

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION

RESOLUTION E-4088
May 24, 2007

R E S O L U T I O N

Resolution E-4088. San Diego Gas & Electric Company requests authority to establish a Market Redesign and Technology Upgrade (MRTU) Memorandum Account to record its incremental costs associated with the California Independent System Operator's MRTU initiative. Approved with modifications.

By SDG&E Advice Letter 1867-E filed on January 29, 2007.

SUMMARY

This Resolution approves the request by San Diego Gas & Electric Company (SDG&E) to establish a Market Redesign and Technology Upgrade (MRTU) Memorandum Account to record its incremental costs associated with the California Independent System Operator's (CAISO) MRTU initiative. SDG&E shall submit to Energy Division periodic cost estimates of the amounts it expects to record in the account prior to each MRTU release.

The MRTU Memorandum Account (MRTUMA) will record SDG&E's incremental capital-related revenue requirement as well as incremental operations and maintenance (O&M) expenses associated with implementing the CAISO's MRTU initiative. The CAISO has targeted MRTU Release 1 by February 2008 and MRTU Release 2 in 2009. SDG&E shall seek recovery of amounts recorded in the MRTUMA in Energy Resource Recovery Account (ERRA) reasonableness proceedings. SDG&E shall submit to the Energy Division 30 days prior to each MRTU release, its best estimate of the amounts it expects to record in the MRTUMA.

There were no protests to SDG&E Advice Letter (AL) 1867-E.

BACKGROUND

Since it was created in 1996, the CAISO has experienced several flaws in its management of the electricity market and transmission systems within its control that will be corrected by the MRTU initiative.

Over the past several years, the CAISO began to design an overhaul of its approach to managing transmission congestion with a redesign of its market structure in order to gain economic and technical efficiencies. The MRTU design, which involves a comprehensive overhaul of the electricity markets administered by the CAISO, would adopt a new full network model that will more accurately reflect the operations of the CAISO controlled grid.

In June 2004, the CAISO Board of Governors approved two parallel programs, the Market Redesign program and the Technology Upgrade program, managed as one CAISO MRTU initiative. The Market Redesign program would provide improvements to assure grid reliability and more efficient and cost effective use of energy resources. The Technology Upgrade program would strengthen the entire CAISO computer backbone it needs to successfully manage and operate the grid.

The Market Redesign program would:

- Create a new Day-Ahead market for energy. By starting the resource scheduling process in the day-ahead time frame, according to the CAISO there would be less reliance on the more volatile hour-ahead or real-time markets, which are the only ones that currently exist.
- Provide a more precise full network model of the grid, which would allow the CAISO to better predict how energy scheduled a day ahead of time will flow in real time.
- Introduce new market rules for energy dispatch and penalties to prevent market manipulation.
- Introduce local prices that would eliminate the distinction between inter- and intra-zonal congestion. Locational Marginal Pricing (LMP) shows the cost of producing power as well as the cost of delivery that would give the CAISO and market participants a clearer picture of the true cost of getting power from one area to another.

The Technology Upgrade program would:

- Provide updated computer technology and software to better manage loads and resources available and scheduled on the grid.
- Provide new computer systems to replace the CAISO's aging infrastructure and hardware.

In February 2006 the CAISO filed its MRTU Tariff with the Federal Energy Regulatory Commission (FERC), which was approved by FERC in September 2006.

On February 9, 2006, the CAISO filed its MRTU Tariff with the FERC. The MRTU Tariff filed was the result of lengthy studies by the CAISO and market participants, stakeholder meetings, and input from various government and regulatory agencies. FERC approved the Tariff in September 2006.

Market participants, including SDG&E, are required to comply with the FERC-approved MRTU Tariff as part of FERC regulations, and with agreements with the CAISO.

The CAISO has targeted MRTU Release 1 to be implemented by February 2008, and MRTU Release 2 in 2009 to address subsequent directives provided by the FERC in adopting MRTU.

