A

Pending advice letters that revise the same tariff sheets: N/A

**Protests and all other correspondence regarding this AL are due no later than 20 days after the date of this filing, unless otherwise authorized by the Commission, and shall be sent to:**

**CPUC, Energy Division  
Attention: Tariff Unit  
505 Van Ness Ave.,  
San Francisco, CA 94102  
jjr@cpuc.ca.gov and inj@cpuc.ca.gov**

**Pacific Gas and Electric Company  
Attn: Brian K. Cherry  
Director, Regulatory Relations  
77 Beale Street, Mail Code B10C  
P.O. Box 770000  
San Francisco, CA 94177  
E-mail: PGETariffs@pge.com**

<sup>1</sup> Discuss in AL if more space is needed.

**PG&E Gas and Electric Advice  
Filing List  
General Order 96-A, Section III(G)**

ABAG Power Pool  
Accent Energy  
Aglet Consumer Alliance  
Agnews Developmental Center  
Ahmed, Ali  
Alcantar & Elsesser  
Anderson Donovan & Poole P.C.  
Applied Power Technologies  
APS Energy Services Co Inc  
Arter & Hadden LLP  
Avista Corp  
Barkovich & Yap, Inc.  
BART  
Bartle Wells Associates  
Blue Ridge Gas  
Bohannon Development Co  
BP Energy Company  
Braun & Associates  
C & H Sugar Co.  
CA Bldg Industry Association  
CA Cotton Ginners & Growers Assoc.  
CA League of Food Processors  
CA Water Service Group  
California Energy Commission  
California Farm Bureau Federation  
California Gas Acquisition Svcs  
California ISO  
Calpine  
Calpine Corp  
Calpine Gilroy Cogen  
Cambridge Energy Research Assoc  
Cameron McKenna  
Cardinal Cogen  
Cellnet Data Systems  
Chevron USA Production Co.  
Childress, David A.  
City of Glendale  
City of Healdsburg  
City of Palo Alto  
City of Redding  
CLECA Law Office  
Constellation New Energy  
Cooperative Community Energy  
CPUC  
Creative Technology  
Cross Border Inc  
Crossborder Inc  
CSC Energy Services  
Davis, Wright Tremaine LLP  
Davis, Wright, Tremaine, LLP  
Defense Fuel Support Center  
Department of the Army  
Department of Water & Power City

DGS Natural Gas Services  
DMM Customer Services  
Douglass & Liddell  
Downey, Brand, Seymour & Rohwer  
Duke Energy  
Duke Energy North America  
Duncan, Virgil E.  
Dutcher, John  
Dynegy Inc.  
Ellison Schneider  
Energy Law Group LLP  
Energy Management Services, LLC  
Enron Energy Services  
Exelon Energy Ohio, Inc  
Exeter Associates  
Foster Farms  
Foster, Wheeler, Martinez  
Franciscan Mobilehome  
Future Resources Associates, Inc  
G. A. Krause & Assoc  
Gas Transmission Northwest Corporation  
GLJ Energy Publications  
Goodin, MacBride, Squeri, Schlotz &  
Hanna & Morton  
Heeg, Peggy A.  
Hitachi Global Storage Technologies  
Hogan Manufacturing, Inc  
House, Lon  
Imperial Irrigation District  
Integrated Utility Consulting Group  
International Power Technology  
Interstate Gas Services, Inc.  
J. R. Wood, Inc  
JTM, Inc  
Kaiser Cement Corp  
Korea Elec Power Corp  
Luce, Forward, Hamilton & Scripps  
Marcus, David  
Masonite Corporation  
Matthew V. Brady & Associates  
Maynor, Donald H.  
McKenzie & Assoc  
McKenzie & Associates  
Meek, Daniel W.  
Mirant California, LLC  
Modesto Irrigation Dist  
Morrison & Foerster  
Morse Richard Weisenmiller & Assoc.  
Navigant Consulting  
New United Motor Mfg, Inc  
Norris & Wong Associates  
North Coast Solar Resources  
Northern California Power Agency

Office of Energy Assessments  
Palo Alto Muni Utilities  
PG&E National Energy Group  
Pinnacle CNG Company  
PITCO  
Piurimi, Inc.  
PPL EnergyPlus, LLC  
Praxair, Inc.  
Price, Roy  
Product Development Dept  
R. M. Hairston & Company  
R. W. Beck & Associates  
Recon Research  
Regional Cogeneration Service  
RMC Lonestar  
Sacramento Municipal Utility District  
SCD Energy Solutions  
Seattle City Light  
Sempra  
Sempra Energy  
Sequoia Union HS Dist  
SESCO  
Sierra Pacific Power Company  
Silicon Valley Power  
Simpson Paper Company  
Smurfit Stone Container Corp  
Southern California Edison  
SPURR  
St. Paul Assoc  
Stanford University  
Sutherland, Asbill & Brennan  
Tabora Caramanis & Associates  
Tansev and Associates  
Tecogen, Inc  
TFS Energy  
Transwestern Pipeline Co  
Turlock Irrigation District  
U S Borax, Inc  
United Cogen Inc.  
URM Groups  
Utility Cost Management LLC  
Utility Resource Network  
Wellhead Electric Company  
Western Hub Properties, LLC  
White & Case  
WMA