

Decision 06-07-031 July 20, 2006

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Consider
Refinements to and Further Development of the
Commission's Resource Adequacy Requirements
Program.

Rulemaking 05-12-013
(Filed December 15, 2005)

OPINION ON REMAINING PHASE 1 ISSUES

Table of contents

Title	Page
OPINION ON REMAINING PHASE 1 ISSUES.....	1
1. Summary	2
2. Background	3
3. RAR Capacity Product (Staff Report II.).....	4
3.1. Impacts of Outages on Qualifying Capacity (Staff Report II.A.1.)	6
3.2. Capacity Derates (Staff Report II.A.2.).....	11
3.3. Penalties for Non-Performance (Staff Report II.A.3.)	12
3.4. Maintenance and Repair Obligations (Staff Report II.A.4.)	14
3.5. Bulletin Board and Centralized Title Clearing (Staff Report II.A.5.)...	15
3.6. Import Requirements (Staff Report II.A.6.)	17
3.7. Creditworthiness (Staff Report II.A.7.)	19
3.8. Intermediaries (Staff Report II.A.8.)	20
3.9. Pooling Of Assets and Substitution (Staff Report II.A.9.)	21
3.10. Regulatory Uncertainty (Staff Report II.A.10.)	23
3.11. Required Elements of Standardized, Tradable Capacity Products	24
4. Implementation Issues (Staff Report III.).....	35
4.1. Filing Guide and Templates (Staff Report III.A.; V.)	35
4.2. Maximum Cumulative Capacity (Staff Report III.B.)	37
4.3. Accounting for Transmission Losses (Staff Report III.C.).....	38
4.4. Process for Resolving Discrepancies (Staff Report III.D.)	39
5. Comments on Draft Decision	39
6. Assignment of Proceeding.....	40
Findings of Fact.....	40
Conclusions of Law	43
ORDER	44

OPINION ON REMAINING PHASE 1 ISSUES

1. Summary

In this decision, we address proposals for refinements to and clarification of the Commission's resource adequacy requirements (RAR) program. In particular, we address topics for which such clarification or refinement would establish clearer expectations among market participants regarding how contracts for resources will count towards fulfilling the procurement obligations that load-serving entities (LSEs) must meet. We refine our definition of the essential elements of a resource adequacy capacity product, which in turn could lead to the development, by and among industry participants, of a standardized capacity product that can be readily traded. Availability of such a capacity product should promote the achievement of RAR program goals and reduce RAR compliance costs incurred by LSEs.

This decision also addresses certain program issues that have arisen during the initial implementation stages of the RAR program adopted by the Commission in Decision (D.) 05-10-042. We review the compliance filing guides and templates that were developed by the Energy Division in consultation with the California Independent System Operator (CAISO) and the California Energy Commission (CEC), and we authorize the Energy Division to make revisions to the filing guides and templates that are consistent with our RAR decisions and necessary to give full effect to those decisions. We also clarify certain resource counting rules and address the treatment of transmission losses in the RAR program.

This decision concludes Phase 1 of this Rulemaking. The proceeding remains open for consideration of issues described in the Order Instituting this

Rulemaking, as set forth in detail in the *Assigned Commissioner's Scoping Memo* dated March 1, 2006 (Scoping Memo).

2. Background

D.06-06-064, our recent decision adding a local procurement obligation (Local RAR) to the Commission's RAR program, includes a discussion of the background of this Commission's RAR program and a summary of the Phase 1 record for this proceeding. We incorporate by reference the background discussion from that decision to avoid unnecessary duplication.

The Commission's Energy Division issued a comprehensive report on Phase 1 topics on April 10, 2006 (Staff Report), and parties were asked to submit post-workshop comments and replies on those topics using the outline of the Staff Report. The issues discussed in Sections I and IV of the Staff Report ("Local Resource Adequacy Requirements" and "Other Issues," respectively) were addressed in D.06-06-064. This decision addresses issues discussed in Sections II, III, and V of the Staff Report ("Tradable Capacity Product Issues," "Implementation Issues," and "Appendices: Resource Adequacy Filing Guides and Templates," respectively.)¹

The following table lists the commenting parties in Phase 1 and the short title or acronym for the party as used in this decision.

¹ Where applicable, section headings herein include cross-references to the corresponding sections of the Staff Report.

COMMENTING PARTIES

Commenting Party or Parties	Short Title or Acronym for Party or Parties
Aglet Consumer Alliance	Aglet
Alliance for Retail Energy Markets	AREM
California Independent System Operator	CAISO
California Manufacturers & Technology Association and California Large Energy Consumers Association	CMTA/CLECA
California Municipal Utilities Association	CMUA
City and County of San Francisco	CCSF
Constellation Energy Commodities Group, Inc. and Constellation NewEnergy, Inc.	Constellation
Division of Ratepayer Advocates	DRA
Energy Producers and Users Coalition	EPUC
Good Company Associates on behalf of TAS	Good/TAS
Independent Energy Producers Association	IEP
Mirant California LLC, Mirant Delta LLC, Mirant Potrero LLC; NRG Energy Inc., and West Coast Power	Mirant/NRG
Pacific Gas and Electric Company	PG&E
Pilot Power Group, Inc.	Pilot Power
Powerex Corp.	Powerex
San Diego Gas & Electric Company	SDG&E
Sempra Global	Sempra Global
Southern California Edison Company	SCE
The Utility Reform Network	TURN
Western Power Trading Forum	WPTF
PG&E, SDG&E, and SCE	IOUs
APS Energy Services, CLECA, CMTA, Coral Power LLC, DRA, Energy Users Forum, J. Aron & Company, TURN, Silicon Valley Leadership Group, and Strategic Energy LLC	Joint Parties

3. RAR Capacity Product (Staff Report II.)

The Commission has recognized that a capacity product that meets the resource counting requirements of the RAR program and that can be readily

traded would be beneficial to the program and its participants. In D.04-10-035, the Commission stated that “a readily traded capacity contract that parties can voluntarily exchange is a useful first step” toward creation of a capacity market, and it raised the possibility of approving specific contract language in subsequent proceedings. (D.04-10-035, p. 42.) In D.05-10-042, the Commission noted that several parties had objected to the idea that the Commission would mandate the use of specific contract language. Instead, parties generally agreed, and the Commission concurred, it would be more helpful for the Commission to focus on “essential contract elements.” (D.05-10-042, p. 26.) The Commission observed that development of a readily transferable capacity contract may warrant further study, and it provided interim guidance to LSEs and suppliers by determining that an RA capacity contract that includes certain, specified minimum elements would qualify as an eligible contract that LSEs could rely upon to meet their procurement obligations.² (*Id.*, 26-27.) The Scoping memo for this proceeding stated that consideration of a tradable capacity product “may be of critical importance to enable LSEs to efficiently acquire capacity to meet their local ... procurement obligations and is therefore included in Phase 1.” (Scoping Memo, p. 3.)

In comments filed on March 13, 2006, several parties addressed issues pertaining to the tradable capacity product concept, and the workshop of March 27, 2006 took up these issues. At the request of the Energy Division, SCE prepared a report on the tradable capacity product issues that were discussed at the March 27 workshop (Workshop Report) based on a staff pre-workshop

² The Commission specified that the capacity identified in a contract must (1) meet Commission-adopted counting protocols, (2) meet CAISO deliverability requirements, (3) not be sold to more than one buyer, (4) be subject to CAISO tariffs, and (5) be made available to the CAISO according to detailed rules. (D.05-10-042, pp. 27-28.)

discussion paper. SCE filed the report on April 3, 2006. The April 10, 2006 Staff Report incorporated the Workshop Report by reference.

The Workshop Report discussed ten issues related to the development of a tradable capacity product, some of which are also applicable to qualifying capacity irrespective of the specific relationship between the entity controlling the generator and LSE, that could potentially be resolved in Phase 1 of this proceeding. The report anticipated that other issues pertaining to standardized terms and conditions of a capacity product would be taken up for consideration in Phase 2. As the report states,

A tradable bilateral capacity product should provide a more efficient means to achieve [RAR program] compliance, especially for smaller load serving entities (LSEs). Parties believe that timely resolution of these issues will facilitate the evolution of a standardized product(s) and facilitate transactions of such product(s). (Workshop Report, p. 2.)

