

October 22, 2002

Advice 2293-E

(Pacific Gas and Electric Company ID U 39 E)

Public Utilities Commission of the State of California

Subject: Transitional Procurement Contracts

Pacific Gas and Electric Company (PG&E) hereby submits for Commission review and approval, through the advice letter process outlined in Decision (D.) 02-08-071, Appendix B, several contracts for the procurement of capacity and energy during the period of 2003 through 2005.¹ Until PG&E regains its investment-grade credit rating and is able to assume all rights and obligations as specified under each contract, the California Department of Water Resources (DWR) will serve as the creditworthy purchaser for the products received under these contracts and the costs of these contracts will be included in DWR's revenue requirement.²

All attachments to this advice letter comprise Confidential Protected Material, in accordance with the May 1, 2002, Protective Order issued in Rulemaking (R.) 01-10-024, and pursuant to Public Utilities Code Section 583.

PG&E will submit separate advice letters for the Commission's review and approval of renewables resources selected as part of the renewables Request for Offers (RFO) and Standard Offer 1 (SO1) contract extensions it may enter into pursuant to D. 02-08-071.

Purpose

Ordering Paragraphs (OP) 3 and 4 of D. 02-08-071 require PG&E to submit any contract under which it is seeking pre-approval under the decision to be filed by advice letter within 30 days of signing or selection. Under the accelerated advice letter process set forth in Appendix B of D. 02-08-071, PG&E asks that the

¹ PG&E reserves all legal rights to challenge the decisions or statutes under which it has been required to make this filing, and nothing in this filing constitutes a waiver of such rights, including its rights to seek relief in federal court for violations of federal law or the U.S. Constitution. See *England v. Louisiana State Board of Medical Examiners*, 375 U.S. 411 (1964). In addition, PG&E reserves any additional legal rights by reason of its status as a debtor under Chapter 11 of the U.S. Bankruptcy Code, and nothing in this filing constitutes a waiver of such rights.

² The Conditions Subsequent of each contract provide for DWR to sign separate contracts for these products with the suppliers.

Commission issue a resolution no later than November 21, 2002, approving the proposed contracts and finding that the contracts in Confidential Appendix A are reasonable and prudent for purposes of recovery in full in retail rates under the Public Utilities Code for the full term of the contract(s) without further Commission review.

Each of the contracts submitted by PG&E for Commission pre-approval contains provisions for a price refresher. Contract prices will be refreshed upon Commission approval of such contract(s).³ Because the prices are “refreshed,” there has been no payment of fees or premiums to keep the offer open. The methodology for pre-approving the refreshed bids is discussed in Confidential Appendix C.

Background

On August 22, 2002, the Commission issued D. 02-08-071 which, among other things, addressed the extent to which, if at all, PG&E, Southern California Edison (SCE) and San Diego Gas and Electric Company (SDG&E) should be permitted to immediately contract for a portion of their residual net short (RNS) in partnership with DWR.^{4, 5} The Commission authorized PG&E to enter into such contracts in partnership with DWR between August 22, 2002, (the effective date of the decision) and January 1, 2003, the expiration date of DWR’s authority to enter into new power contracts pursuant to Assembly Bill 1X.

As part of D. 02-08-071, the Commission also adopted a procedural process for the review and approval of these transitional procurement contracts. That procedural process is based on an accelerated advice letter process of approximately 30 days and includes upfront review of the utility’s overall transitional procurement strategy and specific proposed transitional procurement contracts and procurement process prior to the submission of the advice letter to the Commission. The upfront review is performed by the Procurement Review Group (PRG), whose membership comprises non-market participants who have executed non-disclosure certificates. Participants in PG&E’s PRG include members of the Commission’s Energy Division (ED) and Office of Ratepayer

³ PG&E will promptly file a motion in U.S. Bankruptcy Court for authority to enter into these contracts. PG&E expects its motion to be heard by Judge Montali on November 14, 2002.

⁴ The residual net short is the amount of energy needed to serve a utility customers’ needs net of existing resources, including those supplied by DWR.

⁵ The Commission limited the capacity portion of PG&E’s RNS that could be contracted for prior to the allocation of power available under DWR’s long-term contracts to the on-peak hourly RNS requirement based on a low estimate of PG&E’s RNS. On September 19, 2002, the Commission issued D. 02-09-053, allocating the energy available under DWR’s long-term contracts among the three utilities. On September 30, 2002, PG&E filed updated estimates of its RNS incorporating the DWR energy allocated to it in D. 02-09-053. While the Commission has not yet ruled on the actual amount of RNS contracting PG&E can perform during the transitional period, PG&E believes the energy delivered under the contracts for which PG&E is seeking approval through this advice letter are within the range envisioned by the Commission, as shown in Confidential Appendix D.

Advocates (ORA) staff, The Utility Reform Network (TURN), Natural Resources Defense Council (NRDC), California Energy Commission (CEC), Consumers' Union (CU), Aglet and California Utility Employees (CUE). DWR also participated in the PRG meetings, as well as in contract development and negotiations.

