

Investigation 10-04-010, as corrected by Decisions 10-06-023 and 10-05-053 June 17, 2010

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Investigation on the Commission’s Own Motion Into the Operations and Practices of Constellation NewEnergy, Inc.; Notice of Opportunity for Hearing; and Order to Show Cause Why the Commission Should Not Impose Fines and Sanctions For Constellation NewEnergy, Inc. January 2009 Violation of System Resource Adequacy Requirements.

**FILED**  
**PUBLIC UTILITIES COMMISSION**  
**APRIL 8, 2010**  
**SAN FRANCISCO OFFICE**  
**I.10-04-010**

**ORDER INSTITUTING INVESTIGATION;**  
**NOTICE OF OPPORTUNITY FOR HEARING;**  
**AND ORDER TO SHOW CAUSE**  
**WHY THE COMMISSION SHOULD NOT IMPOSE**  
**APPROPRIATE FINES AND SANCTIONS**

**I. INTRODUCTION**

The California Public Utilities Commission (Commission) established Resource Adequacy Requirements (RAR) pursuant to and defined by Commission Decisions (D.) 05-10-042 and 06-06-064. The Consumer Protection and Safety Division (CPSD) of the Commission conducted an investigation into Constellation NewEnergy, Inc.’s (CNE) compliance with its January 2009 RAR. Based on its investigation, CPSD staff concludes that CNE failed to comply with its RAR procurement obligations and that a fine should be imposed.

CNE submitted a January 2009 Month-Ahead System Resource Adequacy (RA) Compliance Filing on November 26, 2008, which showed that it had not secured adequate resources for January 2009. CNE however included three contracts totaling 180 MW, which were not valid for the month of January 2009, causing CNE to have a deficiency in this amount. On December 15, 2008, CNE submitted an amended January 2009 month-

ahead filing reflecting the newly acquired capacity that corrected the deficiencies in the original filing.

The Commission, therefore, initiates this proceeding in order to consider whether to penalize CNE on the evidence of violations set forth in the CPSD Investigation Report. In this Order, we direct CNE to appear and show cause why the Commission should not find that CNE violated Commission rules by not securing the required energy resources for January 2009 by the day that CNE filed its Month-Ahead System RA Compliance Filing on November 26, 2008, and why the Commission should not impose appropriate penalties.

## **II. BACKGROUND**

Against the backdrop of California's energy crisis, the Commission established comprehensive RAR rules that require LSEs to demonstrate both (1) aggregate and system resource adequacy (acquisition of sufficient generation capacity to serve forecasted retail customer load, including a reserve margin), and (2) local resource adequacy (acquisition of sufficient generation capacity within defined, transmission-constrained areas)<sup>1</sup> in their service areas.

In Decisions (D.) 05-10-042 and 06-06-064, the Commission established rules requiring all Load-Serving Entities (LSEs) in the service territories of California's three largest investor-owned electric utilities to procure sufficient generation capacity, including reserves, to ensure that all retail customers within their service areas have reliable electric service. D.05-10-042 required LSEs to demonstrate that they had acquired sufficient generation capacity to serve forecasted retail customer load plus a reserve margin without accounting for local transmission constraints. D.06-06-064 required LSEs to demonstrate that they had acquired sufficient generation capacity within certain areas of their load with transmission constraints.

---

<sup>1</sup> Resolution E-4017, p. 2.

These decisions were part of a series of Decisions the Commission issued over a period of two and half years, beginning in 2004, to secure cost-effective investments in electric generation capacity for California. In each of these Decisions, the Commission considered and vetted the concerns of all affected LSEs and other interested parties to ensure that the RA program it established is effective and sustainable.

The Commission found that an LSE's failure to make the necessary RAR showings in its compliance filings jeopardizes the reliability of the grid and may burden the California Independent System Operator (CAISO) with the potential obligation to make the requisite procurement as a backstop. The Commission and the CAISO rely on accurate resource procurement and reporting to manage the many uncertainties that pose threats to the reliability of the grid. Therefore, the Commission has determined that LSEs should be held accountable in procuring and reporting accurate resource adequacy compliance filings.

**A. Resource Adequacy Requirement Compliance Filings**

The RAR rules require LSEs to file a report showing that they have procured 100% of the resources necessary to serve their forecasted demand for the month ahead, plus reserve.

- *Month-Ahead System Resource Adequacy Compliance Filings:* (1) a monthly Advice Letter filing with Energy Division using an approved template which demonstrates: (a) acquisition of 100% of the qualifying system capacity obligation (adjusted forecast plus reserve margin) for a "compliance month" from the qualifying capacity providers maintained by the CAISO and the amount of capacity from each provider; and (b) the sale of any qualifying capacity previously identified in a resource adequacy compliance filing for system resource adequacy requirements, and that the capacity remains fully available to the CAISO, and (2) a monthly load forecast submitted to the CEC demonstrating adjustments to the Preliminary Load Forecast for positive and negative load growth due to load migration.

