

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 Pacific Gas and Electric Company; Notice of Opportunity for Hearing; and Order to Show Cause Why the Commission Should Not Impose Fines and Sanctions For Pacific Gas and Electric Company, March, April and July 2010 Violation of System Resource Adequacy Requirements.

FILED
PUBLIC UTILITIES COMMISSION
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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

In 2005 and 2006, the California Public Utilities Commission (Commission) established a Resource Adequacy Requirement (RAR) program pursuant to and defined by Commission Decisions (D.)05-10-042 and 06-06-064. The RAR program requires certain reporting requirements and time limits for fulfilling RAR requirements (RAR procurement obligations). The Commission's Consumer Protection and Safety Division (CPSD) conducted an investigation into Pacific Gas and Electric Company's (PG&E) compliance with its March, April and July 2010 RAR procurement obligations. CPSD's Report presents evidence that PG&E failed to comply with its RAR procurement obligations by not securing the required energy resources for March, April and July 2010 by the time those obligations were required to be secured, and recommends that PG&E be fined \$7,133,100 for these violations.

We, therefore, initiate this proceeding to consider whether to penalize PG&E \$7,133,100 in light of the evidence of violations set forth in the CPSD Investigation Report. In this Order, we direct PG&E to appear and Show Cause why we should not find that PG&E violated Commission rules by not securing the required energy resources for March, April and July 2010 at the time the filings were submitted.

II. BACKGROUND

Against the backdrop of California's energy crisis, we established comprehensive RAR rules that require load serving entities such as PG&E 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) in their service areas.¹ The RAR program was created to ensure that sufficient electrical power resources would be available to the California Independent System Operation (CAISO), to spur infrastructure development, and to effectively and fairly allocate procurement responsibilities among participants.

In D.04-10-035, D.05-10-042 and D.06-06-064, we established rules requiring all load serving entities 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. The load serving entities are also required 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.

These decisions were part of a series of orders we 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, we considered the

¹ Resolution E-4195, p. 2.

concerns of all affected load serving entities and other interested parties to ensure that the Resource Adequacy program we established is effective.

We found that a load serving entity's failure to satisfy its Resource Adequacy Requirements (which include the requisite procurement and reporting aspects) jeopardizes the reliability of the grid and require CAISO to make additional procurement as a backstop.² This 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, we determined that load serving entities should be held accountable in procuring and reporting accurate resource adequacy by way of compliance filings. To ensure compliance, we established penalties to deter program participants from failing to meet their procurement obligations.³ The program requirements include both system-wide and local area obligations for electricity procurement as well as the accurate and timely filing of reports.⁴ The Commission's Energy Division administers the RA program.⁵

In D.04-10-035, we first mandated that load serving entities make *Month-Ahead System Resource Adequacy Compliance Filing* showing they have procured all of their Resource Adequacy Requirements.⁶ In these filings, participants were required to show the capacity they had purchased would be fully available to the CAISO during the specified month. In D.04-01-050, we also adopted an LSE-based RAR program that made each load serving entity responsible for acquiring the resources needed for its own forecasted load plus a reserve margin.

In D.05-10-042 we addressed compliance, holding load serving entities accountable for compliance with all aspects of the program and stating that the essence of the

² D.06-06-064, pp. 65-69, and see Conclusion of Law (COL) 24-26.

³ Id.

⁴ D.05-10-043, pp. 93-95 and D.06-06-064, pp. 65-69.

⁵ D.05-10-043, p. 33.

⁶ D.04-10-035, pp. 37-40; and see, D.05-10-042, Finding of Fact 43.

RAR program is mandatory acquisition of capacity by load serving entities to meet load and reserves. In D.05-10-042, we adopted a set penalty structure of 300% of the cost of new capacity for failure to acquire the capacity needed to meet RA obligations.⁷ Also in D.05-10-042 we established a set penalty structure for the failure by load serving entities to acquire the capacity needed to meet system Resource Adequacy obligations. As noted in the decision:

The essence of the RA program is mandatory LSE acquisition of capacity to meet load and reserves...failure of an LSE to meet the obligation can result in the LSE having to pay, as a sanction for that failure, a multiple of the cost of capacity.⁸

We then addressed local resource adequacy and established penalties associated with local procurement obligations in D.06-06-064.

A. Public Utilities Code Section 380

Public Utilities Code Section 380 authorizes the Commission's resource adequacy programs and our ability to determine the most efficient and equitable means for achieving the RAR program goals.⁹ Section 380(e) compels the Commission to use its "enforcement powers to ensure compliance by all load serving entities."

B. System Resource Adequacy Requirement

The System RAR requires load serving entities to acquire 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.

⁷ On June 25, 2010, the Commission released D.10-06-036 which modified RA penalties. This new decision, however, stated "The new penalty structure will be in effect for violations which occur after the date of this decision." D.10-06-036, p. 49.

⁸ D.05-10-042, p. 94.

⁹ PU Code §380(h).

We also established a set penalty structure of three times the monthly cost for new capacity at \$40 per kW-year for failure to acquire the capacity needed to meet System Resource Adequacy obligations [i.e., three X \$40 per kW-year X the deficiency].¹⁰

C. Resource Adequacy Requirement Compliance Filings

The Resource Adequacy rules also require load serving entities to file a report showing that they have procured 100% of their Resource Adequacy Requirement for the month ahead, plus the reserve.

