

**M e m o r a n d u m**

**Date:** April 17, 2008

**To:** The Commission  
(Meeting of April 24, 2008)

**From:** Pamela Loomis, Deputy Director  
Office of Governmental Affairs (OGA) — Sacramento

**Subject:** **SB 1536 (Dutton) – Electrical restructuring: Power Exchange (PX)**  
**As amended: March 24, 2008**

**LEGISLATIVE SUBCOMMITTEE RECOMMENDATION: SUPPORT WITH AMENDMENTS**

**SUMMARY OF BILL:**

This bill would update the Public Utilities Code (PU Code) to reflect current state of electric markets in California. This bill would remove references to duties assigned to the Power Exchange (PX) as an electric market operator (though the bill would preserve the PX for purposes of winding up operations in bankruptcy). Additionally, this bill would update the definition of an “exempt wholesale generator” to align with the Public Utility Holding Company Act of 2005, as opposed to the now defunct Public Utility Holding Company Act of 1935.

**SUMMARY OF SUPPORTING ARGUMENTS FOR RECOMMENDATION:**

- This bill would eliminate potential confusion resulting from legislation that refers to the PX, which no longer functions in the energy market. Additionally, by synchronizing definitions with federal legislation, this bill will permit close a potential legal loophole created by the different definitions. Lastly, this bill would make clear that the authority initially granted to the PX, where applicable, is now granted to the California Independent System Operator (CAISO). SB 1536 would bring California law in line with federal law.

## SUMMARY OF SUGGESTED AMENDMENTS:

- The California Public Utilities Commission (CPUC) recommends the following amendments:
  - Remove Section 6 of the bill. Section 6 amends Section 339 of the Public Utilities Code, removing references to the PX in a listing of subjects under the California’s “exclusive jurisdiction.” There are ongoing proceedings involving the PX, and the removal of explicit state jurisdiction may remove some tools that were previously at the disposal of the state. The CPUC does not believe there to be substantial cost to maintaining the present references to the PX in Section 339 of the Public Utilities Code. This language does not prescribe any duties to the PX; rather, Section 339 of the Public Utilities Code only establishes state authority. Given the potential benefit of maintaining Section 339 of the Public Utilities Code, and the lack of costs, the CPUC suggests that SB 1536 be amended to remove Section 6, therefore preserving the language of Section 339.
  - Remove Section 9 of the bill If Section 6 is removed. The language that Section 9 of the bill proposed to remove from Section 341.5 of the Public Utilities Code requires that the state authority defined in Section 339 of the Public Utilities Code be reflected in the PX and CAISO bylaws. The bill, as proposed, eliminates references to the PX in both Section 339 and Section 341.5 of the Public Utilities Code. The CPUC believes that if Section 6 of the proposed bill is repealed, therefore preserving the language in Section 339 of the Public Utilities Code, then the language in Section 341.5, which is based on Section 339, should be preserved as well.
  - Restore Section 18 of the bill. On March 24, the bill was amended to delete the proposed repeal of Section 390 of the Public Utilities Code. This change limits the extent of the bill, preserving the short run avoided cost energy methodology related to the PX. The CPUC suggests that the amendment be removed, and Section 390 of the Public Utilities Code be repealed.

Section 390 was adopted as part of AB 1890, California’s electric industry restructuring law of 1996. Among other things, it mandated that the short-run avoided cost (SRAC) energy payments by utilities to Qualifying Facilities (QFs) would be based on the clearing price paid by the PX once that entity was deemed to be functioning properly. Until that time, SRAC energy payments would be based on a “transitional” formula which was tied to California natural gas border price indices. With the failure of the PX, this “transitional” formula is now the permanent method for determining SRAC energy prices. So long as Section 390 remains in effect, the Commission’s ability to establish SRAC energy prices remains tied to the California natural gas border indices, regardless of whether these indices represent the competitive market.

- The CPUC believes this bill is an appropriate bill to repeal Section 390. CPUC believes that, in addition to other “clean up” being conducted through this bill, Section 390 should be repealed as well. Section 390 was enacted based on the premise that a functioning PX would eventually be used to establish SRAC energy payments. As with the other Public Utilities Code provisions to be revised or repealed in this bill, these duties can no longer be performed by the PX, since it no longer exists. CPUC believes that, once Section 390 is repealed, the CPUC will have the discretion and ability to consider a greater range of options for establishing SRAC energy payments.
- In past legislative sessions, the CPUC has recommended that Section 390 be repealed, a position the CPUC continues to support. However, the CPUC’s support of this bill is not contingent on the removal of the amendment; even if the repeal of Section 390 is not included in the bill, CPUC still supports the bill.