(Resolution E-4017, pp. 2-3.) CNE's failure to file a valid Month-Ahead System RA compliance Advice Letter is at issue in this proceeding.

### **B. System Resource Adequacy Requirement**

The System RAR requires LSEs to demonstrate that they have acquired sufficient capacity to serve their retail customer load along with a 15-17% reserve margin. The supply contracts that count for RAR purposes must identify specific resources that provide the qualifying capacity. The Commission also established penalties for non-compliance with System RAR filing requirements, stating that such penalties were necessary for the program to achieve its objectives of providing reliable, cost-effective electricity and fostering an environment for cost effective investment in generation infrastructure. The penalties were set as a multiple of the cost of replacing the capacity an LSE failed to procure.

### **C. Public Utilities Code §380**

In January 2006 the California Legislature enacted Public Utilities (PU) Code §380, essentially codifying the Commission's activities under the RAR proceedings and authorizing the Commission to determine the most equitable means for achieving the RAR program goals.<sup>2</sup> In D.05-10-042, the Commission determined that a penalty regime is the most equitable means for achieving the RAR goals.

[A] regulatory program that imposes significant procurement obligations upon LSEs cannot be expected to succeed unless those LSEs have reason to believe there are consequences for non-compliance that outweigh the costs of compliance.

(D.05-10-042, p. 93; see also, D.06-06-064, p. 66.)

The Commission is empowered to see that the provisions of statutes, such as Section 380, which affect public utilities “are enforced and obeyed, and that violations thereof are promptly prosecuted and penalties therefore . . . , recovered and collected.”<sup>3</sup> Electric service providers (ESPs) are subject to Commission enforcement authority pursuant to the same statutes as if they were public utilities.<sup>4</sup>

---

<sup>2</sup> PU Code §380(h).

<sup>3</sup> PU Code § 2101.

<sup>4</sup> PU Code § 394.25.

### III. CPSD INVESTIGATION REPORT

#### A. Confidential Treatment

CPSD's report documents the results of its investigation into CNE's breach of the Commission's RAR program. Staff has not yet released its report to the public so that CNE may seek confidential treatment from the Commission for any portions of the staff's report it deems confidential. The Commission directs CNE to identify portions of the report for which CNE requests confidential treatment and provide justification for continued confidential treatment of such portions in accordance with Commission's rules and policies. CNE shall provide its justification by written motion filed within fourteen (14) days of the mailing of this Order (return receipt requested) and staff and interested parties may provide responses within ten (10) business days of the written motion. Any party opposing the confidential treatment that CNE requests shall provide justifications for making the relevant parts of the report public. This enforcement proceeding shall be open to the public and transparent because it involves issues affecting the public interest.

#### B. CNE's January 2009 Month-Ahead System Compliance Filing to the Commission and CAISO

CPSD's Report shows that CNE failed to comply with its procurement obligations for January 2009, and is subject to penalties pursuant to D.05-10-042 and D.06-06-064. As the Commission noted in D.06-06-064, non-compliance is serious because it could lead to the CAISO taking costly remedial measures.

We note that time is of the essence with respect to LSE compliance filings. If an LSE fails to make a timely filing demonstrating it has fulfilled its local procurement obligation, the CAISO may determine that it needs to proceed on the assumption that the LSE is deficient and therefore engage a backstop procurement to cover the deficiency, even if the LSE has in fact acquired the capacity needed to cover its obligation. Such backstop procurement could be necessarily costly. Accordingly, the penalty for failure to make a timely compliance filing should, after a grace period not to exceed 10 calendar days, be equal [to] the penalty for a deficiency.

(D.06-06-064, pp. 68-69, emphasis added.) D.06-06-064 explained the non-compliance penalties for both System and Local RAR Year-Ahead compliance filings as follows:

D.05-10-042 adopted the broad policy that for System RAR, a penalty equal to 300% of the cost of new capacity ... is an appropriate sanction for an LSE's failure to acquire the capacity needed to meet its System RAR obligation.

(D.06-06-064, p. 67.) CPSD recommends that the Commission impose the penalty set forth in D.05-10-042.

**C. CNE's System Resource Deficiency**

CPSD's Report shows that CNE's November 26, 2008, Month-Ahead System Resource Adequacy (RA) Compliance Filing secured inadequate resources for January 2009. The deficiencies stem from three contracts, that CNE listed as supplying capacity for January 2009 when in fact the contracts were not valid in January 2009. Two of the contracts were in place from May through September of 2009 and the third contract from October through December of 2009. One contract was for 130 MW and the other two contracts were for 25 MW each, resulting in a total deficiency of 180 MW for the month of January. This resulted in a system-wide deficiency.

