# ATTACHMENT

# Local Resource Adequacy Requirements

# Phase 1 Staff Report

***Prepared in Support of R.05-12-013***
***by the Staff of the***
***California Public Utilities Commission***
***and the California Energy Commission***

## April 10, 2006

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## Introduction

The purpose of this Staff Report is to provide an outline for comments in Phase 1 of R.05-12-013, the California Public Utilities Commission's (CPUC's or Commission's) Local Resource Adequacy Requirements (Local RAR) proceeding. The Staff Report attempts to describe how the Commission's local resource adequacy program will work. Based on filings and workshops, the Staff Report identifies consensus positions when possible, and otherwise offers a staff proposal, which has been informed by the workshop and comment process to date. A few important notes on this Staff Report:

- Parties should use the numbering (outline) system from this report when then file comments and reply comments in this proceeding. Although occasionally explicitly stated, the idea that "*Parties should comment on the issues mentioned herein.*" is implicit throughout the entire document.
- Additional or omitted issues may be added to the end of each related section, so long as they are within the scope of Phase 1 of R.05-12-013.
- With the exception of Section I.A., parties may comment on all issues in this document on April 18, and reply comments on April 25, 2006. Parties may comment on Section I.A. on April 28, 2006 and replies on May 3, 2006.
- The Staff Report is not a final decision, and it does not speak for the Commission. The report often states that the staff "proposes" and "expects" the Commission to take certain actions—but it is not a Commission decision on any of the issues. Instead, the Staff Report is intended to elicit comments in order to inform the Commission and help the Commission make its decision. If there are errors and omissions in

various parts of the Staff Report—parties' comments will clarify and improve the record available to the Commission.

The Commission stated its intention in the December 15, 2005 Order Instituting Rulemaking (R.05-12-013) to adopt a Local RAR program, in addition to the to system Resource Adequacy Requirements (System RAR) program adopted in D.05-10-042 and D.04-10-035. The purpose of a Local RAR program is to ensure sufficient local generation capacity is contracted for and is available to the California Independent System Operator (CAISO) to meet local reliability needs. The R.05-12-013 proceeding has been divided into phases, with various issues to be addressed in each phase.[1] As noted in the Scoping Memo, one purpose of Phase 2 of R.05-12-013 is to consider capacity markets, and while parties have mentioned capacity markets consistently throughout the comments and in the workshops held[2] on February 8th and 9th, and March 7th, 15th, and 27th, the issue of capacity markets is not discussed in this Staff Report since it is not currently under consideration for adoption in Phase 1 of R.05-12-013.

The goal of a Local RAR program is to ensure there is enough generation available within local load pockets (or "local areas") so that the CAISO can respond to various changes or "contingencies" that occur on the transmission system and thereby preserve reliability. Local load pockets are defined by physical transmission constraints that limit the amount of transmission that can be transferred into or out of the load pocket, compared to the load demand within the area. If the transfer capability into the local load pocket is less than the load demand in the area, then, depending on reliability criteria, LSEs may

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[1] See Scoping Memo, March 1, 2006, available at http://www.cpuc.ca.gov/PUBLISHED/RULINGS/54059.htm.

[2] The workshops on February 8th and 9th, and March 15th were transcribed. The record of those workshops is fully available to this proceeding record.

need to procure enough capacity within the local load pocket to satisfy the load demand. This minimum amount of capacity is referred to as the local capacity requirement (LCR).

The CAISO proposes to identify local load pockets for 2007 in its 2007 LCR study. The CAISO's 2007 LCR study should also identify the amount of capacity that the CAISO believes is necessary to meet the LCR in each of its identified for local load pockets. The CAISO has agreed to provide both a "high," "low," and "intermediate" LCR for each local load pocket, based on various levels of reliability.[3] After an opportunity for parties to comment on the 2007 LCR study, the Commission will adopt a Local Resource Adequacy Requirement (Local RAR), based upon the Commission's assessment of the appropriate level of reliability, balanced against the costs of such reliability, so that California ratepayers do not pay for "reliability at any cost." The Commission is expected to establish a Local RAR for all CPUC-jurisdictional LSEs for 2007. The defined local areas are intended to remain relatively stable over time, but local area boundaries would be updated to accommodate changes to the transmission system, changes in the availability of generation, and changes in load in the local load pockets.