#### **DIVISION ANALYSIS (Energy Division):**

- On the subject of the PX, the bill would bring the text of the law in line with present practice. While the CPUC and California Independent System Operator (CAISO) presently operate without the PX, the actual text of the Public Utilities code has not been updated. The bill would solidify current practice and eliminate text of the law that no longer applies.
- On the subject of the “exempt wholesale generator,” the current law refers to a federal designation that has been replaced. The Public Utility Holding Company Act of 1935 has been replaced by the Public Utility Holding Company Act of 2005, so the previous designation no longer exists. The change in California law proposed in the bill would recognize the current federal definition, avoiding potential loopholes or legal uncertainties. It is unclear if this is necessary for the new federal definition to be applied, but would resolve the issue with certainty.
- Given the complexity of electric policy and regulation, having clarity in the Public Utilities Code will be valuable.

#### **PROGRAM BACKGROUND:**

- Electric Restructuring in California included plans for two separate entities- the CAISO that would operate the grid and the PX that would run a day-ahead market. The PX went bankrupt in 2001, and the CAISO has been the sole operator of a centralized market in California ever since. In the enabling legislation for the restructuring of the electricity industry (AB 1890), the PX is explicitly referenced and assigned duties involved both in the transition to competitive markets and the ongoing operation of this market. Now that the PX no longer exists, many of these roles are currently fulfilled by the CAISO.

- This legislation would not require any reports or other action by the CPUC.

**LEGISLATIVE HISTORY:**

The bill would bring the letter of the law into line with present practice by the CPUC and the electric sector more broadly.

**FISCAL IMPACT:**

None.

**STATUS:**

On April 14, 2008, SB 1536 was passed by the Senate to the Assembly (Vote: 36-0). The bill is presently in the Assembly Rules Committee awaiting policy committee assignment.

**SUPPORT/OPPOSITION:**

None on file.

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**BILL LANGUAGE:**

BILL NUMBER: SB 1536 AMENDED  
BILL TEXT

AMENDED IN SENATE MARCH 24, 2008

INTRODUCED BY Senator Dutton

FEBRUARY 22, 2008

An act to amend Sections 216, 330, 331, 335, 339, 340, 341.2, 341.5, 359, 361, 365, 367, 373, and 376, of, to repeal Sections ~~338, 367.7, and 390~~ 338 and 367.7 of, and to repeal Article 4 (commencing with Section 355) of Chapter 2.3 of Part 1 of Division 1 of, the Public Utilities Code, relating to the electricity.

LEGISLATIVE COUNSEL'S DIGEST

SB 1536, as amended, Dutton. Electrical restructuring: Power Exchange.

Under existing law, the Public Utilities Commission has regulatory authority over public utilities, including electrical corporations. The existing restructuring of the electrical services industry provides for the creation of the Power Exchange as an incorporated public benefit nonprofit corporation.

This bill would repeal the provisions creating the Power Exchange and repeal *certain* provisions pertaining to the prescribed functions of the Power Exchange. The bill would make conforming changes to existing law by deleting *certain* references to the Power Exchange. The bill would state that it does not preclude a reorganized Power Exchange from winding up its operations pursuant to a plan in bankruptcy and pursuant to orders of the Federal Energy Regulatory Commission.

The existing definition of a "public utility" within the Public Utilities Act provides that ownership or operation of a facility that has been certified by the Federal Energy Regulatory Commission (FERC) as an exempt wholesale generator pursuant to a specified section of the Public Utility Holding Company Act of 1935 does not make a corporation or person a public utility solely due to the ownership or operation of the facility. The existing definition of an "exempt wholesale generator" defined the term by incorporating the definition from the Public Utility Holding Company Act of 1935. The federal Energy Policy Act of 2005 repealed the Public Utility Holding Company Act of 1935 and adopted the Public Utility Holding Company Act of 2005, which includes a definition for "exempt wholesale generator." The definition of a "public utility" provides that ownership, control, operation, or management of an electric plant used for sales into the Power Exchange does not make a corporation or person a public utility solely because of that ownership, participation, or sale.

This bill would delete references to facilities certified by the FERC as "exempt wholesale generators" pursuant to the Public Utility

Holding Company Act of 1935, and would instead reference the definition of that term in the Public Utility Holding Company Act of 2005. The bill would replace the provision in the definition of a "public utility" that provides that ownership, control, operation, or management of an electric plant used for sales into the Power Exchange does not make a corporation or person a public utility with a provision that ownership, control, operation, or management of an electric plant used for sales into a market established and operated by the Independent System Operator or any other wholesale electricity market does not make a corporation or person a public utility solely due to the ownership, participation, or sale.