Description of Request for Offer (RFO) Solicitation Process

PG&E attempted to get the largest possible number of bids in the transitional procurement process. To develop its list of potential bidders, PG&E sought out all parties that it thought might be interested in participating in the RFO. PG&E contacted parties that are currently participating in the California market, as well as other potential participants. PG&E developed an initial list based on suppliers with whom it had contracted in the past. In addition, PG&E supplemented that list by contacting suppliers that had contracts with DWR, and also contacted suppliers that were listed as members of Western States Power Pool. PG&E also initiated contact with several utilities in the Northwest that it thought might have power available for seasonal exchanges. In addition, certain suppliers contacted PG&E after the issuance of D. 02-08-071 to express interest, and were subsequently added to the list of RFO recipients. PG&E also worked with industry groups including Independent Energy Producers (IEP), to identify additional potential suppliers, including smaller entities.

Prior to issuing the RFO, PG&E contacted suppliers to see if they would be willing and able to supply power under the draft RFO products. In order to develop products that are consistent with meeting PG&E's unmet needs and the current market, PG&E sought feedback from market participants on the draft RFO products, and modified the products to incorporate the feedback received.

PG&E e-mailed the general and renewables RFO to 151 market participants. PG&E's data indicates that 57 parties expressed interest in the general RFO. Twenty parties eventually submitted bids in the general RFO. PG&E received and evaluated 59 bids in the general RFO, totaling 6,764 MWs, although many of these bids were mutually exclusive bids from the same resources.

Bid Evaluation Process

All transactions that were received on September 30, 2002, were explicitly modeled, and a market value was calculated for each. The 59 distinct transactions resulting from the evaluation are presented in Confidential Appendix B – Relative Cost Effectiveness.

PG&E reviewed each of the confirmations and eliminated the specific transactions that did not meet certain commercial and non-commercial terms. These transactions and the reasons for elimination are included in Confidential Appendix B.

The first step of the evaluation process was to examine the behavior of the existing portfolio. PG&E examined the characteristics of the existing portfolio to determine its sensitivity to various risk drivers such as electric price, gas price, hydro conditions and variations to load. This led to the determination of which products to pursue.

Those transactions were evaluated and their value calculated under a wide range of scenarios. A short list of contracts which had higher market values, and higher benefit/cost ratios was selected. Those results demonstrate that the proposed transitional contracts provide a substantial benefit to ratepayers, and a significant hedge against adverse conditions. PG&E negotiated with the short list, which resulted in the contracts proposed in Confidential Appendix A.

Involvement of the Procurement Review Group (PRG)

PG&E's PRG met four times prior to the submission of this advice letter. The specific dates and minutes of those meetings are provided in Confidential Appendix E. PG&E first discussed the draft RFO products and sought PRG feedback before issuing the RFO. After issuing the RFO, PG&E discussed its residual net short, the types of products that could meet PG&E's RNS needs, and different ways to evaluate the benefits of the products that were bid. At PG&E's final meeting, PG&E presented its short list of offers it might accept and presented its cost/ benefit analysis. The cost-effectiveness results, included in Confidential Attachment B were presented to the PRG.

PG&E has shared its final recommendations with the PRG. Based on subsequent discussions with TURN, PG&E understands that it supports Commission approval of the attached contracts.⁶

Protests

Appendix B of D. 02-08-071 requires that protests to this advice letter be made within seven days of its filing. Accordingly, protests are due on or before **October 29, 2002**. Replies to protests should be filed within three days of the protest, or November 1, 2002. Because of the accelerated timeline provided for protests, PG&E asks that all protests be mailed electronically to RxDd@pge.com and the service list for R. 01-10-024.

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:

⁶ CEC, NRDC and CUE neither support nor oppose Commission approval of the contracts. ORA and Energy Division are not taking a position at this time.

IMC Branch Chief – Energy Division
California Public Utilities Commission
505 Van Ness Avenue, 4th Floor
San Francisco, California 94102

Facsimile: (415) 703-2200
E-mail: jjr@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: Les Guliasi
Director, Regulatory Relations
77 Beale Street, Mail Code B10C
P.O. Box 770000
San Francisco, California 94177

Facsimile: (415) 973-7226
E-mail: RxDd@pge.com

Effective Date

PG&E requests that this advice filing become effective on November 21, 2002.

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 R.01-10-024. Non-market participants who are members of PG&E's Procurement Review Group and have signed appropriate Non-Disclosure Certificates will also receive the advice letter and accompanying confidential attachments by overnight mail.

The portions of this advice letter so marked Confidential Protected Material are in accordance with the May 1, 2002, Protective Order in R. 01-10-024 Regarding Confidentiality of Pacific Gas and Electric Company (PG&E) Power Procurement Information. As required by that Order, reviewing representatives of Market Participating Parties will not be granted access to Protected Material, but will

instead be limited to reviewing redacted versions of documents that contain Protected Material.

Vice President – Regulatory Relations

Attachments –

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| Confidential Appendix A | - | Transitional Procurement Contracts for which PG&E Seeks Commission Approval |
| Confidential Appendix B | - | Responses to Adopted Master Data Request in Appendix C of D. 02-08-071 |
| | | <ul style="list-style-type: none">• Briefing Package provided to ultimate decision maker• Quantitative process used to rank offers• Relative cost-effectiveness of the offer• Break-even spot price equivalent to the contract• Electronic copy of data and forecasts used by the utility to analyze contracts included in Confidential Appendix A |
| Confidential Appendix C | - | Description of Price Refresher Formula |
| Confidential Appendix D | - | Authorized Low Case RNS and Amounts/Percentages met with Contracts provided in Confidential Appendix A |
| Confidential Appendix E | - | Procurement Review Group Minutes |