Throughout the entirety of this document, the staff use the term "Local Capacity Requirement (LCR)" to refer to the CAISO's requirement and/or the

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[3] See CAISO's "Report of the California Independent System Operator Summarizing the Meet and Confer Process to Develop Study Input Assumptions", February 22, 2006, p.7. "As agreed-upon by the parties at the meet and confer session and to help evaluate the sensitivity of the contingency criteria as expressed by performance levels, the CAISO will publish the LCR based on Performance Level B and Performance Level C criterion, yielding the low and high range LCR scenarios. In addition, the CAISO will incorporate all projects operational on or before June 1, 2007 all all other feasible operational solutions brought forth by the PTOs and as agreed to by the CAISO. Such solutions that can reduce the need for procurement to meet the Performance Level C criteria will be incorporated into the LCR study and the resulting LCR published for this third scenario. This will represent the medium-range scenario."

CAISO's study. The staff use the term "Local RAR" to refer to the Commission's requirement and/or program. Local RAR is distinct from "System RAR", which has commonly been referred to as just "RAR". The Commission's Resource Adequacy (RA) program will be both the system RAR and the Local RAR (as adopted).

# I. Local Resource Adequacy Requirements

The following Local RAR proposal is for 2007 Local RAR, and may need to be changed for 2008 and beyond.

## *I. A. Local Capacity Requirements (LCR)*

***Parties may comment on all issues in Section I.A. on April 28, 2006, and reply comments on May 3, 2006.***

### I. A. 1. CAISO's LCR Study Preparation and Release

The CAISO submitted its 2006 LCR to R.04-04-003 on September 23, 2005, and the Commission was unable to act on it in its October 2005 Resource Adequacy Order. The CAISO's 2006 study was submitted to R.05-12-013, with some additional materials on January 31, 2006. The CAISO issued a market notice (but has not submitted to this proceeding's record) regarding revisions to its CAISO's 2006 LCR study on March 27, 2006. The CAISO's "updated 2006 results" are available from its website.[4]

As mentioned in the Introduction above, the California Independent System Operator (CAISO) is currently preparing a study on the 2007 local capacity requirements (LCR). The 2007 LCR study will identify each locally

[4] For CAISO's March 27, 2006 Local Capacity Technical Analysis, see http://www.caiso.com/17c6/17c6a16019910.html.

constrained area in the CAISO control area by transmission constraints, using 2007 load and resource information. The staff expects that the 2007 LCR study will be released no later than April 21, 2006. The CAISO has announced it will host a meeting in Folsom, CA on April 26, 2006 to review the study.[5]

The CAISO is expected to perform yearly studies hereafter to identify local load pockets with insufficient transmission capability to meet peak load needs. The CAISO identified nine local load pockets in its preliminary 2006 LCR study, although changes in load, generation, and transmission may change the results of the 2007 LCR study.

The CAISO 2006 LCR study is anticipated to provide a list of generators that meet reliability needs in each local area. We currently understand that in some areas, almost every generation unit is needed to meet local reliability needs; in other areas approximately 70% of generation units are needed. The staff would appreciate if the CAISO could identify the MW and owners of the units identified as qualifying capacity in local areas.

### I. A. 2. Key Issues in LCR Study

The key issues for the Commission's consideration prior to the adoption of the recommendations in the 2007 LCR study are the appropriateness of: (a) the input assumptions used to develop the 2007 LCR study, including the transmission system configuration, generation, and load forecasts; (b) the 2007 LCR study methodology, including maximization of import capability, the status

[5] The CAISO issued an email to the service list of R.05-12-013 on March 16, 2006 that it would host a meeting on April 26, 2006, which included the following text: "The California ISO will be hosting a meeting on 4/26/06 from 10:00 a.m. to 4:00 p.m. in the ISO boardroom to discuss the results of its 2007 Local Capacity Requirements Technical Analysis. Please contact Charity Wilson at cwilson @ caiso.com or 916-608-7147 if you would like to attend this meeting. Replies should be received no later than Friday, April 21, 2006."

of all “must-take” units, maintaining path flows, and NERC Performance Level Criteria; and (c) the definition of the load pocket (i.e. fixed boundaries based on transmission constraints or some other method based on effectiveness).