Vote: majority. Appropriation: no. Fiscal committee: no.  
State-mandated local program: no.

THE PEOPLE OF THE STATE OF CALIFORNIA DO ENACT AS FOLLOWS:

SECTION 1. Section 216 of the Public Utilities Code is amended to read:

216. (a) "Public utility" includes every common carrier, toll bridge corporation, pipeline corporation, gas corporation, electrical corporation, telephone corporation, telegraph corporation, water corporation, sewer system corporation, and heat corporation, where the service is performed for, or the commodity is delivered to, the public or any portion thereof.

(b) Whenever any common carrier, toll bridge corporation, pipeline corporation, gas corporation, electrical corporation, telephone corporation, telegraph corporation, water corporation, sewer system corporation, or heat corporation performs a service for, or delivers a commodity to, the public or any portion thereof for which any compensation or payment whatsoever is received, that common carrier, toll bridge corporation, pipeline corporation, gas corporation, electrical corporation, telephone corporation, telegraph corporation, water corporation, sewer system corporation, or heat corporation, is a public utility subject to the jurisdiction, control, and regulation of the commission and the provisions of this part.

(c) When any person or corporation performs any service for, or delivers any commodity to, any person, private corporation, municipality, or other political subdivision of the state, that in turn either directly or indirectly, mediately or immediately, performs that service for, or delivers that commodity to, the public or any portion thereof, that person or corporation is a public utility subject to the jurisdiction, control, and regulation of the commission and the provisions of this part.

(d) Ownership or operation of a facility that employs cogeneration technology or produces power from other than a conventional power source or the ownership or operation of a facility which employs landfill gas technology does not make a corporation or person a public utility within the meaning of this section solely because of the ownership or operation of that facility.

(e) Any corporation or person engaged directly or indirectly in developing, producing, transmitting, distributing, delivering, or selling any form of heat derived from geothermal or solar resources or from cogeneration technology to any privately owned or publicly owned public utility, or to the public or any portion thereof, is not a public utility within the meaning of this section solely by reason of engaging in any of those activities.

(f) The ownership or operation of a facility that sells compressed natural gas at retail to the public for use only as a motor vehicle fuel, and the selling of compressed natural gas at retail from that facility to the public for use only as a motor vehicle fuel, does not make the corporation or person a public utility within the meaning of this section solely because of that ownership, operation, or sale.

(g) Ownership or operation of a facility that is an exempt wholesale generator, as defined in the Public Utility Holding Company Act of 2005 (42 U.S.C. Sec. 16451 (6)), does not make a corporation or person a public utility within the meaning of this section, solely due to the ownership or operation of that facility.

(h) The ownership, control, operation, or management of an electric plant used for direct transactions or participation directly or indirectly in direct transactions, as permitted by subdivision (b) of Section 365, sales into a market established and operated by the Independent System Operator or any other wholesale electricity market, or the use or sale as permitted under subdivisions (b) to (d), inclusive, of Section 218, shall not make a corporation or person a public utility within the meaning of this section solely because of that ownership, participation, or sale.

SEC. 2. Section 330 of the Public Utilities Code is amended to read:

330. In order to provide guidance in carrying out this chapter, the Legislature finds and declares all of the following:

(a) It is the intent of the Legislature that a cumulative rate reduction of at least 20 percent be achieved not later than April 1, 2002, for residential and small commercial customers, from the rates in effect on June 10, 1996. In determining that the April 1, 2002, rate reduction has been met, the commission shall exclude the costs of the competitively procured electricity and the costs associated with the rate reduction bonds, as defined in Section 840.

(b) The people, businesses, and institutions of California spend nearly twenty-three billion dollars (\$23,000,000,000) annually on electricity, so that reductions in the price of electricity would significantly benefit the economy of the state and its residents.

(c) The Public Utilities Commission has opened rulemaking and investigation proceedings with regard to restructuring California's electric power industry and reforming utility regulation.

(d) The commission has found, after an extensive public review process, that the interests of ratepayers and the state as a whole will be best served by moving from the regulatory framework existing on January 1, 1997, in which retail electricity service is provided principally by electrical corporations subject to an obligation to provide ultimate consumers in exclusive service territories with reliable electric service at regulated rates, to a framework under which competition would be allowed in the supply of electric power and customers would be allowed to have the right to choose their supplier of electric power.