In its AL 1867-E, SDG&E requests Commission authority to establish an MRTU Memorandum Account (MRTUMA) to record SDG&E's incremental capital-related revenue requirement and incremental O&M expenses associated with implementing the CAISO's MRTU initiative.

On January 29, 2007 SDG&E filed AL 1867-E requesting authority to establish the MRTUMA. According to SDG&E, the MRTUMA will record incremental capital-related revenue requirements such as depreciation, applicable taxes, and an authorized return on rate base, and incremental O&M expenses. The MRTU initiative will require the utilities to obtain new and upgraded systems and incur expenses for computer hardware, software licensing, and information technology labor to allow SDG&E's continued interactions with the CAISO. Incremental in this context means that the amounts SDG&E will record in the MRTUMA will be in addition to that portion of SDG&E's current authorized revenue requirements for funding the CAISO's MRTU initiative.

SDG&E proposes to request recovery of amounts recorded in the MRTUMA in an ERRA reasonableness proceeding or another regulatory proceeding as directed by the Commission. SDG&E proposes that the balance in the MRTUMA would be transferred to the Non-fuel Generation Balancing Account (NGBA) for rate recovery, applicable to bundled service customers, upon Commission approval.

NOTICE

Notice of SDG&E AL 1867-E was made by publication in the Commission's Daily Calendar. SDG&E states that a copy of the Advice Letter was mailed and distributed in accordance with Section III-G of General Order 96-A.

PROTESTS

There were no protests to SDG&E Advice Letter 1867-E.

DISCUSSION

Energy Division has reviewed SDG&E's AL 1867-E. Discussion of the relevant facts that lead to the approval of this advice letter, with modifications, follows.

The California Public Utilities Commission (CPUC) supports the CAISO's MRTU initiative.

For about the previous five years the CPUC has provided support for the CAISO's MRTU initiative, conditional with the FERC's approval of certain elements that the FERC has accepted. The CPUC has been working with the investor owned utilities (IOUs, i.e., Pacific Gas and Electric Co., SDG&E, and Southern California Edison Company) and the CAISO to ensure that there will be an LMP market design with consumer safeguards that will protect consumers from market manipulation as experienced during the energy crisis of 2001-2002. The CPUC recognizes that MRTU is a major project undertaking and Release 1 implementation, currently scheduled for February 2008, is just the beginning of implementing a complete MRTU.

The CPUC expects the IOUs to be fully prepared for MRTU and to have the resources necessary to be able to participate in the new market design, LMP, and a day-ahead energy market. SDG&E is authorized to establish the MRTUMA.

The IOUs should be prepared with the necessary resources, tools, computer software and hardware to be able to implement MRTU Release 1, currently scheduled for February 2008, and all subsequent Releases. To meet this objective, the IOUs should be permitted to track incremental MRTU-related costs in a memorandum account. We therefore authorize SDG&E to establish its MRTUMA proposed in AL 1867-E.

Recovery of the amounts recorded in SDG&E's MRTMUA shall be addressed in SDG&E's ERRA reasonableness review proceeding.

SDG&E states in its advice letter filing that it will record in the proposed MRTUMA its incremental capital-related revenue requirements and incremental O&M expenses associated with implementing the CAISO's MRTU initiative. SDG&E states it will request recovery of amounts recorded in this MRTU Memorandum Account (MRTUMA) in an ERRA reasonableness proceeding or another regulatory proceeding as directed by the Commission. SDG&E indicates that the balance in the MRTUMA would be transferred to the Non-fuel Generation Balancing Account (NGBA) upon Commission approval.

The amounts that SDG&E records in the MRTUMA shall be reviewed by the Commission in SDG&E's annual ERRA reasonableness proceeding. In that proceeding SDG&E shall present any amounts that it has recorded in the MRTUMA that it proposes to include in rates. Before we authorize recovery in rates of any amounts recorded in the MRTUMA, SDG&E will need to present sufficient information in that proceeding to justify that the amounts it has recorded are incremental and have been reasonably incurred to implement the CAISO's MRTU initiative. Additionally, before SDG&E transfers any balance in the MRTUMA to the NGBA or a different balancing account for rate recovery, SDG&E will require a Commission order to do so.