Section 3 of this decision addresses the ten issues (Sections 3.1 through 3.10) and also sets forth an updated and refined listing of essential elements of a capacity product that replaces the listing set forth in D.05-10-042. (Section 3.11.) As will be noted in each applicable section, our policy decision regarding the issue being addressed will apply to all qualifying capacity.

3.1. Impacts of Outages on Qualifying Capacity (Staff Report II.A.1.)

The Workshop Report describes the need for clarification regarding how forced and scheduled outages impact resource owners and LSEs as follows:

Certain parties are concerned that current counting rules and proposed CAISO tariffs do not provide clarity on the effect of forced outage rates on Qualifying Capacity (QC). In addition, it is unclear if and how testing requirements and protocols will be developed and applied either related to repairs after forced outages or on a routine basis. The impact of such actions on QC is also unclear.

Uncertainty in these areas may lead to suppliers not offering all available QC to market participants in anticipation of some form of “derate” once such rules are established. Uncertainty regarding treatment of QC will also affect LSEs since requiring the replacement of derated capacity would effectively require the LSE to account for forced outages twice. Additionally, with regard to scheduled outages, parties believe that so long as any scheduled outage change is approved by the CAISO pursuant to its Open Access Transmission Tariff (Tariff), the movement of the Scheduled Outage date change should not automatically trigger any replacement obligation upon the LSEs. This is notable, because often times LSEs are not aware of when generators have scheduled such outages. (Workshop Report, p. 4.)

The Workshop Report states that there was general consensus that the Commission should adopt a “forced is forced” policy whereby LSEs would be able to rely upon the QC of a unit that is established by the CAISO for a given RAR compliance year. An LSE that has claimed QC from a unit that experiences a forced outage would be able to count the established QC for that unit in its RAR compliance filings, and it would not be subject to a penalty or replacement obligation for that QC. The post-workshop comments generally affirm the consensus described in the report, although the CAISO proposed adopting a variation of the policy.

We hereby affirm that our RAR program shall include the “forced is forced” policy as generally described in the Workshop Report. We believe that this approach is consistent with our prior RAR decisions establishing a planning reserve requirement, and that it is necessary to avoid requiring LSEs to account for forced outages twice – once through the reserve margin procurement requirement and once through replacement procurement.

We provide the following additional clarification. First, we reiterate our understanding and expectation that the CAISO will establish and publish a list of

generating units and the QC for those units so that LSEs will know and be able to rely on the extent to which the resources they acquire and use for their RAR compliance showings will count toward meeting their procurement obligation. As discussed in the following section, we determine that LSEs will need access to the list 90 days prior to the filing date for year-ahead compliance filings, and publication of the CAISO's QC list will therefore be needed on or about July 1. LSEs will rely upon this QC list for their year-ahead and month-ahead RAR compliance filings for and throughout the applicable compliance year, and the Commission will not hold LSEs accountable for any changes in a unit's QC that may be identified by the CAISO after the list is established on or about July 1.³

Thus, for the applicable compliance year, LSEs will not be subject to any Commission-imposed penalty or Commission-imposed replacement procurement obligation in the event of a forced outage of a unit that was on the QC list and used by the LSE in fulfillment of its RAR procurement obligation. Since the QC list will be established on a yearly basis, we concur with the report's observation that for multi-year contracts, the contracting parties will need to incorporate terms that assign the risk for future QC changes. Finally, we note our concurrence with the position of the CAISO and others who contend that this annual approach to establishing unit-specific QCs may appropriately be revisited after experience is gained with the operation of the RAR program.

³ We understand that the CAISO may regularly update the QC list throughout the year to reflect the current state of the generation fleet. It is the version that is published and in effect on or about July 1 that becomes official for purposes of the RAR program. We ask that the CAISO make an appropriate designation so there is clarity regarding the official list for the applicable RAR compliance year. Ministerial changes such as changes in resource identification numbers must be clearly distinguished from substantive changes that will only be applicable for the following compliance year.

The CAISO proposes that the “forced is forced” policy be restricted to outages of limited duration. Specifically, the CAISO proposes that LSEs be subject to a replacement obligation that begins when the outage duration is expected to last beyond the seventh day of the third month following the month in which the outage occurred. In support of this proposal, the CAISO describes the scenario where a unit suffers a catastrophic mechanical failure and the owner determines that it is uneconomic to remedy the failure. The CAISO maintains that allowing the LSE to count the unit for the duration of the compliance year is anathema to RAR reliability goals. We will not adopt this proposed restriction of the “forced is forced” policy. As Constellation, SCE, and TURN correctly note in their reply comments, the reserve margin that we adopted in D.04-01-050 encompasses forced outages. We do not find it is necessary or appropriate to require LSEs to engage in replacement procurement when doing so would effectively require them to procure more than the reserve margin. This policy is applicable to all QC.

With respect to scheduled outages, the Workshop Report reported consensus on the QC counting protocol set forth in the table below.⁴ If the CAISO changes the approved schedule for an RAR resource, the LSE will not be held responsible for procuring replacement capacity. However, the CAISO’s

⁴ Mirant/NRG suggests that we either use the term “planned” rather than “scheduled” or define “scheduled” to exclude scheduled outages resulting from forced or maintenance outage events. We adopt the latter approach.

For purposes of RAR, a scheduled outage that affects all or part of a unit’s QC is defined as one that is designated “Approved Planned” according to the CAISO’s outage coordination rules and procedures. The length of the outage and magnitude of curtailment are also taken from the CAISO’s outage coordination rules and procedures. Similarly, we specify that a forced outage that affects all or part of a unit’s QC is one that is designated “forced” according to CAISO’s outage coordination rules and procedures.

denial of an original scheduled outage request on a RAR resource would not constitute a “change” in a scheduled outage, and, therefore would not warrant an exemption from replacement procurement. We will approve this protocol for scheduled outages. This policy is applicable to all QC. We note that under its tariff, the CAISO retains discretion to accept or deny any particular request for a scheduled outage.

Scheduled Outages

Time Period	Description of How Resource Would Count at Time of the Showing
<p style="text-align: center;">Summer</p> <p>May through September</p>	<p>Any month where days of scheduled outages exceed 25% of days in the month, the resource does not count for RAR. If scheduled outages are less than or equal to 25% the resource does count for RAR.</p>
<p style="text-align: center;">Non-Summer Months</p> <p>October through April</p>	<p>For scheduled outages less than 1 week, the resource counts for RAR.</p> <p>For scheduled outages 1 week to 2 weeks, the amount counted for RAR is prorated using the formula: $[1 - (\text{days of scheduled outage} / \text{days in month}) - 0.25] * \text{MW} = \text{RAR}$ The formula will allow resources to count between 50% and 25%.</p> <p>For scheduled outages over 2 weeks, the resource does not count for RAR.</p>

As noted in Section 4.1 below, we are authorizing and directing the Energy Division to develop detailed RAR compliance filing guides and templates based on the policies developed here. These filing procedures should address, among other things, the partial outage of a unit and other operational complexities.

Numerous parties requested that the Commission commit to reopening the resource adequacy program rules related to outages in Phase 2 of this proceeding. We have previously expressed the importance of the CAISO establishing generator performance obligations, and we recognize that we may need to revisit the resource adequacy program rules when comprehensive

CAISO rules related to outages are further developed and/or as the program's experience requires.

**3.2. Capacity Derates
(Staff Report II.A.2.)**

Parties are concerned that since a resource's QC can change over time, there is a risk of capacity "derates" that must be accommodated in commercial transactions, particularly those of any meaningful duration. Accordingly, parties seek the establishment of clear rules concerning when derates can occur, what notice might be provided to LSEs, the process by which the CAISO will derate a resource, and how QC can be affected by future deliverability assessments. There is consensus that such adjustments need to occur on a known and standardized cycle to sufficiently accommodate the transaction time needed for LSEs to make their annual year-ahead RAR showings.