(e) Competition in the electric generation market will encourage innovation, efficiency, and better service from all market participants, and will permit the reduction of costly regulatory oversight.

(f) The delivery of electricity over transmission and distribution systems is currently regulated, and will continue to be regulated to ensure system safety, reliability, environmental protection, and fair access for all market participants.

(g) Reliable electric service is of utmost importance to the safety, health, and welfare of the state's citizenry and economy. It is the intent of the Legislature that electric industry restructuring should enhance the reliability of the interconnected regional transmission systems, and provide strong coordination and enforceable protocols for all users of the power grid.

(h) It is important that sufficient supplies of electric generation will be available to maintain the reliable service to the citizens and businesses of the state.

(i) Reliable electric service depends on conscientious inspection and maintenance of transmission and distribution systems. To continue and enhance the reliability of the delivery of electricity, the Independent System Operator and the commission, respectively, should set inspection, maintenance, repair, and replacement standards.

(j) It is the intent of the Legislature that California enter into a compact with western region states. That compact should require the publicly and investor-owned utilities located in those states, that sell energy to California retail customers, to adhere to enforceable standards and protocols to protect the reliability of the interconnected regional transmission and distribution systems.

(k) In order to achieve meaningful wholesale and retail competition in the electric generation market, it is essential to do all of the following:

(1) Separate monopoly utility transmission functions from competitive generation functions, through development of independent, third-party control of transmission access and pricing.

(2) Permit all customers to choose from among competing suppliers of electric power.

(3) Provide customers and suppliers with open, nondiscriminatory, and comparable access to transmission and distribution services.

(l) The commission has properly concluded that:

(1) This competition will best be introduced by the creation of an Independent System Operator.

(2) Generation of electricity should be open to competition.

(3) There is a need to ensure that no participant in these new market institutions has the ability to exercise significant market power so that operation of the new market institutions would be distorted.

(4) These new market institutions should commence simultaneously with the phase in of customer choice, and the public will be best served if these institutions and the nonbypassable transition cost recovery mechanism referred to in subdivisions (s) to (w), inclusive, are in place simultaneously and no later than January 1, 1998.

(m) It is the intention of the Legislature that California's publicly owned electric utilities and investor-owned electric utilities should commit control of their transmission facilities to the Independent System Operator. These utilities should jointly advocate to the Federal Energy Regulatory Commission a pricing methodology for the Independent System Operator that results in an equitable return on capital investment in transmission facilities for all Independent System Operator participants.

(n) Opportunities to acquire electric power in the competitive market must be available to California consumers as soon as practicable, but no later than January 1, 1998, so that all customers can share in the benefits of competition.

(o) Under the existing regulatory framework, California's electrical corporations were granted franchise rights to provide

electricity to consumers in their service territories.

(p) Consistent with federal and state policies, California electrical corporations invested in power plants and entered into contractual obligations in order to provide reliable electrical service on a nondiscriminatory basis to all consumers within their service territories who requested service.

(q) The cost of these investments and contractual obligations are currently being recovered in electricity rates charged by electrical corporations to their consumers.

(r) Transmission and distribution of electric power remain essential services imbued with the public interest that are provided over facilities owned and maintained by the state's electrical corporations.

(s) It is proper to allow electrical corporations an opportunity to continue to recover, over a reasonable transition period, those costs and categories of costs for generation-related assets and obligations, including costs associated with any subsequent renegotiation or buyout of existing generation-related contracts, that the commission, prior to December 20, 1995, had authorized for collection in rates and that may not be recoverable in market prices in a competitive generation market, and appropriate additions incurred after December 20, 1995, for capital additions to generating facilities existing as of December 20, 1995, that the commission determines are reasonable and should be recovered, provided that the costs are necessary to maintain those facilities through December 31, 2001. In determining the costs to be recovered, it is appropriate to net the negative value of above market assets against the positive value of below market assets.

(t) The transition to a competitive generation market should be orderly, protect electric system reliability, provide the investors in these electrical corporations with a fair opportunity to fully recover the costs associated with commission approved generation-related assets and obligations, and be completed as expeditiously as possible.

(u) The transition to expanded customer choice, competitive markets, and performance based ratemaking as described in Decision 95-12-063, as modified by Decision 96-01-009, of the Public Utilities Commission, can produce hardships for employees who have dedicated their working lives to utility employment. It is preferable that any necessary reductions in the utility workforce directly caused by electrical restructuring, be accomplished through offers of voluntary severance, retraining, early retirement, outplacement, and related benefits. Whether workforce reductions are voluntary or involuntary, reasonable costs associated with these sorts of benefits should be included in the competition transition charge.