SDG&E indicates in AL 1867-E that this advice letter filing will not increase any rate or charge, cause the withdrawal of service, or conflict with any other schedule or rule. Because this advice letter filing request is merely to establish an

account for recording costs for possible future recovery in rates, SDG&E's assertion is justified.

SDG&E expects to record a total of about \$3.7 million in capital and O&M costs in their MRTU Memorandum Account by February 1, 2008.

When MRTU goes online by February 1, 2008, SDG&E reported that it expects to record about \$3.2 million in capital costs and \$0.5 million in O&M costs for a total of about \$3.7 million.

During 2008 and beyond, SDG&E expects to incur additional capital costs and additional on-going labor costs for software license fees and information technology support to maintain compatibility with the CAISO's MRTU Release 1 and subsequent releases.

Currently there is a large uncertainty in the MRTU-related costs that the IOUs will incur.

MRTU implementation will be a multi-year process and the CAISO has not determined all of the requirements it will have for market participants. While the CAISO plans to implement MRTU Release 1 by February 2008, it also plans for a Release 2 sometime in 2009, and possibly subsequent releases.

It is expected that the IOUs will incur expenses related to software development and revisions, computer hardware, internal labor costs, and possible contractor or consultant work that would be allocated to MRTU. Since the CAISO has not designed or set out the requirements for subsequent releases, there is currently no firm cost or expense estimate.

In order for the CPUC to have a better estimate of MRTU costs and expenses, we will require SDG&E to submit to Energy Division informational filings for cost estimates and amounts expected to be recorded in the MRTUMA.

Since some MRTU-related costs have already been included in a prior rate case, provisions are in place to prevent double recovery.

In its 2008 General Rate Case (GRC) SDG&E included the costs for 2.5 Full Time Equivalent personnel expected to support MRTU.

SDG&E should reduce its actual recorded MRTU expenditures by any previous Commission-authorized expenditures reflected in SDG&E's rate levels to ensure that SDG&E does not double-recover its MRTU expenditures. As noted above, in order to recover amounts recorded in the MRTUMA SDG&E must first provide justification in ERRRA reasonableness proceedings that its entries to the MRTUMA are incremental and have been reasonably incurred to implement the CAISO MRTU initiative. SDG&E should also obtain Commission approval by order before transferring the balance in the MRTUMA to the NGBA or some other balancing account for rate recovery, applicable to SDG&E's bundled customers as proposed by SDG&E.

SDG&E is not requesting any cost recovery for MRTU at this time.

This Resolution does not prejudice what costs associated with SDG&E's efforts to comply with the CAISO's MRTU initiative the Commission may subsequently authorize SDG&E to recover in rates.

Cost recovery associated with SDG&E's MRTU expenses is subject to a future Commission order(s). This Resolution does not prejudice or determine what costs the Commission will allow SDG&E to recover in rates associated with MRTU.

COMMENTS

Public Utilities Code section 311(g) (1) generally requires resolutions to be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g) (3) provides that this 30-day period may be reduced or waived pursuant to Commission adopted rule.

The 30-day comment period for the draft of this resolution was neither waived nor reduced. Accordingly, this draft resolution was mailed to parties for comments, and will be placed on the Commission's agenda no earlier than 30 days from the date the draft resolution was issued for comment.

No comments were filed for this resolution.