The staff expects that the CAISO’s proposed LCR for each local load pocket will include consideration for non-generation resources, including operational responses to contingencies identified in the 2007 LCR study (such as short-term equipment upgrades, reevaluation of line ratings, and demand response), as well as load shedding options. The CAISO study should indicate how these non-generation resources have been accounted for in the LCR for each local load pocket.

The staff expects that the CAISO's 2007 LCR study will identify the amount of capacity that the CAISO believes is necessary to meet the LCR in each of its identified for local load pockets, and subareas, if necessary. The CAISO has agreed to provide both a "high," "low," and "intermediate" LCR for each local load pocket, based on various levels of reliability (N-1, N-1-1, etc.). The staff also expects the CAISO study will include some range of generator effectiveness. (See also Section I.B.4, I.B.5, and I.B.7 for more discussion of generator effectiveness.)

As noted above, the staff expects that the 2007 LCR report will show various levels of reliability. Parties may comment on the differences between the levels of reliability shown in the LCR report.

The staff expects the CAISO study will include information about the size of each unit within the local area, as well as the ownership status of the unit. The 2006 LCR study methodology assumed a large number of units are “must-take” and “muni” units in the local areas, so these units should be identified as “must take” or “muni” in the list of qualified capacity available to meet the local capacity requirement.

### I. A. 3. CPUC Adoption of a 2007 Local RAR

Based upon its own review and comments filed in response to the CAISO 2007 LCR study, the staff expects the Commission will adopt a 2007 Local RAR for each local area in its Phase 1 decision in R.05-12-013. In reaching this determination, Commission has stated it will consider the "costs and benefits of alternative approaches to reliability criteria used to define the local obligation" in its adoption of the 2007 Local RAR amounts for each local area. (D.05-12-042, p. 81)

### I. A. 4. CPUC Adoption of 2008 Local RAR and Beyond

The CPUC will not adopt a 2008 Local RAR for each local area in its Phase 1 decision in R.05-12-013. The CPUC decision will only adopt a 2007 Local RAR. This limitation is so for a few key reasons. First, the CPUC will only have a 2007 LCR study to review, and not a 2008 study. Thus, there will be no record upon which to base a 2008 Local RAR. Second, because the CPUC's Resource Adequacy program is in transition (and a new CAISO market design is scheduled to be implemented in 2007), the timing and assumptions for any 2008 LCR study will likely require revision to meet the evolving needs of the CPUC, stakeholders, and market participants.

The original Joint IOU Proposal[6] suggested that local areas be defined for a period of time greater than one year. Because the CPUC is not going to consider adopting a Local RAR for 2008 or beyond, this issue should be considered when the Commission turns to consideration of a 2008 LCR study.

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[6] The Joint IOU Proposal was filed on January 24, 2006 in R.05-12-013. The proposal was modified and expanded in comments filed in the same docket on March 13, 2006.

Numerous parties suggested that the LCR study cycle should occur concurrent with the Grid Planning Process. In fact, the Joint IOU proposal suggests that the Grid Planning Process may be adapted to produce an annual LCR report in lieu of the CAISO producing the report through some other process or division, as currently occurs.

The staff agrees that the Commission and the CAISO must create a schedule that provides adequate time for market participants to meet their RAR, while balancing the need for LSE compliance filings to be submitted to the relevant state agencies with sufficient time for review. The CPUC should establish a timeline for meeting the RAR. Below is a straw proposal for the next schedule.