The Workshop Report notes that consensus also appears to have been reached that in order for LSEs and others to make informed decisions regarding the products they will use in their upcoming year-ahead filings, the QC for any generator shall be established approximately 90 days before the year-ahead compliance filing is due (about July 1, 2006 for this cycle). The report notes further that this approach recognizes that QC is not a function of availability, and that D.05-10-042 tasked the CAISO with developing performance standards for generators.

As we noted earlier, we expect that the CAISO will establish and publish a list of generation units and the QC for those units on an annual basis. We also determined that once the list is established for a compliance year, LSEs will not be required to engage in additional procurement as a result of any change in the QC for a unit that was used in its compliance filing. This policy is applicable to

all QC. In view of the compliance filing cycle we have established in earlier RAR decisions, it is apparent that the QC list should be published on or about July 1 so that LSEs will have adequate time, and knowledge of units' QCs, so that they can procure their requirements from among the available units.

For purposes of the RAR program, unit derates would thus be reflected in the next year's QC list. We note, as the workshop report observes, that the imposition of QC adjustments on a regular (annual) cycle, and the potential for suppliers to lose a quantity of product they would otherwise be able to sell in the RAR market, provides an additional market incentive to maintain the availability of capacity. This incentive is above and beyond the existing regulatory requirements imposed by the Commission through General Order (GO) 167.⁵

3.3. Penalties for Non-Performance (Staff Report II.A.3.)

The workshops revealed concern that the willingness and ability of buyers and sellers to negotiate contracts for RAR capacity is undermined because penalties for non-performance by generators and by LSEs subject to our RAR program have not been defined with sufficient clarity. For example, parties find it is unclear when an LSE has demonstrated compliance with the RA requirements and when its obligation ends with respect to the seller's performance. Such uncertainty affects the determination of performance

⁵ GO 167, *Enforcement of Maintenance and Operation Standards for Electric Generating Facilities*, was adopted by the Commission to implement and enforce standards for the maintenance and operation of certain electric generating facilities and power plants so as to maintain and protect the public health and safety of California residents and businesses, to ensure that electric generating facilities are effectively and appropriately maintained and efficiently operated, and to ensure electrical service reliability and adequacy. The GO does not apply to certain facilities, including nuclear plants and certain Qualifying Facilities, among others.

exposure between the parties and how contracting parties might mitigate that risk exposure. Parties therefore ask that any potential penalties for nonperformance be clearly defined in order to facilitate the most economic transactions. Many parties are also concerned that the penalty level set by the Commission will be a key driver in the risk allocation embedded in individual commercial transactions and risk management in portfolio development, and, therefore, will have significant commercial implications. Thus, while agreeing that penalties must act as a deterrent to LSE non-compliance, parties believe they should not be so punitive as to cause irreparable financial harm to LSEs or unnecessarily raise transaction costs.

It is apparent that greater clarity regarding penalties for non-compliance with the Commission's RAR program would facilitate contracting by enabling contracting parties to identify and assign non-performance risks. We took a step towards providing such clarity in our recent decision on Local RAR, wherein we adopted a reference capacity price as the basis for calculating non-compliance penalties for both Local and System RAR. We are providing further definition of the penalty regime for LSEs in this decision. For example, we have clarified that the LSE responsibility for a given RAR compliance period (year-ahead or month-ahead) ends when it has made a timely and valid RAR compliance filing that demonstrates it has met its procurement obligation for that period. Except where GO 167 is applicable, penalties for generator non-performance must be addressed by the CAISO, while contract provisions may create yet other penalties for failure to satisfy contract requirements. Finally, we intend to address the penalty regime further in Phase 2 of this proceeding both to recognize new facts such as the CAISO's Reliability Capacity Services Tariff and to consider adopting a GO that would further delineate penalties that a

non-compliant LSE could face. The GO may address, among other things, a process for ministerial imposition of penalties for lesser violations.

In the meantime, if a Scheduling Coordinator for an LSE submits a Resource Adequacy filing that demonstrates non-compliance with Commission rules, the CAISO is to notify the Scheduling Coordinator, or in the case of a mismatch between a Resource Adequacy filing and Supply Plan, the relevant Scheduling Coordinators, within 10 days in an attempt to resolve the issue. If this process does not resolve the concern, the CAISO will notify the Commission. The Energy Division will then notify the LSE and allow the LSE a limited period of time to resolve any violation. If the LSE fails to do so, the Energy Division would recommend that the Commission initiate an enforcement proceeding.

3.4. Maintenance and Repair Obligations (Staff Report II.A.4.)

The Workshop Report notes that maintenance and repair obligations, have not been defined for all resource adequacy units, and it suggests that the Commission should consider if minimum standards should be applied in order to ensure that reliable capacity is available under the must-offer obligation for all units. The report notes that many parties have very different standards, and that it would be helpful to have a common requirement for this product. Under draft CAISO tariff language, the standard is “good utility practices” but some parties are concerned that this language is not sufficiently robust. While parties generally felt that GO 167’s obligations are adequate for those units to which it applies, there was no agreement on how to enforce such obligations on units outside the reach of GO 167.

We accept the general consensus that GO 167 adequately addresses maintenance and repair obligations for those units to which it applies. With

respect to other units, we generally agree with the observation of Constellation that contracting parties can be expected to negotiate maintenance and repair obligations. However, to promote a reasonable degree of uniformity in contract provisions that may facilitate trading of RAR capacity contracts, we find it reasonable to accept the proposal of WPTF to require that all suppliers of qualifying RAR capacity agree to follow Good Utility Practices as defined in CAISO tariffs and to comply with all applicable laws, regulations, and standards. We hereby adopt this as our policy for RAR, applicable to all QC. At this time we are not persuaded that SCE's proposal to require that generators that are exempt from GO 167 pursuant to Pub. Util. Code § 761.3 be subject to the "General Duty Standards" set forth in the general order is necessary for the success of the RAR program.

3.5. Bulletin Board and Centralized Title Clearing (Staff Report II.A.5.)

The Workshop Report notes that there currently is no process or mechanism in place to verify that the QC an LSE is buying is, in fact, available. While the CAISO has a process in place to post and update the QC for the net dependable capacity of units, that process does not take into account planned outage information or provide insight into the availability of the QC for purchase by an LSE. The report notes that this is particularly an issue for transactions of partial units where several parties may be transacting for different "pieces" of a generating unit. It is also unclear, the report notes, what roles the Commission or the CAISO will provide and what process will be used to resolve conflicts over QC counting rights between LSEs and asset owners.

The report goes on to note that mechanisms such as electronic bulletin boards are especially important for LSEs to manage their capacity positions

between the time they must make their annual showings and the time they must make their month-ahead showings. While the aggregate amount of System and Local RAR obligation will remain constant from the annual showing to the month-ahead showing, the entity responsible for serving the load and thus complying with the RAR showing may well change. Thus, LSEs will need to either buy or sell capacity to match their obligations, and a mechanism, such as a bulletin board, would be a useful interim tool to facilitate these transfers. Parties assert that a bulletin board-type mechanism would aid in helping market liquidity and transparency since it would include a posting of bids and offers and could include information about executed transactions.

Notwithstanding the concern noted in the Workshop Report regarding the need for a process to address QC counting issues, staff advises us that it has been able to work with LSEs to resolve discrepancies in the 2006 compliance filings.

We accept and endorse the general consensus that a bulletin board (or boards) on which bids and offers for qualifying RAR capacity would be posted would be a useful tool that would promote transparency and liquidity in the market and thereby assist in the implementation of the RAR program. We clarify that this Commission is not assuming responsibility for the development or operation of a bulletin board, and we are not designating the entity or entities that would undertake such development and operation. We are confident that if the availability of a bulletin board is as useful a tool as the parties and we believe it is, those with the necessary enterprise and expertise will step in to fill the need for such a tool.