Month-Ahead System Resource Adequacy Compliance Filings: (1) a monthly compliance filing with appropriate Commission Staff using an approved template which demonstrates: (a) acquisition of 100 percent of the qualifying system capacity obligation (adjusted forecast plus reserve margin) for a “compliance month” from the qualifying capacity providers maintained by the California Independent System Operator 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 Year Ahead Local Resource Adequacy requirements, and that the capacity remains fully available to the California Independent System Operator; and (2) a monthly load forecast submitted to the California Energy Commission demonstrating adjustments to the Preliminary Load Forecast for positive and negative load growth due to load migration.¹¹

III. CPSD Investigation Report

A. PG&E’s March, April and July 2010 *Month Month-Ahead System Resource Adequacy Compliance Filing to the Commission and CAISO*

CPSD’s Investigative Report, which is mailed to PG&E concurrently with this OII, presents evidence that PG&E failed to comply with the March, April and July 2010 *Month-Ahead System Resource Adequacy Compliance Filing* requirements by not

¹⁰ D.05-10-043, COL 21 and D.06-06-064, COL 25 and 26.

¹¹ Resolution E-4195, pp. 8-9.

securing the requisite capacity. CPSD's Report also presents evidence that PG&E is subject to penalties pursuant to D.05-10-042 and D.06-06-064. As we noted in D.06-06-064, non-compliance is serious because it could require the CAISO to take 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.¹²

B. PG&E's System Resource Deficiency

CPSD's Investigative Report presents evidence that PG&E was deficient in satisfying its RA requirements (qualifying system capacity obligation) as indicated in

Table 1:

TABLE 1

<u>Month</u>	<u>Obligation</u>	<u>Validated</u>	<u>Deficiency</u>
March	Confidential MW	Confidential MW	167.72 MW
April	Confidential MW	Confidential MW	258.82 MW
July	Confidential MW	Confidential MW	<u>286.77 MW</u>
Totals	Confidential MW	Confidential MW	713.31 MW

The deficiency was noticed by the CAISO, which works in conjunction with the Commission in monitoring the implementation of the Resource Adequacy program. The CAISO staff reviews filings to verify the validity of contracts listed by load serving entities. In its review of PG&E's March, April and July 2010 *Month-Ahead*

¹² D.06-06-064, pp. 68-69, emphasis added.

System Resource Adequacy Compliance Filings, the CAISO identified contract deficiencies from several of PG&E's suppliers. These contract deficiencies showed that PG&E did not meet its qualifying system capacity obligations by the amounts indicated in **Table 1**.

C. Penalty Assessment

D.06-06-064 explained the rationale for 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.¹³

We prescribed a set penalty structure in 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 these guidelines, the penalties for the 713.31 MW of total deficiencies at 300% of the deficiency based on a rate of \$40 per kW-year is calculated as follows:¹⁴

- $713.31 \text{ MW/month} \times 1000 \text{ kW/MW} = 713,310 \text{ kW/month}$
- $\$40\text{kW/year} \div 12 \text{ months} \times 713,310 \text{ kW/month} \times 300\% = \$7,133,100$

The penalties for the RAR deficiencies per month thus total as follows:

¹³ D.06-06-064, p. 67.

¹⁴ 1000kW/MW is used to convert MW to kW.

March	\$1,677,200
April	\$2,588,200
July	<u>\$2,867,700</u>

Total Fine \$7,133,100

CPSD recommends that the Commission impose a penalty of \$7,133,100 consistent with the formula established in D.05-10-042.

Therefore, **IT IS ORDERED** that:

1. An investigation on the Commission's own motion is instituted into the Operations and Practices of PG&E, to determine whether it violated Commission Resource Adequacy program rules, regulations, or orders in failing to timely meet its qualifying system capacity obligations for March, April and July 2010.

2. PG&E is hereby ordered to respond to these allegations and Show Cause why it should not be sanctioned for violating Commission rules by not securing the required energy resources for March, April and July 2010 at the time the filings were submitted in violation of Resource Adequacy rules adopted pursuant to Public Utilities Code section 380 and D.05-10-042 and D.06-06-064.

3. CPSD is hereby named as a party to this proceeding.

4. This proceeding is categorized as adjudicatory. Pursuant to Rule 8.2(b), *Ex Parte* communications are not allowed. Categorization of this proceeding is appealable pursuant to Rule 7.6.

5. It is preliminarily determined that hearings are needed. According, pursuant to Rule 7.2, the assigned Commissioner shall set a prehearing conference as soon as practicable to address the schedule for this proceeding, issues to be addressed, and need for hearing.

6. The scope of the issues in this proceeding is preliminarily determined to be whether PG&E violated the resource adequacy rules and whether it should be sanctioned. This ordering paragraph suffices for the "preliminary scoping memo" required by Rule 7.1(c). The issues of this proceeding are framed in the above order.

7. A copy of this Order and CPSD's Investigative Report are to be served by certified mail, return receipt requested, on Respondent Pacific Gas and Electric Company at the following address:

Pacific Gas and Electric Company
77 Beale Street, # 100
San Francisco, CA 94105
Attention: Agent for Service of Process

This order is effective today.

Dated June 9, 2011, at San Francisco, California.

MICHAEL R. PEEVEY
President
TIMOTHY ALAN SIMON
MICHEL PETER FLORIO
CATHERINE J.K. SANDOVAL
MARK FERRON
Commissioners