(v) Charges associated with the transition should be collected over a specific period of time on a nonbypassable basis and in a manner that does not result in an increase in rates to customers of electrical corporations. In order to insulate the policy of nonbypassability against incursions, if exemptions from the competition transition charge are granted, a firewall shall be created that segregates recovery of the cost of exemptions as follows:

(1) The cost of the competition transition charge exemptions granted to members of the combined class of residential and small commercial customers shall be recovered only from those customers.

(2) The cost of the competition transition charge exemptions

granted to members of the combined class of customers other than residential and small commercial customers shall be recovered only from those customers. The commission shall retain existing cost allocation authority provided that the firewall and rate freeze principles are not violated.

(w) It is the intent of the Legislature to require and enable electrical corporations to monetize a portion of the competition transition charge for residential and small commercial consumers so that these customers will receive rate reductions of no less than 10 percent for 1998 continuing through 2002. Electrical corporations shall, by June 1, 1997, or earlier, secure the means to finance the competition transition charge by applying concurrently for financing orders from the Public Utilities Commission and for rate reduction bonds from the California Infrastructure and Economic Development Bank.

(x) California's public utility electrical corporations provide substantial benefits to all Californians, including employment and support of the state's economy. Restructuring the electric services industry pursuant to the act that added this chapter will continue these benefits, and will also offer meaningful and immediate rate reductions for residential and small commercial customers, and facilitate competition in the supply of electric power.

SEC. 3. Section 331 of the Public Utilities Code is amended to read:

331. The definitions set forth in this section shall govern the construction of this chapter.

(a) "Aggregator" means any marketer, broker, public agency, city, county, or special district, that combines the loads of multiple end-use customers in facilitating the sale and purchase of electric energy, transmission, and other services on behalf of these customers.

(b) "Broker" means an entity that arranges the sale and purchase of electric energy, transmission, and other services between buyers and sellers, but does not take title to any of the power sold.

(c) "Direct transaction" means a contract between any one or more electric generators, marketers, or brokers of electric power and one or more retail customers providing for the purchase and sale of electric power or any ancillary services.

(d) "Fire wall" means the line of demarcation separating residential and small commercial customers from all other customers as described in subdivision (e) of Section 367.

(e) "Marketer" means any entity that buys electric energy, transmission, and other services from traditional utilities and other suppliers, and then resells those services at wholesale or to an end-use customer.

(f) "Microgeneration facility" means a cogeneration facility of less than one megawatt.

(g) "Restructuring trust" means the tax-exempt public benefit trust established by Decision 96-08-038 of the Public Utilities Commission to provide for the design and development of the hardware and software systems for the Independent System Operator and that may undertake other activities, as needed, as ordered by the commission.

(h) "Small commercial customer" means a customer that has a maximum peak demand of less than 20 kilowatts.

SEC. 4. Section 335 of the Public Utilities Code is amended to read:

335. In order to ensure that the interests of the people of California are served, a five-member Electricity Oversight Board is hereby created as provided in Section 336. For purposes of this chapter, any reference to the Oversight Board shall mean the Electricity Oversight Board. Its functions shall be all of the following:

(a) To oversee the Independent System Operator.

(b) To serve as an appeal board for majority decisions of the Independent System Operator governing board, as they relate to matters subject to exclusive state jurisdiction, as specified in Section 339.

(c) To investigate any matter related to the wholesale market for electricity to ensure that the interests of California's citizens and consumers are served, protected, and represented in relation to the availability of electric transmission and generation and related costs, during periods of peak demand.

SEC. 5. Section 338 of the Public Utilities Code is repealed.

SEC. 6. Section 339 of the Public Utilities Code is amended to read:

339. (a) The Oversight Board is the appeal board for majority decisions of the Independent System Operator governing board relating to matters that are identified in subdivision (b) as they pertain to the Independent System Operator.

(b) The following matters are subject to California's exclusive jurisdiction:

(1) Selections by California of governing board members, as described in Sections 335 and 337.

(2) Matters pertaining to retail electric service or retail sales of electric energy.

(3) Ensuring that the purposes and functions of the Independent System Operator are consistent with the purposes and functions of California nonprofit public benefit corporations, including duties of care and conflict of interest standards for directors of the corporation.

(4) State functions assigned to the Independent System Operator under state law.

(5) Open meeting standards and meeting notice requirements.

(6) Appointment of advisory representatives representing state interests.

(7) Public access to corporate records.

(8) The amendment of bylaws relevant to these matters.

(c) Only members of the Independent System Operator governing board may appeal a majority decision of the Independent System Operator related to any of the matters specified in subdivision (b) to the Oversight Board.

