

Memorandum



Date: December 20, 2013
To: Edward Randolph
Director of Energy Division
From: **Public Utilities Commission—**
San Francisco Kayode Kajopaiye, Branch Chief
Division of Water and Audits
Subject: Southern California Edison Advice Letter 2928-E
Quarterly Procurement Plan Compliance Report for the Second Quarter of 2013

Based on the results of its audit, the Division of Water and Audits' Utility Audit, Finance and Compliance Branch (UAFCB) did not find any material reasons for Energy Division (ED) to deny the approval of Southern California Edison's (SCE) Advice Letter No. (AL) 2928-E. The SCE procurement transactions executed during the second quarter of 2013 (Q2) that UAFCB examined were, in all material respects, in compliance with SCE's Procurement Plan, as approved in Decision (D.) 12-01-033, Assembly Bill (AB) 57 procurement rules, and several procurement-related Commission directives. SCE's transactions conducted in the Integrated Forward Market (IFM) and the Residual Unit Commitment Market (RUC) are outside the scope of UAFCB's audits. This audit is limited in scope and does not provide full assurance to the reasonableness of SCE's Q2 Quarterly Compliance Report (QCR) filing or its Q2 transactions.

A. Negative Audit Finding:

SCE failed to demonstrate that it was in compliance with D.04-12-048, Ordering Paragraph (OP) 15. SCE failed to consult with its Procurement Review Group (PRG) before it executed a resource adequacy (RA) sale contract with Shell Energy North America (US) LP. This contract has a term greater than 90 days or three calendar months.

B. Recommendations:

SCE needs to consult with its PRG before it executes any contracts with terms greater than 90 days or three calendar months.

C. Background:

As required by D.02-10-062, OP 8, and clarified in D.03-12-062, Pacific Gas and Electric Company (PG&E), San Diego Gas and Electric Company (SDG&E) and SCE must each submit a quarterly compliance report (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' quarterly procurement compliance filings.

The objective of these quarterly audits is to determine if the utilities were in compliance with their California Public Utilities Commission's (Commission) approved procurement plans, while complying with AB 57 procurement rules and several procurement-related regulatory rulings and decisions, including, but 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. Negative Findings

Finding: SCE failed to demonstrate that it was in compliance with D.04-12-048, OP 15. In Q2, SCE executed a RA sale contract with Shell Energy North America (US) LP. The contract term of this contract is four months. During the PRG meeting dated May 15, 2013, SCE notified its PRG that it intended to sell its excess RA to Energy Service Providers (ESP). SCE, however, did not specifically present the counterparty, price, and term of the aforementioned contract to its PRG and did not consult with its PRG specifically on the contract.

Criteria: In D.04-12-048, OP 15, the Commission requires that utilities consult with the PRG for transactions with delivery periods greater than three calendar months, or one quarter.

SCE's Response: SCE asserts the following:

1. There is nothing in D.03-12-062 or D.04-12-048 requiring that the PRG consultation be "transaction-specific" or be conducted during the actual negotiating process prior to execution.
2. Page 37 of D.03-12-062 indicated that the Commission requires the utilities consult with their PRG for transactions greater than 90 days, but leaves to the utilities' discretion the exact process for approaching such procurement.
3. Page 39 of D.03-12-062 specifically excluded negotiated bilateral transactions from a more robust PRG consultation that the Commission prefers for Request for Offers (RFO) transactions because the negotiation process for the former typically does not afford the time for such a transaction-specific consultation.

UAFCB's Rebuttal: SCE's notification to the PRG during the May 15, 2013 PRG meeting regarding selling its excess RA capacity to an ESP does not follow the Commission's requirements indicated in D.04-12-048, OP 15. The Commission requires that utilities consult with the PRG for transactions with delivery periods greater than three calendar months, or one quarter. Clearly, the Commission intends that the utilities consult with the PRG for specific transactions. SCE's notification that took place during the May 15, 2013 PRG meeting did not mention the RA sale contract that it planned to execute with Shell Energy North America (US) LP in Q2.

In addition, PRG consultation should take place before contract execution. Informing the PRG about bilateral contracts after the fact is not a form of consultation but rather notification. Per Energy Division, if SCE had time constraints and could not timely conduct a PRG meeting to specifically discuss the aforementioned RA sale contract, SCE could e-mail its PRG members regarding the contract and solicit the PRG members' feedback prior to its contract execution. SCE should have communicated its negotiation status of the RA sale contract to its PRG members by e-mail during its negotiation process.

In D.03-12-062, the Commission indicated that Office of Ratepayer Advocates (ORA) requested that the Commission approve an eleven-step procurement process for use by PG&E, SCE and SDG&E. The process included three steps for the utilities to consult with their PRG specifically on transactions as shown below:

1. Share bids with PRG;
2. Evaluate candidate hedges and rank according to cost-benefit analysis; and
3. Meet with the PRG and solicit comments from PRG members and attempt to reach a consensus.

The Commission agreed with ORA that ORA's recommended eleven-step procurement process represented a prudent and common sense approach. The Commission does not explicitly require the utilities to follow the process for short-term transactions less than 90 days because the process is clearly too burdensome for these short-term transactions. For longer-term transactions beyond 90 days, however, the Commission indicated that it prefers that the utilities follow the ordered process. The Commission further indicated that it requires that the utilities consult with their PRG for transactions greater than 90 days, but leaves to the utilities' discretion the exact process for approaching such procurement. UAFCB determined that such utilities' discretion should not violate D.04-12-048, OP 15 which requires transaction-specific PRG consultation.

E. Conclusion:

SCE's AL 2928-E and its Q2 procurement transactions for electricity and natural gas that UAFCB reviewed were, in material respects, in compliance with SCE's Commission-approved procurement plan and all relevant Commission decisions. SCE's Q2 transactions that UAFCB reviewed, in material respects, appear to be complete, accurate and properly authorized by management.

If you have any questions, please contact Tracy Fok at (415) 703-3122.

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