With respect to the general consensus that Commission guidance regarding the attributes of a bulletin board may be helpful in spurring the development of such a tool, we simply note that the RAR compliance filing

guides and templates established by the Energy Division, as modified by the Energy Division from time to time, represent a detailed compendium of the RAR program elements and should therefore be useful to those who would design a bulletin board for RAR capacity trading. Finally, we note that a bulletin board for RAR capacity potentially represents a valuable data source for the Commission, the CAISO, and stakeholders, and we hope that attention is paid for the need for all to have access to data in the bulletin board to the extent consistent with confidentiality protocols.

We go no further at this time. We recognize the concern of Constellation and others that more work among parties and possible further Commission guidance may be needed before a bulletin board is launched. We stand ready to address this matter further, as needed, in Phase 2 of this proceeding.

In view of the staff's report that it has been able to resolve discrepancies, the need for a title clearinghouse established by the CAISO to address overselling the QC of a given unit and gaming by LSEs is unclear. Before commenting further on this topic, we would want to know more about the nature and extent of the problem as well as the proposed solution and potential alternate solutions such as standard contract language requiring the seller to warrant that it has exclusive right to the unit's capacity and that the contracted quantity of capacity has not been committed to any other party.

3.6. Import Requirements (Staff Report II.A.6.)

The Workshop Report discusses several areas of uncertainty related to the use of import resources to meet the counting requirements of the RAR program. These include uncertainty regarding allocation of import rights for multi-year contracts, how intertie space is allocated with respect to contracts with evergreen

provisions, and various other questions relative to the use of imports as capacity resources. The Workshop Report identifies little consensus on these topics, and it notes that the issue of whether must-offer obligations are applicable to import resources is the subject of SCE's pending petition for modification of D.05-10-042.

While we understand the need for clarity regarding how import resources should count toward fulfillment of LSEs' procurement obligations, we generally agree (with one exception described below) with SCE's post-workshop comments that no action with respect to imports need be taken in this decision. We will address the must-offer obligation when we resolve SCE's petition for modification of D.05-10-042, and we will be in a better position to resolve allocation issues after we have had an opportunity to consider the action of the Federal Energy Regulatory Commission (FERC) regarding the CAISO's request for FERC approval of an RAR import allocation methodology for 2007.

We adopt the uncontested proposal of Powerex to clarify that "a firm transmission requirement" need not be a required element for qualifying imports as a tradable capacity product that counts for RAR. As Powerex notes, it is more appropriate to use specific elements of the transmission requirement in the counting protocol for imports rather than the designation "firm." These elements are: (1) the contract is an Import Energy Product with operating reserves, (2) the contract cannot be curtailed for economic reasons, and (3a.) the contract is delivered on transmission that cannot be curtailed in operating hours for economic reasons or bumped by higher priority transmission or, (3b.) the contract specifies a scheduling point as defined in the CAISO's tariff, (not seller's choice).

**3.7. Creditworthiness
(Staff Report II.A.7.)**

Some LSEs have discovered that QC is only available from non-creditworthy counterparties, which raises the problem of defining the responsibility of LSEs to enter into RAR contracts with generators or other suppliers that are not creditworthy. Unlike utilities, which have rate recovery opportunities pursuant to Assembly Bill 57, electric service providers (ESPs) do not have such a regulatory cost recovery mechanism. For ESPs, the cost of a transaction with a non-creditworthy supplier will increase in light of the additional security provisions that must be put into place.

We accept and adopt the consensus position described in the workshop report that the Commission should not decide or impose any specific credit requirements for any form of capacity contract used for compliance purposes, as those requirements will be determined by the individual companies based upon internal risk controls.

The Workshop Report observes that in certain cases, some LSEs may seek waivers from full RAR compliance should circumstances exist where they cannot secure RAR capacity from providers under terms that satisfy their creditworthiness thresholds. Parties may propose standards for waivers in the next phase of this rulemaking. We make the following observations pending our review of any such proposals. First, we agree with and accept PG&E's recommendation that an LSE requesting a waiver would need to show, at a minimum, that no counterparties were reasonably available to the LSE and no other alternatives (such as another LSE, intermediary, or Generator) were available. We also agree with and accept PG&E's proposal that an LSE that is granted a waiver on the basis of unavailability of creditworthy providers would be responsible for applicable CAISO backstop procurement costs but not

responsible for a penalty. As WPTF points out, the risks of non-performance may be minimal with respect to capacity as distinct from the provision of energy. Thus, it would be appropriate to consider the risk to the buyer of default and the appropriate collateral requirement for that risk in evaluating either individual waiver requests or *ex ante* standards for waivers. Finally, we agree with the comments of TURN and WPTF suggesting that creditworthiness issues may be adequately addressed through commercially available means, and, therefore, that the standard for approval of waivers would be set high.

**3.8. Intermediaries
(Staff Report II.A.8.)**

An intermediary is a party in the middle of an RAR capacity transaction chain. Such a party may be a power marketer that secured long-term rights to market the energy and capacity from an asset owner's projects, or it may be another LSE that is seeking to "lay off" some RAR capacity that is surplus for some period of time without completely relinquishing its rights for the capacity in later periods. In other contexts an intermediary may exist because the RAR capacity seller was better able to transact with such an entity due to creditworthiness concerns.

The Workshop Report observes that some parties are concerned that our RAR policies presume that transactions will occur solely between LSEs and generating asset owners, and therefore assume that a contract for RAR capacity can directly impose outage scheduling requirements or other performance obligations on the generating capacity. However, this would not be the case where the generator did not concede those rights in an initial transaction. Accordingly, the report continues, there is a need for clarity in way the RAR

program interacts between the Commission's policies over LSEs and CAISO's policies with respect to QC certification and availability obligations.

Since our prior decisions may not be clear on this point, we hereby state our understanding that intermediaries can provide a valuable function in bringing parties together to achieve economically efficient transactions, and that the use of intermediaries is approved. We do not assume that LSEs will only secure QC directly from asset owners. LSEs have an obligation to procure QC, and generating assets providing QC carry availability obligations directly to the CAISO irrespective of which entity currently holds the capacity rights. As the Workshop Report notes, this transfer of obligation should result in a greater ability of RAR capacity to move in a secondary market for the standardized product.

3.9. Pooling Of Assets and Substitution (Staff Report II.A.9.)

The Workshop Report observes that pooling a portfolio of units with specific unit identification can help reduce the seller's counting risks and allow optimization of the generation fleet over different times of the year. An inability to pool assets or restrictions on capacity substitution may result in less generation being made available to the market, the report goes on to observe. Notwithstanding their benefits, the report states, there is uncertainty regarding both pooling and substitution of assets.

In pre-workshop comments, Constellation suggested that the specific procedures for qualification of pooled assets as capacity resources used by the New York Independent System Operator (NYISO) be adopted. SCE suggested that the Commission allow LSEs to substitute qualifying capacity from resources

up to the month-ahead showing. Energy Division suggested that the current "busbar rule" be expanded to the plant level.

With respect to the pooling of assets, the CAISO suggested that it must know which units will be available to commit and control in day-ahead and real-time. Accordingly, the CAISO takes the position that RAR resources must be identified in the month-ahead reports so that it can configure the specific resources into its systems, as necessary, and effectively run the grid. The CAISO cannot support proposals that would move identification of the specific resources to anything closer than the month-ahead showing. As appropriate, the CAISO could consider the concept of pooling/portfolio RAR in the context of its Market Redesign and Technology Update (MRTU) process.

With regard to substitution of assets for fulfillment of Local RAR, the CAISO believes that it must have full authority to determine whether a substitution can be made since the information and knowledge to do so is the purview of the CAISO. The report notes that a substituted unit does not necessarily have to be at the exact same "busbar" but it must be electrically equivalent to the substituted-for unit and provide comparable benefits to the transmission system. If allowed, any substitution would be evaluated by the CAISO on a case-by-case basis and subject to the particular transmission configuration and resources already operating. Substitution allowed without professional and prudent evaluation could lead to CAISO re-dispatch, resulting in undesirable cost shifts and/or market manipulation opportunities.

We approve and adopt the CAISO's proposal regarding substitution. Thus, we do not allow substitution for Local RAR but we do allow it for System RAR. As PG&E points out, and as the CAISO acknowledges, substitution could affect the ability of the CAISO to evaluate efficacy of LSEs' aggregate local

procurement, and, therefore, the need for backstop local procurement by the CAISO. While substitution of System RAR resources should be permitted up to the month-ahead showing, we will not allow pooling or substitution of resources for fulfillment of Local RAR.