SEC. 7. Section 340 of the Public Utilities Code is amended to read:

340. The Oversight Board shall take the steps that are necessary to ensure the earliest possible incorporation of the Independent System Operator as an incorporated public benefit, nonprofit corporations under the Corporations Code.

SEC. 8. Section 341.2 of the Public Utilities Code is amended to read:

341.2. The Bagley-Keene Open Meeting Act (Article 9 (commencing with Section 11120) of Chapter 1 of Part 1 of Division 3 of Title 2 of the Government Code) applies to meetings of the Oversight Board. In addition to the allowances of that act, the Oversight Board may

hold a closed session to consider a matter based on information that has received a grant of confidential status pursuant to regulations of the Oversight Board, provided that any action taken on such a matter shall be taken by vote in an open session.

SEC. 9. Section 341.5 of the Public Utilities Code is amended to read:

341.5. (a) The Independent System Operator bylaws shall contain provisions that identify those matters specified in subdivision (b) of Section 339 as matters within state jurisdiction. The bylaws shall also contain provisions which state that California's bylaws approval function with respect to the matters specified in subdivision (b) of Section 339 shall not preclude the Federal Energy Regulatory Commission from taking any action necessary to address undue discrimination or other violations of the Federal Power Act (16 U.S.C.A. Sec. 791a et seq.) or to exercise any other commission responsibility under the Federal Power Act. In taking any such action, the Federal Energy Regulatory Commission shall give due respect to California's jurisdictional interests in the functions of the Independent System Operator and to attempt to accommodate state interests to the extent those interests are not inconsistent with the Federal Energy Regulatory Commission's statutory responsibilities. The bylaws shall state that any future agreement regarding the apportionment of the Independent System Operator board appointment function among participating states associated with the expansion of the Independent System Operator into a multistate entity shall be filed with the Federal Energy Regulatory Commission pursuant to Section 205 of the Federal Power Act (16 U.S.C.A. Sec. 824d).

(b) Any necessary bylaw changes to implement the provisions of Section 335, 337, 339, or subdivision (a) of this section, or changes required pursuant to an agreement as contemplated by subdivision (a) of this section with a participating state for a regional organization, shall be effective upon approval of the respective governing boards and the Oversight Board and acceptance for filing by the Federal Energy Regulatory Commission.

SEC. 10. Article 4 (commencing with Section 355) of Chapter 2.3 of Part 1 of Division 1 of the Public Utilities Code is repealed.

SEC. 11. Section 359 of the Public Utilities Code is amended to read:

359. (a) It is the intent of the Legislature to provide for the evolution of the Independent System Operator into a regional organization to promote the development of regional electricity transmission markets in the western states and to improve the access of consumers served by the Independent System Operator to those markets.

(b) The preferred means by which the voluntary evolution described in subdivision (a) should occur is through the adoption of a regional compact or other comparable agreement among cooperating party states, the retail customers of which states would reside within the geographic territories served by the Independent System Operator.

(c) The agreement described in subdivision (b) should provide for all of the following:

(1) An equitable process for the appointment or confirmation by party states of members of the governing boards of the Independent System Operator.

(2) A respecification of the size, structure, representation, eligible membership, nominating procedures, and member terms of

service of the governing boards of the Independent System Operator.

(3) Mechanisms by which each party state, jointly or separately, can oversee effectively the actions of the Independent System Operator as those actions relate to the assurance of electricity system reliability within the party state and to matters that affect electricity sales to the retail customers of the party state or otherwise affect the general welfare of the electricity consumers and the general public of the party state.

(4) The adherence by publicly owned and investor-owned utilities located in party states to enforceable standards and protocols to protect the reliability of the interconnected regional transmission and distribution systems.

SEC. 12. Section 361 of the Public Utilities Code is amended to read:

361. The commission shall ensure that any funds secured by the restructuring trusts established for the purposes of developing the Independent System Operator shall be placed at the disposal of the Independent System Operator.

SEC. 13. Section 365 of the Public Utilities Code is amended to read:

365. The actions of the commission pursuant to this chapter shall be consistent with the findings and declarations contained in Section 330. In addition, the commission shall do all of the following:

(a) Facilitate the efforts of the state's electrical corporations to develop and obtain authorization from the Federal Energy Regulatory Commission for the creation and operation of an Independent System Operator, for the determination of which transmission and distribution facilities are subject to the exclusive jurisdiction of the commission, and for approval, to the extent necessary, of the cost recovery mechanism established as provided in Sections 367 to 376, inclusive. The commission shall also participate fully in all proceedings before the Federal Energy Regulatory Commission in connection with the Independent System Operator and shall encourage the Federal Energy Regulatory Commission to adopt protocols and procedures that strengthen the reliability of the interconnected transmission grid, encourage all publicly owned utilities in California to become full participants, and maximize enforceability of such protocols and procedures by all market participants.