***Proposed Schedule for 2008 Local RAR***

| | |
|---|---|
| December 2006 | PTOs submit base cases to CAISO |
| February 2007 | CAISO releases 2008 LCR study |
| March 2007 | Parties comment on 2008 LCR study |
| May 2007 | CPUC reviews CAISO's 2008 LCR study and Commission adopts Local RAR for 2008 |
| June 2007 | CPUC allocates 2008 Local RAR to all LSEs |
| October 1, 2007 | LSEs file Local RAR showing and "Year-Ahead" System RAR |
| November 1, 2007 | CAISO analyzes demonstrations for "residual" needs due to effectiveness factors and reports back to to LSEs |
| December 1, 2007 | LSEs demonstrate any additional procurement of "residual" through revised Local RAR, year ahead System RAR, and even December 2007 monthly System RAR, after which time the CAISO may engage in backstop procurement to resolve |

Local RAR deficiencies. (Date could be adjusted to coincide with monthly showing date.)

### I. A. 5. Zonal Capacity Requirement (ZCR)

As noted in the Phase 1 Scoping Memo in R.05-12-013, the CPUC is not considering adoption of a 2007 zonal capacity requirement for CPUC-jurisdictional LSEs in its Phase 1 decision in R.05-12-013. The issue has been slated to be discussed in Phase 2. No comments need to be provided on this topic.

## *I. B. Local Resource Adequacy Requirements (Local RAR)*

***Parties may comment on all issues in Section I.B. (and onwards) on April 18, 2006, and reply comments on April 25, 2006.***

### I. B. 1. Adoption of a Local RAR Annually

By June 2006, the staff expects the Commission will adopt a 2007 Local RAR. The Local RAR will be informed by the CAISO 2007 LCR study, and comments on that LCR study. The staff expects that the Commission will announce its intention to initiate a subsequent proceeding (an OIR or some other process) to determine future Local RAR amounts for years 2008 and beyond. Although there are some cases where the Commission makes upfront determinations on a methodology and delegates authority to staff – the staff does not expect annual Local RAR to be determined this way (at least not yet).

The staff expects the Commission will also adopt geographic definitions of the local areas for 2007, and by extension, the Commission will identify which units (qualified capacity) can be used to fulfill the Local RAR demonstration in 2007.

The staff expects that the Commission will need to announce its intention to adopt a 2008 Local RAR prior to the September 2007 Local RAR showing. Staff expects that the process of adopting 2008 Local RAR (and by extension, identifying qualified capacity for meeting the Local RAR showing) will be an annual process. While it may further many goals of simplicity and certainty to adopt a multi-year approach to Local RAR, there are also benefits to maintaining an annual process. First, transmission and generation systems are constantly evolving, and the LCR analysis should keep pace with those changes. Second, setting an LCR annually may encourage generators to seek out multi-year contracts if there is some possibility that they may not be designated as within a local area in future years.

### I. B. 2. Allocation of Local RAR to CPUC-jurisdictional LSEs

The CPUC must address how the LCR is going to be translated into a CPUC-jurisdictional LSE obligation to procure resources, and allocated among CPUC-jurisdictional LSEs as Local RAR. Defining Local RAR obligation by proportion of load served in existing IOU distribution service area, provides administrative simplicity, as there are significant obstacles to identifying which load is located in each particular local load pocket. Thus, staff expects that for 2007, every CPUC-jurisdictional LSE will have a Local RAR in each IOU distribution service territory in which it serves load. Every such LSE will be required to contract with Resource Adequacy (RA) qualifying resources within the defined local areas in order to meet its Local RAR. Each LSE's Local RAR will be a percentage of the total Local RAR adopted by the CPUC (*which is **informed** by the CAISO's LCR study*), based on that LSE's forecasted peak load in

each IOU distribution service area. The forecasted peak load will be based on the same basic load forecasting process used to determine system RAR.

Staff notes that the formula for allocation noted above may need to be refined further as the percentage of CPUC-jurisdictional LSE peak load to Participating Transmission Owner (PTO) distribution service area peak load.[7] The refinement to the PTO distribution area would allow the Commission's Local RAR program to account for the fact that non-CPUC-jurisdictional entities provide (and need to provide) some amount of the local resources. In the CAISO's 2006 LCR study, the muni resources were "taken off the top" of the LCR for each local area, therefore, only the remaining load and resources need to be allocated to CPUC-jurisdictional entities. The California Energy Commission (CEC) may need to ask for additional load forecasting information if the PTO service area (and not the IOU distribution service area) is used to calculate the Local RAR obligation.