We will not approve use of the NYISO procedures for pooling at this time. As suggested by the CAISO, this topic may be revisited after the MRTU process is implemented and an integrated day-ahead market is functioning.

3.10. Regulatory Uncertainty (Staff Report II.A.10.)

The Workshop Report states that it is difficult to reflect in contracts what happens in the event of a major regulatory change such as a revised counting rule or testing requirement. This regulatory uncertainty, the report observes, pertains to both single year and multi-year contracts. Some parties believe the California track record is particularly poor on this point, and all parties would like to see regulatory stability that is sufficient to encourage the signing of multi-year deals.

The Workshop Report states that there is apparent consensus that the Commission and the CAISO should each adopt a policy whereby any regulatory changes to their respective RAR programs that could be significantly disruptive would only become effective through a phase-in basis or prospectively after the completion of the current RAR year-ahead compliance cycle. The report goes on to state that market participants should be given ample opportunity to participate in formal proceedings that seek to change market rules.

We recognize the concerns about the need for stability and certainty in our RAR program. Changing the rules of the program too frequently, or with too little sensitivity to the needs of the contracting parties for regulatory stability,

could discourage contracting and subvert our RAR program goals. On the other hand, we must recognize that the RAR program is in its beginning stages, and any RAR program element that proves to be unworkable, unnecessarily costly, outdated, or ineffective should not be maintained solely in the pursuit of regulatory certainty.

It is our intention to continue to pursue any additions and refinements to our RAR program through an open, participatory process where all stakeholders can register their concerns, offer their proposals, and advise us if a proposed action would be disruptive or undermine contracting. While we cannot make blanket pronouncements that are binding upon future Commissions, we intend to consider the need for reasonable stability and certainty so that contracting parties can negotiate terms and conditions in reasonable reliance upon the continued existence of the RAR program elements. Finally, we recognize that phase-in mechanisms designed to ameliorate or avoid significant disruptions, such as the phase-in of the requirement for unit-specific contracts that we adopted in D.05-10-042, can be appropriate means of achieving program goals while minimizing transitional burdens on parties. Similarly, we generally concur that program changes and additions that could affect contracting should be implemented prospectively, beginning with the next RAR year-ahead compliance cycle.

3.11. Required Elements of Standardized, Tradable Capacity Products

While we intend to consider a central capacity market approach later in this proceeding, we have recognized that a standardized capacity product that might be developed in the near term would be beneficial to the RAR program's success if it (1) can be readily bought, sold, or traded by and among market

participants, (2) ensures continued availability of the underlying generation resource to the CAISO at the times and places the CAISO needs to be able to call upon the resource, and (3) comports with our RAR program requirements. As noted earlier in this decision, we provided interim guidance in D.05-10-042 by approving five minimum elements of a resource adequacy (RA) capacity product.

Our early experience with the RAR program has shown limited use of capacity products to date, although there has been some use of partial unit RA products. We understand that most LSEs are still using bundled capacity and energy contracts in their RAR compliance filings. Also, the Energy Division reports that in some instances, smaller LSEs have experienced difficulties procuring capacity in the small sizes needed to match their loads.

To provide additional near-term guidance to parties that could promote the development and use of capacity products, we now revisit the essential elements of a capacity product suitable for the RAR program. We note that doing so is suggested in the comments of a number of parties that urged the Commission to bring these policy topics into a specific focus for standardized, tradable capacity products. Joint Parties, in particular, highlighted our previous attempt in D.05-10-042 and suggested expanding upon the required elements enumerated there by addressing the additional policy topics.⁶ As we do so, we recognize the view advanced by EPUC that discussions on the essential elements of a product remain unresolved, and that this topic will not necessarily be completed in this Phase 1 decision. We nevertheless believe that providing appropriate guidance and direction at this time will be helpful to all parties.

⁶ Joint Parties, April 21, 2006 Comments on Staff Report, pp. 2-7.

Following the general organization of the Staff Report and the Workshop Report, we have addressed ten areas of RAR program clarification and refinement under the heading “RAR Capacity Product.” We recognize, however, that many of these topics apply to all qualifying capacity used by LSEs in compliance filings. For example, the treatment of forced outages is important not only for standardized capacity products, but also for other contracts and even for generating resources owned by LSEs. In Section 3.11 we bring these various elements together in a way that allows for the creation of a standardized, tradable capacity product. In so doing, it is important to note that establishing a set of required elements for a readily traded, standardized capacity product does not preclude LSEs from satisfying RA requirements with resources they own, traditional energy products, or other forms of capacity contracts that comply with the requirements established in this and previous RA decisions.

The Workshop Report notes that parties affirm the Commission’s action in D.05-10-042 to identify essential contract elements rather than adopt specific contract language. Commercial flexibility is important, so the parties continue to prefer that we adopt required elements that contracts must satisfy and leave contract language to the market participants.

In D.05-10-042, we determined that RA capacity contracts that include five identified minimum elements would qualify as eligible contracts that LSEs can rely upon to meet their procurement obligations. We set out these elements not as a comprehensive summary of requirements that all contracts or qualifying capacity must satisfy, but as a means of fostering a “readily transferable capacity contract.”⁷ In their opening comments and at the March 27, 2006 workshop, parties told us we had not succeeded in creating sufficient clarity to encourage

⁷ D.05-10-042, p. 26.

such contracts. To reduce contracting risk and encourage development of RA capacity products and their use by LSEs in satisfying their procurement obligations, we now revise and expand the minimum elements of an RA capacity contract that would qualify for System and Local RAR. We build upon the list of required elements established in D.05-10-042, incorporating policies resolved earlier in this decision and refining some of the particulars from the earlier list. Capacity products that conform to these elements will be accepted for purposes of Year-Ahead and Month-Ahead compliance filings by LSEs for both System⁸ and Local RAR starting in year 2007. For the sake of clarity, we repeat here that these are the elements of a standard, tradable capacity product, and that qualifying capacity does not necessarily have to meet these elements.

We intend and expect that establishing these essential elements will be a contribution towards development of a standardized, tradable RAR Capacity Product. By resolving the specific, outstanding issues that the parties identified as barriers to the establishment of standardized, tradable capacity products, the commercial market should now be able to establish such products. Perhaps more importantly, we believe that we are now establishing a set of requirements that will allow capacity products to be resold, subdivided following their initial creation, and handled by market intermediaries.⁹ By fostering the development

⁸ D.05-10-042 determined that system requirements may be satisfied with generating units located within the CAISO control area and by imports from other control areas, subject to certain limitations. The required elements described in this decision address only generating units located in the CAISO control area. We will examine extensions of these required elements to address imports in Phase 2.

⁹ In keeping with an explicit desire to foster reselling and trading, we depart from terminology commonly used by the parties in their comments. We use "holder" to replace "buyer" and we use "generator" to replace "seller." We use this terminology to specifically communicate that it is the current Holder of a standardized capacity product that may use the capacity for compliance filings. Likewise, it is the original

of this specialized form of qualifying capacity, as one option among several that LSEs can choose from, we hope to lubricate market transactions, especially those associated with load migration between LSEs.

Accordingly, we hereby determine that a standardized, tradable capacity product that possesses all of the following four broad categories of requirements and their specific elements shall qualify as a resource that LSEs can use to satisfy their RAR procurement obligations, provided the underlying generator satisfies the general obligations applicable to qualifying capacity when used for RA compliance purposes. Going forward, for future compliance filings beginning with the 2007 compliance year, these requirements replace those enumerated in D.05-10-042, pp. 27-28, in their entirety.

We note that IOU procurement is carried out pursuant to Long Term Procurement Plans (LTPPs). In order not to delay the IOUs' contracting for RA capacity for 2007, we provisionally approve their use of RA products that meet the terms of this decision for 2007 procurement. We direct the IOUs to amend their LTPPs to provide details of how they will use RA products in 2007. By taking this approach, we ensure that the IOUs maintain their LTPPs with up-to-date information about their approved procurement products while avoiding unnecessary delay in the contracting process that will occur in the immediate future.