(b) (1) Authorize direct transactions between electricity suppliers and end use customers, subject to implementation of the nonbypassable charge referred to in Sections 367 to 376, inclusive. Direct transactions shall commence simultaneously with the start of an Independent System Operator referred to in subdivision (a). The simultaneous commencement shall occur as soon as practicable, but no later than January 1, 1998. The commission shall develop a phase-in schedule at the conclusion of which all customers shall have the right to engage in direct transactions. Any phase-in of customer eligibility for direct transactions ordered by the commission shall be equitable to all customer classes and accomplished as soon as practicable, consistent with operational and other technological considerations, and shall be completed for all customers by January 1, 2002.

(2) Customers shall be eligible for direct access irrespective of any direct access phase-in implemented pursuant to this section if at least one-half of that customer's electrical load is supplied by

energy from a renewable resource provider certified pursuant to Section 383, provided however that nothing in this section shall provide for direct access for electric consumers served by municipal utilities unless so authorized by the governing board of that municipal utility.

SEC. 14. Section 367 of the Public Utilities Code is amended to read:

367. The commission shall identify and determine those costs and categories of costs for generation-related assets and obligations, consisting of generation facilities, generation-related regulatory assets, nuclear settlements, and power purchase contracts, including, but not limited to, restructurings, renegotiations or terminations thereof approved by the commission, that were being collected in commission-approved rates on December 20, 1995, and that may become uneconomic as a result of a competitive generation market, in that these costs may not be recoverable in market prices in a competitive market, and appropriate costs incurred after December 20, 1995, for capital additions to generating facilities existing as of December 20, 1995, that the commission determines are reasonable and should be recovered, provided that these additions are necessary to maintain the facilities through December 31, 2001. These uneconomic costs shall include transition costs as defined in subdivision (f) of Section 840, and shall be recovered from all customers or in the case of fixed transition amounts, from the customers specified in subdivision (a) of Section 841, on a nonbypassable basis and shall:

(a) Be amortized over a reasonable time period, including collection on an accelerated basis, consistent with not increasing rates for any rate schedule, contract, or tariff option above the levels in effect on June 10, 1996; provided that, the recovery shall not extend beyond December 31, 2001, except as follows:

(1) Costs associated with employee-related transition costs as set forth in subdivision (b) of Section 375 shall continue until fully collected; provided, however, that the cost collection shall not extend beyond December 31, 2006.

(2) Power purchase contract obligations shall continue for the duration of the contract. Costs associated with any buy-out, buy-down, or renegotiation of the contracts shall continue to be collected for the duration of any agreement governing the buy-out, buy-down, or renegotiated contract; provided, however, no power purchase contract shall be extended as a result of the buy-out, buy-down, or renegotiation.

(3) Costs associated with contracts approved by the commission to settle issues associated with the Biennial Resource Plan Update may be collected through March 31, 2002; provided that only 80 percent of the balance of the costs remaining after December 31, 2001, shall be eligible for recovery.

(4) Nuclear incremental cost incentive plans for the San Onofre nuclear generating station shall continue for the full term as authorized by the commission in Decision 96-01-011 and Decision 96-04-059; provided that the recovery shall not extend beyond December 31, 2003.

(5) Costs associated with the exemptions provided in subdivision (a) of Section 374 may be collected through March 31, 2002, provided that only fifty million dollars (\$50,000,000) of the balance of the costs remaining after December 31, 2001, shall be eligible for recovery.

(6) Fixed transition amounts, as defined in subdivision (d) of Section 840, may be recovered from the customers specified in subdivision (a) of Section 841 until all rate reduction bonds associated with the fixed transition amounts have been paid in full by the financing entity.

(b) Be based on a calculation mechanism that nets the negative value of all above market utility-owned generation-related assets against the positive value of all below market utility-owned generation related assets. For those assets subject to valuation, the valuations used for the calculation of the uneconomic portion of the net book value shall be determined not later than December 31, 2001, and shall be based on appraisal, sale, or other divestiture. The commission's determination of the costs eligible for recovery and of the valuation of those assets at the time the assets are exposed to market risk or retired, in a proceeding under Section 455.5, 851, or otherwise, shall be final, and notwithstanding Section 1708 or any other provision of law, may not be rescinded, altered or amended.