If the staff proposal is adopted, an LSE's Local RAR can be derived as the following equation:

[LSE IOU service area RAR/Total IOU service area RAR] * Total CPUC-Local RAR in IOU service territory = LSE Local RAR.

"IOU service area RAR" means the total System RAR in that IOU distribution service area, and "LSE-1 SCE Service Area RAR" means the "System RAR that LSE-1 is responsible for in the SCE distribution service area".

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[7] The PTO service territories include non-CPUC jurisdictional entities, whereas the IOU distribution service areas do not include non-CPUC jurisdictional entities.

- ***Numerical Example 1***

| | |
|---|---|
| LSE-1 SCE Service Area RAR = | 100 MW in SCE's service area |
| SCE Service Area RAR[8] = | 20,000 MW |
| LSE-1 as a % of total SCE Service Area RAR = | 0.5% (0.005=100/20,000) |
| Total Local RAR in SCE-Service Area = | 5,000 MW |
| LSE-1 Local RAR for SCE-Service Area= | 25 MW (=0.5% * 5,000) |

If SCE's distribution service area has a total of 20,000 MW of RAR and the CPUC adopts a 5,000 MW local requirement to meet needs in the SCE service territory Local RAR, then LSE-1, which has 100 MW of load in the SCE service territory (and thus 0.5% of the load in the SCE service area), will be allocated a Local RAR obligation of 25 MW (5,000 * 0.005) for SCE's distribution service area.

- ***Exemption of Small LSEs***

Staff does not concur with AReM's suggest in its January 24th Proposal to exempt LSEs with a Local RAR obligation of less than 1 MW. Any LSE with less than 1 MW of Local RAR *per IOU distribution service area* should not be exempt from Local RAR in that distribution service area.

### I. B. 3. Load Forecasting and Assignment Notification of Local RAR

The staff expects that the CEC, working in coordination with the CPUC's Energy Division, will calculate the Local RAR for each LSE, and notification will be made to the LSE via a letter. This notification will be done concurrently with

[8] This line item is NOT the System RAR for SCE as an LSE.

the notice for the System RAR "year ahead" load forecast. The staff expectation is that this notice will be provided to LSEs on June 30, 2006.

AReM's Comments on March 13th note the concern that the release of the load forecast information may not be compatible with the Phase 1 decision, thus delaying procurement for 2007. (p.11) This concern is not an issue so long as the Commission ultimately determines LSE responsibility for Local RAR is determined on the basis of LSE load shares in IOU distribution service areas, as proposed above. This concern may be an issue if the Commission decides that the LSE responsibility for Local RAR is determined on the basis of LSE load shares in the PTO area (instead of the IOU distribution area.)

### I. B. 4. Aggregation of Local Areas

Several parties advocated aggregating or pooling the seven local areas identified in PG&E's territory in the 2006 LCR Report. This aggregation concept has two components: (1) determining each LSE's allocation of Local RAR based on its share of load in all of the local areas within one IOU distribution service area and (2) determining which qualifying capacity (generators) counts towards the Local RAR showing, if all the areas have been aggregated.

***a) Staff Proposal for Aggregation for Determining Qualifying Capacity for Local RAR***

For the purpose of determining each LSE's allocation of Local RAR, the staff recommends that the Commission's RA program aggregate all the local areas within a IOU distribution service area to derive one Local RAR for the entire IOU distribution service area, which shall then be allocated to LSE's based upon their proportion of load in that service area. The seven local areas within an PG&E's distribution service area would be aggregated as the "PG&E Local Areas". Each LSE will have one Local RAR obligation in PG&E distribution

service area, and not seven separate Local RAR obligations in PG&E distribution service area.

This aggregation of Local RAR will obviate the need for LSEs to procure resources in every local area. Each LSE may simply procure qualifying local capacity, and the LSE's Local RAR will be aggregated at the IOU service area and met via qualifying capacity resources throughout the local areas within the IOU distribution service area. This aggregation will make the program administratively convenient. The staff also acknowledge that within each local areas, there may be subareas--- and the staff proposes that these sub areas area be likewise aggregated.