Generator that is always subject to the requirements to provide the capacity to the CAISO under the conditions of the standardized product, irrespective of how many times the product has been sold to different LSEs or market intermediaries. It is the current Holder of the capacity that is allowed to count it towards satisfying our RAR requirements. While buyer and seller are descriptive of the two sides of a specific market transaction, Holder and Generator are preferable terms to use in this context.

In comments on the draft decision, each of the IOUs suggested that LSEs should be allowed to unbundle the local and system resource adequacy attributes from a given unit. In reply comments, NRG supported this approach while Mirant strongly disagreed with it. Unbundling local and system attributes is not consistent with D.06-06-064, in which we recently decided not to allow unbundled products to count for local resource adequacy counting purposes. Accordingly, we decline to allow unbundled products to be part of the standardized tradable product that can count for local or system resource adequacy.

Category 1 - Required Features of RAR Capacity

1. Capacity must meet the counting protocols adopted by the Commission in D.04-10-035, in D.05-10-042, and as modified in subsequent Commission decisions. These counting protocols are reflected in the net qualifying capacity list published approximately July 1 each year in advance of the Year-Ahead compliance filing process. An RA Capacity product is a quantity of capacity that is intended for satisfying RAR obligations and has no associated energy entitlement. The aggregate of all RA Capacity products from a specific generator is less than or equal to the net qualifying capacity of that generator to be used for the Year-Ahead compliance filing process.
2. An RA Capacity Product is denominated in any size, with the minimum of one megawatt, and is specific to an individual generating unit.
3. An RA Capacity Product has a time interval of one individual calendar month.
4. An RA Capacity product:
 - a. is valued for RAR compliance purposes using the net qualifying capacity list¹⁰ designated by the Commission for the Year-Ahead compliance filing process,

¹⁰ As noted earlier, while some identifying fields in this list may change during the course of the year, the QC itself will not change.

- b. is always written for a single generating unit and the magnitude of the Capacity Product can never be larger than the total qualifying capacity of the generating unit for the month as enumerated on the qualifying capacity list then being used for compliance purposes, and
 - c. sold for periods further forward than the compliance year for a Commission designed net qualifying capacity list is subject to rerating based on the outages and performance of the underlying generating unit, and capacity product Holder and Generator must assign responsibility for such risk as part of the commercial terms of the transaction.
- 5. An RA Capacity product may not be counted for a calendar month listed for planned outages confirmed through the CAISO outage scheduling process unless its outage is planned for less than the thresholds established in Section 3.1 of this decision. To the extent that a CAISO-initiated outage scheduling change subsequent to the CAISO approved outage schedule renders a generator unit unqualified to provide RA capacity, then the RA Capacity product retains its original value. CAISO denial of a proposed outage during the annual generator outage scheduling process does not constitute a change that affects RA capacity.
- 6. Generators shall maintain and operate any generating unit used to establish RAR Capacity Product as follows:
 - a. all units shall follow "Good Utility Practice," as defined in the CAISO Tariff,
 - b. any unit subject to Commission GO 167 shall conform to the requirements of that Order, and
 - c. it is understood that maintenance of generating units shall not include any excessive obligation that the generator undertake major capital improvements, facility enhancements, or the construction of new facilities.
- 7. Parties transacting RA Capacity Products agree to negotiate in good faith to make necessary amendments, if any, to their agreements to conform to subsequent clarifications, revisions or decisions issued by the Commission or conform to CAISO tariffs, to maintain the benefits of the bargain struck by the Parties.

Category 2 - Deliverability Determinations

In order to satisfy compliance requirements, RA Capacity Products must meet the deliverability requirements as determined by the Commission and the CAISO.

Category 3 - Compliance with CAISO Unit Commitment and Dispatch Requirements and other CAISO Tariff Requirements

In order to satisfy compliance requirements, RA Capacity Products must meet the unit commitment and dispatch requirements as determined by the CAISO, along with other informational reporting requirements established by the Commission and the CAISO.

Category 4 - Additional Requirements Concerning Trading and Use of RAR Capacity Product

1. The same RA Capacity Product cannot be sold to more than one Holder at a time, i.e. double-selling is prohibited. Holder has exclusive rights to count the RA Capacity toward Holder's RAR. To assure this:
 - a. Generator warrants that the aggregation of all quantities from a generating unit does not exceed the net qualifying capacity of the generator.
 - b. Generator is liable for replacement of any capacity disallowed by CAISO or Commission resulting from the LSE compliance filing review processes in which an investigation of double counting has cleared the LSE of any error. Such replacement must be from generators that are eligible to satisfy the intended use of the RA Capacity by the LSE to satisfy RAR, whether system or local.¹¹ Notice of investigations of alleged double selling will be provided to generators and affected generators may participate in the investigation.
2. Original Holder can transfer title to RA Capacity obtained through a standard, tradable capacity product to any other market participant and all rights provided to the original Holder or the CAISO are automatically transferred to subsequent Holders.

¹¹ If the disallowed capacity was meant to fulfill local RAR, replacement must be from another generator listed on the QC list for that same Local RAR area.

3. Holder may subdivide any RA Capacity without limit provided:
 - a. the quantity of any resulting RA Capacity product is not less than one megawatt, and duration is not less than one month beginning the first day of the month and ending the final day of the month,
 - b. all new Holders and original Generator agree to accept all terms and conditions necessary to satisfy Commission Elements for standardized RA Capacity, including CAISO tariff requirements and
 - c. the sum of all RA Capacity held by new Holders shall exactly match the original quantity sold in the transaction, e.g., a single RA Capacity product of 15 megawatts (MW) can become two RA Capacity products of 5 MW and 10 MW.

In comments on the draft decision, numerous parties expressed the desire for modifications to this list of elements to assure the flexibility they perceived necessary to use specific resources they already possess in satisfying system and local RA requirements. These parties may have misunderstood the intended applicability of this list, thinking its applicability is broad rather than narrow. To clarify our intent regarding the applicability of this list, we have therefore modified it to focus it exclusively on the required elements of a standardized, readily tradable capacity product. Drawing upon the list of essential elements that was included in the draft decision, we now enumerate RA certain program requirements applicable to all qualifying capacity. The following list is intended to be useful to the LSEs needing to satisfy our requirements, but it is not comprehensive. Establishing a complete enumeration of our requirements will be accomplished when we develop a General Order for resource adequacy. For now, the following list must be viewed in conjunction with D.04-10-035, D.05-10-042, D.06-06-064 and the associated workshop reports preceding these decisions to establish all of the requirements on LSEs and the nature of the resources they may use to satisfy RA requirements.

**General Requirements for Qualifying Capacity
(Partial List - See D.04-10-035, D.05-10-042, and D.06-06-064
for Full List of Requirements for Qualifying Capacity)**

1. Qualifying capacity for generators for RA purposes is set forth in a net qualifying capacity list established by the CAISO.
2. Qualifying capacity retains the value set forth for it on the net qualifying capacity list designated by the CPUC for the compliance year irrespective of forced outages or unit performance during the compliance year.
3. In order to satisfy compliance requirements, RA Capacity must meet the deliverability requirements as determined by the Commission and the CAISO.
 - a. A generating unit listed on the net qualifying capacity list designated by the Commission for the Year-Ahead compliance filing process is deliverable for system RAR for all months of that compliance year,
 - b. Only a generator listed on the qualifying capacity list designated by the Commission for that compliance year, and listed as located in a Local Area, is deliverable for Local RAR for that Local Area or aggregate local pocket requirement throughout the compliance year.