(c) Be limited in the case of utility-owned fossil generation to the uneconomic portion of the net book value of the fossil capital investment existing as of January 1, 1998, and appropriate costs incurred after December 20, 1995, for capital additions to generating facilities existing as of December 20, 1995, that the commission determines are reasonable and should be recovered, provided that the additions are necessary to maintain the facilities through December 31, 2001. All "going forward costs" of fossil plant operation, including operation and maintenance, administrative and general, fuel and fuel transportation costs, shall be recovered solely from contracts with the Independent System Operator, provided that for the purposes of this chapter, the following costs may be recoverable pursuant to this section:

(1) Commission-approved operating costs for particular utility-owned fossil powerplants or units, at particular times when reactive power/voltage support is not yet procurable at market-based rates in locations where it is deemed needed for the reactive power/voltage support by the Independent System Operator, provided that the units are otherwise authorized to recover market-based rates and provided further that for an electrical corporation that is also a gas corporation and that serves at least four million customers as of December 20, 1995, the commission shall allow the electrical corporation to retain any earnings from operations of the reactive power/voltage support plants or units and shall not require the utility to apply any portions to offset recovery of transition costs. Cost recovery under the cost recovery mechanism shall end on December 31, 2001.

(2) An electrical corporation that, as of December 20, 1995, served at least four million customers, and that was also a gas corporation that served less than four thousand customers, may recover, pursuant to this section, 100 percent of the uneconomic portion of the fixed costs paid under fuel and fuel transportation contracts that were executed prior to December 20, 1995, and were subsequently determined to be reasonable by the commission, or 100 percent of the buy-down or buy-out costs associated with the contracts to the extent the costs are determined to be reasonable by the commission.

(d) Be adjusted throughout the period through March 31, 2002, to track accrual and recovery of costs provided for in this subdivision. Recovery of costs prior to December 31, 2001, shall include a return

as provided for in Decision 95-12-063, as modified by Decision 96-01-009, together with associated taxes.

(e) (1) Be allocated among the various classes of customers, rate schedules, and tariff options to ensure that costs are recovered from these classes, rate schedules, contract rates, and tariff options, including self-generation deferral, interruptible, and standby rate options in substantially the same proportion as similar costs are recovered as of June 10, 1996, through the regulated retail rates of the relevant electric utility, provided that there shall be a firewall segregating the recovery of the costs of competition transition charge exemptions such that the costs of competition transition charge exemptions granted to members of the combined class of residential and small commercial customers shall be recovered only from these customers, and the costs of competition transition charge exemptions granted to members of the combined class of customers, other than residential and small commercial customers, shall be recovered only from these customers.

(2) Individual customers shall not experience rate increases as a result of the allocation of transition costs.

(3) The commission shall retain existing cost allocation authority, provided the firewall and rate freeze principles are not violated.

SEC. 15. Section 367.7 of the Public Utilities Code is repealed.

SEC. 16. Section 373 of the Public Utilities Code is amended to read:

373. (a) Electrical corporations may apply to the commission for an order determining that the costs identified in Sections 367, 368, 375, and 376 not be collected from a particular class of customer or category of electricity consumption.

(b) Subject to the fire wall specified in subdivision (e) of Section 367, the provisions of this section and Sections 372 and 374 shall apply in the event the commission authorizes a nonbypassable charge prior to the implementation of an Independent System Operator referred to in subdivision (a) of Section 365.

SEC. 17. Section 376 of the Public Utilities Code is amended to read:

376. To the extent that the costs of programs to accommodate the implementation of direct access and the Independent System Operator, that have been funded by an electrical corporation and have been found by the commission or the Federal Energy Regulatory Commission to be recoverable from the utility's customers, reduce an electrical corporation's opportunity to recover its utility generation-related plant and regulatory assets by the end of the year 2001, the electrical corporation may recover unrecovered utility generation-related plant and regulatory assets after December 31, 2001, in an amount equal to the utility's cost of commission-approved or Federal Energy Regulatory Commission approved restructuring-related implementation programs. An electrical corporation's ability to collect the amounts from retail customers after the year 2001 shall be reduced to the extent the Independent System Operator reimburses the electrical corporation for the costs of any of these programs.

~~SEC. 18. Section 390 of the Public Utilities Code is repealed.~~

~~SEC. 19.~~ SEC. 18. Nothing in this act precludes a reorganized Power Exchange from winding up its operations pursuant to a plan in bankruptcy and pursuant to orders of

the Federal Energy Regulatory Commission.