The deficiency was noticed by the CAISO, which works in conjunction with the Commission in monitoring the implementation of the RA program. The CAISO staff reviews filings to verify the validity of contracts listed by LSEs. In its review of CNE's January 2009 filing, CAISO identified contract deficiencies from two of CNE's suppliers. CAISO staff contacted the suppliers, to confirm the deficiencies. On December 5, 2008, CAISO sent Commission staff a report showing the deficiencies.<sup>5</sup> The suppliers confirmed that contracts were not in place for January 2009 for the listed capacity.

---

<sup>5</sup> See Confidential Attachments to the Investigation Report on Constellation NewEnergy, Attachment 2, CAISO contracts validation.

#### D. Penalty Assessment

As prescribed in D.05-10-042, the penalty for the RAR deficiency totals \$1,800,000. According to D.05-10-042:

A penalty equal to three times the monthly cost for new capacity is an appropriate sanction for an LSE's failure to acquire the capacity needed to meet its RA obligation. (Conclusion of Law (COL) 21)

A price of \$40 per kW-year is a reasonable and appropriate measure of the cost of new capacity for purposes of both Local and System RAR penalties. (COL 26)

Using this formula, the penalties for the 180 MW-month total deficiency at 300% of the deficiency based on a rate of \$40 per kW-year is calculated as follows:<sup>6</sup>

- 180 MW/month x 1000 kW/MW = 180,000 kW/month
- \$40kW/year ÷ 12 months x 180,000 kW/month x 300% =  
\$1,800,000

Therefore, **IT IS ORDERED** that:

1. An investigation on the Commission's own motion is instituted into the Operations and Practices of CNE, to determine whether it violated Commission Resource Adequacy program rules, regulations, or orders in its November 26, 2008 Month-Ahead System Resource Adequacy (RA) Compliance Filing for January 2009.

2. The Commission directs CNE to identify portions of the CPSD report for which CNE requests confidential treatment and to provide written justifications within fourteen days of this Order is mailed for continued confidential treatment of such portions in accordance with Commission's rules and policies. Commission staff and other interested parties may provide responses within ten (10) business days of the written motion. Any party opposing the confidential treatment that CNE requests shall provide justifications for making the relevant parts of the report public. This enforcement proceeding shall be open to the public and transparent because it involves issues affecting

---

<sup>6</sup> 1000kW/MW is used to convert MW to kW.

the public interest. A copy of CPSD's Investigation Report on CNE's compliance violations will be placed in the docket designated for this proceeding, subject to any redactions requested by CNE that are consistent with our protocols.

3. CNE is directed to appear at a time and place to be determined by an Administrative Law Judge (ALJ) and show cause why the Commission should not find that CNE violated RAR rules made pursuant to Public Utilities Code section 380 by allowing system wide procurement deficiencies. The Commission's authority to impose penalties is established in Public Utilities Code section 2107 and 2108 and in D.05-10-042 and D.06-06-064.

4. After an ALJ is assigned, a Prehearing Conference (PHC) pursuant to Rule 7.2 will be convened and the ALJ will calendar a date, time and location for a hearing on the Order to Show Cause in a subsequent ruling or order. The subsequent ruling will set a schedule for the issuance of prepared testimony and any additional discovery matters. CNE shall serve prepared testimony responding to the issues stated above and any other allegations presented in this OII/OSC.

5. This ordering paragraph suffices for the "preliminary scoping memo" required by the Commission's Rules of Practices and Procedure (Rule), Rule 7.1(c). This proceeding is categorized as adjudicatory and may be set for evidentiary hearing, at the discretion of the assigned ALJ. Pursuant to Rule 8.2(b), ex-parte communications are not allowed. Categorization of this proceeding is appealable pursuant to Rule 7.6. The issues of this proceeding are framed in the above order.

6. A PHC shall be scheduled for the purpose of setting a schedule for this proceeding, including dates for the exchange of written testimony, determining which witnesses will need to testify, and addressing discovery issues. Any person filing a response to this Order Instituting Investigation, Notice with Opportunity to be Heard, and Order to Show Cause must state in any response any objections to such orders and notice regarding the need for hearings, issues to be considered, or proposed schedule. However, objections may not address factual allegations that an evidentiary hearing will decide.

7. A copy of this order and the staff report to be personally served on the Respondent at its registered agent for service of process:

CT Corporation System  
818 West Seventh Street  
Los Angeles, CA 90017

8. The temporary service list is hereby established for this proceeding to include CNE, the Director of the Energy Division, and the Director of the CPSD, and shall be used for service of all pleadings until a new service list for this proceeding is established. An initial service list for this proceeding shall be created by the Commission's Process Office and posted on the Commission's Website ([www.cpuc.ca.gov](http://www.cpuc.ca.gov)) as soon as it is practicable after the first prehearing conference. Any interested party may also obtain the service list by contacting the Process Office at (415) 703-2021.

This order is effective today.

Dated April 8, 2010 at San Francisco, California.

MICHAEL R. PEEVEY  
President  
DIAN M. GRUENEICH  
JOHN A. BOHN  
TIMOTHY ALAN SIMON  
NANCY E. RYAN  
Commissioners