**Compliance with CAISO Unit Commitment and Dispatch
Requirements, and Other Information Reporting
Requirements**

1. Generating units used to satisfy RA requirements must be subject to all applicable CAISO Tariff requirements, including submitting supply schedules.
2. Unless the generating unit used to satisfy RA requirements is forced out of service, is undergoing planned maintenance or is affected by an event of *force majeure* that results in a partial or full outage of that unit, the generating unit must be made available to the CAISO as outlined by the Commission. Namely, RA Capacity must be made available to the CAISO for all hours of every day of the contract term in the following manner:
 - a. The generating unit from which the RA Capacity is derived must be self-scheduled by the unit's scheduling coordinator for energy delivery within the CAISO control area up to the amount of all RA Capacity sold from that unit, and any amount of RA Capacity not so

scheduled is subject to the provisions of (b) – (e) listed below. In the event of a discrepancy between the RAR filings and the Supply Plans submitted to the CAISO, generating unit Scheduling Coordinators must endeavor to assist the CAISO to resolve any discrepancies between the CAISO Supply Plans and the RAR filings, including amendment of their Supply Plans.

- b. Once established, Capacity must be bid into the CAISO’s MRTU Day-Ahead Integrated Forward Market if not already scheduled.
 - c. Once established, Capacity must be subject to the CAISO’s Residual Unit Commitment (RUC) process if the bid is not accepted. Capacity must submit a zero dollar (\$0) bid into RUC. Capacity will not be eligible for any RUC availability payment or revenue.
 - d. In the pre-MRTU period, Capacity must be made available to the CAISO subject to the FERC’s original Must Offer Obligation (FERC MOO) process or its successors.¹² In the event of a Must Offer Waiver Denial (“MOWD”) by the CAISO, the unit’s Scheduling Coordinator shall submit supplemental energy or Ancillary Service bids to the CAISO.
 - e. If the FERC MOO is no longer operative, Capacity shall be made available to the CAISO as follows: (1) the CAISO shall have the right to commit any type of Units on a Day-Ahead basis; and (2) the CAISO shall have the right, on an intra-hour or Hour-Ahead basis, to call on supplemental energy and/or Ancillary Services from only those Units whose start-up time permits such a call.
3. Generating Units must conform to all applicable CAISO data collection, testing, and reporting requirements as well as all Commission information reporting requirements.

**Use of Capacity to Satisfy an LSE’s System and
Local RA Requirements**

1. Capacity derived from a generating unit listed on the net qualifying capacity list designated by the Commission may be used to satisfy an LSE’s RAR as follows:

¹² The FERC MOO process continues to evolve from its original form established by FERC order in June 2001.

- a. RA Capacity from any generating unit can be used to comply with an LSE's system RAR.
 - b. Capacity derived from any generating unit attributed to a local area can be used to satisfy local RAR for that local area or any aggregation of local areas established by the Commission as part of local RAR.
 - c. Capacity used by an LSE to satisfy Local RAR must also be reported by that same LSE to satisfy System RAR. There is to be no separation of system and local credit of units between LSEs for purposes of System and Local RAR compliance. Units may sell partial capacity to different LSEs, but cannot sell the same local RA Capacity and system RA Capacity to different buyers.
2. All non-IOU LSEs may buy and sell RA Capacity Products in order to meet Commission requirements by using bilateral contracts, bulletin boards, exchanges and other commercial mechanisms.
 3. In month-ahead compliance filings, in satisfying system RA requirements, any RA Capacity Products may be substituted for equivalent amounts of resources that were accepted as part of an LSE's Year-Ahead compliance filings.

4. Implementation Issues (Staff Report III.)

The Scoping Memo provided that certain RAR "implementation issues" could be taken up in Phase 1. These are "program gaps or deficiencies" that were identified during the initial implementation activities for System RAR earlier this year (both for "year-ahead" and for "month-ahead" System RAR) and which require Commission resolution as soon as possible, and in particular before LSEs' compliance filings for 2007 are due.

4.1. Filing Guide and Templates (Staff Report III.A.; V.)

The Staff Report invited parties to comment on the Energy Division's recently issued RAR filing guides, associated templates, frequently asked

questions, and errata for the 2006 year-ahead and month-ahead compliance filings. These materials were attached to the Staff Report as appendices.

PG&E suggests that the templates be modified to provide the ability to specify or highlight limitations associated with legacy contracts. PG&E is concerned that inclusion of a resource on a particular spreadsheet tab that does not fit the resource well may lead to misunderstanding. Our Energy Division informs us that the reporting requirements can and will be modified to address this concern.

SCE notes that the templates require LSEs' officers to certify that (a) they have responsibility for the activities reflected in the filings; (b) they have reviewed the compliance filing; (c) based on their knowledge, the filing does not contain any untrue statements; and (d) based on their knowledge, the filing contains all of the information required to be provided by Commission orders and regulations. Since compliance filings can be lengthy, SCE believes some modification is necessary to reflect the concern that officers cannot, based on their own knowledge, reasonably attest to every element of the factual information in the filing. SCE proposes the following modifications to Statements 2, 3, and 4 of the verification, which we hereby approve and adopt as being consistent with Rule 2.4 of our Rules of Practice and Procedure.

2. I have reviewed, or have caused to be reviewed, this compliance filing.
3. Based on my knowledge, information, or belief, this filing does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements true.
4. Based on my knowledge, information, or belief, this [filing] contains all of the information required to be provided by Commission orders, rules, and regulations.

With the revisions described above, we approve the RAR filing guides and templates and instructions developed by the Energy Division as representing the appropriate implementation of our RAR decisions to date. We further authorize the Energy Division to modify those templates and instructions and promulgate additional filing procedures and instructions as necessary for the orderly implementation of the adopted RAR program, both for system and for local requirements, and the changing needs of the program. We clarify here that failure of an LSE to submit a compliance filing in accordance with the filing instructions and reporting templates promulgated by the Energy Division may be deemed a violation of a Commission order.

**4.2. Maximum Cumulative Capacity
(Staff Report III.B.)**

SCE's March 13, 2006 comments requested that we adjust the year-ahead templates so that the Maximum Cumulative Capacity (MCC) calculation would be 103.5% (90% of 115%) of the peak hour load of an LSE's load forecast. In addition, SCE suggested that the MCC's should be based upon 115% of peak hour load for both year-ahead and month-ahead for consistency. In the Staff Report, the Energy Division suggested that, going forward, the calculation of the LSE obligation for each resource category, for both year-ahead and monthly RAR showing, should be based on the LSE's RAR (115% of forecast load). We approve this uncontested adjustment.

Constellation requests a clarification with respect to adjustments for load migration for Local RAR. However, in our recent decision on Local RAR we determined that monthly filings would not be required for the local program component.

4.3. Accounting for Transmission Losses (Staff Report III.C.)

The current method for dealing with transmission losses uses the simplifying assumption of increasing an LSE's load forecast by a flat 3%. In its March 13 comments, SCE requests that for the 2007 RAR showing, transmission losses be incorporated through the application of loss factors to resources and that all resources and loads be adjusted to a common reference point – the CAISO grid. SCE notes that its method would encourage LSEs to contract with resources located near their load. Since the current approach effectively assigns a common loss factor that does not consider the actual transmission losses associated with a particular resource, an LSE that has contracted with a resource that is close to its load is treated the same as a similarly situated LSE that has contracted with a resource that is outside the state even though the latter resource incurs higher transmission losses than the local resource to deliver energy to the LSE. SCE maintains this is not efficient and results in unfair subsidies.

Constellation and the CAISO point out that SCE's approach would add administrative complexity to the RAR program. Constellation also notes that because the RAR capacity is unbundled from the energy deliveries, and because the CAISO may dispatch one LSE's RAR capacity to cover system conditions triggered by another LSE's loads, the perceived benefits of efficiency and fairness are not clear.

Resolving this issue requires a balancing of the objectives of administrative simplicity and accuracy in resource counting protocols. Since the net benefits of SCE's proposed approach are unclear, but it is clear that it would add administrative complexity that could be costly for participants as well as the

Commission and the CAISO to administer, we choose not to approve this approach at this time.

4.4. Process for Resolving Discrepancies (Staff Report III.D.)

In its Interim Reliability Requirements (IRR) tariff filing with the FERC, the CAISO, in response to stakeholder comments, has proposed parameters of the role it would assume in resolving discrepancies between the CAISO's Monthly Supply Plan submitted by generators and the LSE's monthly showings. Key to this process would be the CAISO's contact with the Scheduling Coordinator of each entity and attempt to resolve the discrepancy before reporting any LSE deficiency to the Commission.