For the purposes of determining which qualifying capacity counts towards the Local RAR showing, staff proposes having all capacity located in any local load pocket within an IOU distribution service area count towards meeting the Local RAR requirement in that IOU distribution service area. It has been argued that aggregation will increase the size and depth of the market for local capacity, and thereby reduce market power. Staff recognizes the possibility that LSE's will procure more than the minimum required local capacity in some local areas, and fail to procure sufficient capacity in another local area. In that case, the CAISO will need to procure backstop local capacity to ensure that the minimum required generation is available in every local area.

This staff proposal takes a different approach than the Joint IOU proposal and the PG&E modified proposal. It interacts closely with market power issues discussed below. For this proposal to work, the price paid by CAISO backstop has to be less than the LSE's are willing to pay, especially in the local areas where most of the generation is needed. Otherwise the generators will have no incentive to deal with the LSEs. Conversely, the penalties for LSE non-

compliance have to be high enough that LSEs are not better off relying on CAISO backstop.

- ***Numerical Example 2***

LSE-2 PG&E Service Area RAR = 100 MW in PG&E's service area

PG&E Service Area RAR = 20,000 MW

LSE-2 as a % of total PG&E Service Area RAR = 0.5%

Local RAR in Local Area 1 in PG&E Service Area = 1,000 MW

Local RAR in Local Area 2 in PG&E Service Area = 2,000 MW

Local RAR in Local Area 3 in PG&E Service Area = 3,000 MW

Total Local RAR in PG&E Service Area = 8,000 MW

LSE-2 Local RAR for PG&E-territory= 40 MW (0.5% * 8,000)

If the local capacity requirement of all of the local areas in PG&E's territory equals 8,000 MW, then LSE-2 has a Local RAR of 40 MW (8,000 * .005) in PG&E's service territory.

***b) Joint IOU Proposal for Aggregation for Determining Local RAR allocation Qualifying Capacity***

An alternative to the staff proposal for determining Local RAR allocation and determining which qualifying capacity counts towards the Local RAR showing is the Joint IOU Proposal. The Joint IOU proposal addressed this issue by splitting the PG&E service territory into two sections, one consisting of local areas where 95% of local generators are needed and one where less than 95% of local generators are needed. (See Joint IOU Comments, March 13, 2006 at p. 6) During the workshop process, PG&E announced its intention to serve supplemental information, including numerical examples, for how the aggregation proposal would work to guard against over or under procurement.

PG&E filed supplemental details on this aspect of the Joint IOU proposal on April 5, 2006.[9] The PG&E supplemental filing includes additional details about this aspect of its proposal, as well as numerous numerical examples.

### I. B. 5. Compliance Demonstration for Local RAR

The staff expects that the Local RAR demonstration will be an annual demonstration made via advice and made concurrently with the System RAR "year ahead" demonstration wherein LSEs demonstrate that they have procured 90% of the capacity necessary to meet 115%-117% of their peak load for the 5 summer months of the following year. For the 2007 compliance year, the Local RAR demonstration will be made on October 2, 2006. (October 2, 2006 is the first business day in 2006 after the established due date of September 30th.)
The staff expects that the Local RAR compliance demonstration will consist of a 12 month showing (January through December) for 100% of the required local resources. Resources that count towards meeting Local RAR will also count towards meeting System RAR. The June 10, 2005 workshop report based on workshops held in the Commission's prior RA rulemaking, R.04-04-003 ("Phase II Workshop Report") reflects that participants agreed that 100% of local capacity requirements must be met on a year-ahead timeframe for all 12 months of the year.[10] Significantly, having Local RAR procurement and demonstration occur on a year-ahead basis for all 12 months introduces a set of implementation and timing considerations that were not anticipated when the Commission established the 90% forward commitment requirement for the 5 summer months to be reported on September 30th. Given that the year ahead reporting

[9] See "Clarification by PG&E Regarding Distribution of Local Resource Adequacy Requirements", filed April 5, 2006, in R.05-12-013.
[10] See "Resource Adequacy Phase 2 Workshop Report", June 10, 2005 in R.04-04-003, p.95 ; available at http://www.cpuc.ca.gov/PUBLISHED/REPORT/46914.PDF.

requirement is a 5 month obligation, the September Local RAR showing will have to demonstrate that each LSE has procured 100% of the local requirement for each month of the next calendar year.