FINDINGS

1. Since it was created in 1996, the CAISO has experienced several flaws in its management of the electricity market and transmission systems within its control that will be corrected by the MRTU initiative.
2. In June 2004, the CAISO Board of Governors approved two parallel programs, the Market Redesign program and the Technology Upgrade program, to be managed as one CAISO MRTU initiative.
3. The MRTU design will adopt a new full network model that will more accurately reflect the operations of the CAISO controlled grid.
4. The MRTU initiative will create a new Day-Ahead market for energy in addition to the currently existing hour-ahead and real-time markets.
5. On February 9, 2006, the CAISO filed its MRTU tariff with the FERC.
6. FERC approved the CAISO's MRTU tariff in September 2006.
7. SDG&E filed AL 1867-E on January 29, 2007 to propose establishment of a MRTU Memorandum Account (MRTUMA) to record its incremental costs associated with MRTU.
8. Market participants, including SDG&E, are required to comply with the FERC-approved MRTU tariff as part of FERC regulations and agreements with the CAISO.
9. The CAISO has targeted MRTU Release 1 to be implemented by February 2008, and MRTU Release 2 in 2009 to address subsequent directives provided by the FERC in adopting MRTU.
10. The CPUC supports the CAISO's MRTU initiative.
11. The CPUC expects the IOUs to be fully prepared for MRTU and to have the resources necessary to be able to participate in the new market design, LMP, and a day-ahead market.
12. SDG&E's proposal to establish an MRTUMA is justified in order to meet the objectives of the CAISO's MRTU initiative.
13. SDG&E reported it expects to record a total of about \$3.7 million for MRTU expenses by the start of implementation for MRTU Release 1.
14. Since some MRTU-related costs have already been included in a prior rate case, provisions are needed to prevent double recovery.
15. In its 2008 GRC, SDG&E included a forecast of costs associated with 2.5 Full Time Equivalent personnel to support the CAISO's MRTU initiative.
16. SDG&E should reduce its actual recorded MRTU expenditures by any previous Commission-authorized expenditures reflected in SDG&E's rate levels to ensure that SDG&E does not double-recover its MRTU expenditures.

17. SDG&E's AL 1867-E filing will not create an increase in any rate or charge at this time, cause the reduction or withdrawal of service, or conflict with any other schedule or rule.
18. Cost recovery associated with the amounts recorded in SDG&E's MRTU Memorandum Account is subject to a future Commission order in SDG&E's ERRRA reasonableness proceedings.
19. Transfer of the balance in the MRTUMA to the NGBA or some other balancing account for rate recovery, applicable to SDG&E bundled service customers, is subject to a future Commission order.
20. This Resolution does not prejudge what costs the Commission will allow SDG&E to recover in rates associated with MRTU.
21. Currently there is a large uncertainty in the MRTU-related costs that the IOUs will incur.
22. SDG&E should submit to Energy Division informational filings for cost estimates and amounts expected to be recorded in the MRTU Memorandum Account 30 days prior to each MRTU Release.
23. SDG&E Advice Letter 1867-E was not protested.

THEREFORE IT IS ORDERED THAT:

1. The request of SDG&E, in its Advice Letter 1867-E, to establish an MRTU Memorandum Account (MRTUMA) is approved with the modifications specified herein.
2. SDG&E shall submit to Energy Division informational filings for cost estimates and amounts expected to be recorded in the MRTU Memorandum Account 30 days prior to each MRTU Release.
3. Cost recovery of amounts recorded in SDG&E's MRTU Memorandum Account is subject to a future Commission order(s) in SDG&E's ERRRA reasonableness proceedings. This Resolution does not prejudge or determine what costs the Commission will allow SDG&E to recover in rates associated with complying and participating in the CAISO's MRTU initiative. In order to recover amounts recorded in the MRTUMA, SDG&E must first provide justification that its entries to the MRTUMA are incremental and have been reasonably incurred to implement the CAISO MRTU initiative. Transfer of the balance in the MRTUMA to the NGBA or some other balancing account for rate recovery, applicable to SDG&E's bundled service customers, is subject to a future Commission order.

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 May 24, 2007; the following Commissioners voting favorably thereon:

Paul Clanon
Executive Director

MICHAEL R. PEEVEY
PRESIDENT
DIAN M. GRUENEICH
JOHN A. BOHN
RACHELLE B. CHONG
TIMOTHY ALAN SIMON
Commissioners