In comments submitted on March 13, Alliance for Retail Energy Markets requests that the Commission determine a process for resolving such discrepancies. No party has identified a need, or submitted a proposal to address any such need, for this Commission to establish a dispute resolution process at this time that would specifically address disputes not resolved through the process proposed in the CAISO's IRR tariff. We therefore defer any action on this topic at this time. We note that our staff is working with the CAISO to resolve discrepancies.

5. Comments on Draft Decision

On June 20, 2006, the draft decision was filed and served on parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7 of the Commission's Rules of Practice and Procedure. Comments on the draft decision were filed by AReM, CAISO, Calpine Corporation, CMTA/CLECA, Constellation, Cogeneration Association of California, DRA, PG&E, Powerex, SDG&E, SCE, and WPTF. Replies to these comments were filed by AReM, CAISO,

Constellation, Mirant, NRG, PG&E, Powerex, SCE, and TURN. We have made certain modifications to the draft decision that were suggested in the comments. Among other things, we have restated the essential elements of a tradable capacity product (Section 3.11) to provide clarification regarding elements that are specific to the standardized capacity product and those that are broadly applicable RAR program requirements. We have also corrected certain drafting errors that were noted in the comments. We have not adopted the proposal by the IOUs to unbundle “system” and “local” attributes of a standard, tradable capacity product.

6. Assignment of Proceeding

Michael R. Peevey is the Assigned Commissioner and Mark S. Wetzell is the assigned Administrative Law Judge for this proceeding.

Findings of Fact

1. A “forced is forced” policy whereby LSEs would be able to rely upon the QC of a unit that is established by the CAISO for a given RAR compliance year, and not incur a penalty or replacement obligation in the event of a forced outage of that unit, is consistent with our prior RAR decisions establishing a planning reserve requirement.

2. Because the reserve margin requirement adopted in D.04-01-050 encompasses forced outages, requiring LSEs to engage in replacement procurement following a forced outage would effectively require them to procure more than the adopted reserve margin.

3. LSEs need to know the extent to which the resources they acquire and use for their RAR compliance showings will count toward meeting their procurement obligation.

4. The Commission understands and expects that the CAISO will establish and publish a list of generating units and the QC for those units.

5. In order for LSEs and others to make informed decisions regarding the products they will use in their upcoming year-ahead compliance filings, the QC for any generator needs to be established approximately 90 days before the year-ahead compliance filing is due, or on or about July 1.

6. The imposition of QC adjustments on a regular cycle and the potential for suppliers to lose a quantity of product they would otherwise be able to sell in the RAR market provide an incentive for suppliers to maintain the availability of capacity.

7. RAR violations will be handled first through action by the Energy Division such as a notification letter providing the LSE with a limited time to resolve the violation, and then, if the LSE fails to do so, the Energy Division would recommend that the Commission initiate an enforcement proceeding.

8. While General Order 167 adequately addresses maintenance and repair obligations for those units to which it applies, it is reasonable to require that all suppliers of qualifying RAR capacity agree to follow Good Utility Practices as defined in CAISO tariffs and to comply with all applicable laws, regulations, and standards regarding maintenance and repair.

9. A bulletin board on which bids and offers for qualifying RAR capacity are posted would be a useful tool for promoting transparency and liquidity in the market.

10. With respect to qualifying imports as a tradable capacity product that counts for RAR, it is more appropriate to use specific elements of the transmission requirement in the counting protocol for imports rather than the designation "firm."

11. Intermediaries can provide a valuable function in bringing parties together to achieve economically efficient transactions.

12. The CAISO needs full authority to determine whether a substitution of assets can be made since the information and knowledge to do so is in its purview.

13. Changing the rules of the RAR program too frequently, or with too little sensitivity to the needs of the contracting parties for regulatory stability, could discourage contracting and undermine RAR program goals.

14. A standardized capacity product that might be developed in the near term would be beneficial to the RAR program's success if it (1) can be readily bought, sold, or traded by and among market participants; (2) ensures continued availability of the underlying generation resource to the CAISO at the times and places the CAISO needs to be able to call upon the resource; and (3) comports with our RAR program requirements.

15. Establishing essential elements of an RA Capacity contract that qualifies toward meeting an LSE's procurement obligation could contribute to the development of a standardized, tradable RA Capacity Product.

16. The compliance filing templates developed by the Energy Division can be modified to provide the ability to specify or highlight limitations associated with legacy contracts.

17. SCE's proposed modifications to Statements 2, 3, and 4 of the compliance filing verification are consistent with Rule 2.4 of the Rules of Practice and Procedure.

18. The proposed adjustment to the MCC calculation whereby the LSE obligation for each resource category, for both year-ahead and monthly RAR showing, is based on the LSE's RAR (115% of forecast load), should be approved.

19. SCE's proposed approach to accounting for transmission losses would add administrative complexity that could be costly for some participants as well as the Commission and the CAISO to administer.

20. In its IRR tariff filing, the CAISO has proposed parameters of the role it would assume in resolving discrepancies between the CAISO's Monthly Supply Plan submitted by generators and the LSE's monthly RAR showings.

Conclusions of Law

1. The Commission should not hold LSEs accountable for changes in a resource's QC that may be identified by the CAISO after the list is established on or about July 1 of each year; thus, for the applicable RAR compliance year, LSEs should not be subject to any Commission-imposed penalty or Commission-imposed replacement procurement obligation as the result of a forced outage of a unit that was on the CAISO's QC list and used by the LSE in fulfillment of its RAR procurement obligation.

2. Because the reserve margin adopted in D.04-01-050 encompasses forced outages, LSEs should not be required to engage in replacement procurement following a forced outage.

3. The consensus QC counting protocol for scheduled outages that is set forth in the foregoing discussion should be adopted.

4. For purposes of the RAR program, unit derates during an RAR compliance year should be reflected in the next year's QC list.

5. The Commission should not decide or impose any specific credit requirements for a standard capacity product, as those requirements will be determined by the individual companies based upon internal risk controls.

6. The Commission intends to continue to pursue any additions and refinements to the RAR program through an open, participatory process, with due consideration of the need for reasonable program stability and certainty.

7. To reduce contracting risk and encourage development of RAR capacity products and their use by LSEs in satisfying their procurement obligations, the required elements of a standard RA capacity contract set forth in the foregoing discussion should be approved in place of the contract elements approved in D.05-10-042. Capacity products that conform to these elements will be accepted for purposes of Year-Ahead and Month-Ahead compliance filings by LSEs for both System and Local RAR.

8. The RAR filing guides and templates and instructions developed by the Energy Division should be approved, and the Energy Division should be authorized to modify those templates and instructions and promulgate additional filing procedures and instructions as necessary for the orderly implementation of the adopted RAR program and the changing needs of the program.

9. Failure of an LSE to submit a compliance filing in accordance with the filing instructions and reporting templates promulgated by the Energy Division may be deemed a violation of a Commission order.

O R D E R

IT IS ORDERED that:

1. The Commission's Resource Adequacy Requirements program is modified and clarified as set forth in the foregoing discussion, findings of fact, and conclusions of law.

2. The Executive Director shall ensure that Commission staff undertakes the activities identified for staff in the foregoing discussion, findings, and conclusions.

3. Pacific Gas and Electric Company, San Diego Gas & Electric Company, and Southern California Edison Company (the IOUs) are authorized to use resource adequacy (RA) capacity products that meet the terms of this decision for 2007 procurement. The IOUs shall, on or before September 1, 2006, amend their Long Term Procurement Plans to provide details of how they will use RA products in 2007.

4. Phase 1 of this proceeding is concluded; the proceeding remains open for consideration of issues listed in the Scoping Memo that are not resolved by Decision 06-06-064 or by today's order.

This order is effective today.

Dated July 20, 2006, at San Francisco, California.

MICHAEL R. PEEVEY
President
GEOFFREY F. BROWN
DIAN M. GRUENEICH
JOHN A. BOHN
RACHELLE B. CHONG
Commissioners