It appears that this 12 month, 100% Local RAR demonstration is appropriate for several reasons. First, there is a possibility that even if all LSEs procure their full allocation of Local RAR, they may not have procured all of the resources necessary to meet the reliability needs of a particular local load pocket. This deficiency can only be determined after the CAISO has the opportunity to analyze the effectiveness factors of all of the units actually procured to meet the Local RAR in a local load pocket. To the extent that additional units are needed to meet effectiveness factor concerns, the CAISO needs to identify the units, and LSEs should have the first opportunity to engage in this procurement, rather than have no choice but to rely on CAISO backstop procurement mechanisms. Consequently, Local RAR demonstrations should be made in sufficient time to permit the CAISO to engage in such analysis and identification of "residual" procurement needs. Second, the CAISO needs to be able to prepare for any necessary backstop procurement after the LSEs have made all of their procurement demonstrations, including those that may meet "residual" needs. The CAISO must have sufficient time to review any additional procurement demonstrations and determine if backstop or "supplemental procurement" is required. If so, the CAISO must have sufficient time to engage in a process to secure the resources it needs to maintain local area reliability. Third, a year long procurement obligation should provide assurance of revenue adequacy to those units that are most needed to ensure the reliability of the CAISO grid, and encourage the type of longer term procurement that the CPUC supports.

The staff expects that the Local RAR compliance demonstration shall be made on a Commission provided template, in accordance with a Local RAR filing guide. The existing System RAR year ahead filing guide may be updated and/or amended to provide the rules for LSEs to use in their showing. (The existing System RAR year ahead filing guide is provided in the Appendices.)

The staff expects that the Local RAR template will include the LSE's Local RAR obligation by service territory, the LSE's contracted-for units of qualified capacity within the local areas, the name of the local area where the units are located, the MW of qualified capacity, the contract ID numbers, etc. The template will have adjustments for DR programs and as well as for Reliability Must Run (RMR) units (if local RAR credit is given for RMR Condition 1 and/or RMR Condition 2 units—see additional discussion on this below.) Staff will attempt to combine the System RAR and Local RAR templates as much as possible, so as to not ask for duplicative information.

### I. B. 6. Counting Resources for Local RAR

The staff expects that the Commission will adopt a program where each LSE must show compliance with the Local RAR by showing contracted-for resource adequacy (RA) capacity from generating units the CPUC has identified as qualifying as local generation in the relevant local area. The Local RAR shall be procured, in advance, for the entire year, but different units may be used to meet the Local RAR in different months, so long as compliance is demonstrated for every month. There will be no adjustment for incremental load migration expected during the year, beyond what is already accounted for during the load forecasting period.

### *a) Counting Reliability Must Run (RMR) Condition 1 and Condition 2 Resources for Local RAR*

For 2007, the CAISO has informed workshop participants that they will designate units as RMR according to their annual RMR process; however, its process doesn't finalize RMR contracts until after the October 2, 2006 RAR filing deadline. Therefore, there will be no RMR Condition 1 or 2 units eligible to count towards either Local RAR or System RAR demonstrations in 2007[11]. For 2006, Condition 2 units were able to count for System RAR (both year ahead and monthly). In addition to the conflicting RMR vs. RA contract timing problems already mentioned, some parties do not want RMR units to continue to "count" for RAR showings since they represent a different resource obligation than the RA contracts.

The CPUC staff understands that CAISO will announce its RMR information, as per its usual schedule, in early July. The staff further understands that CAISO will notify specific resources of its intention to designate them as RMR, and the CAISO will present its recommendations to the CAISO Board in early September, etc. Then, the October 2, 2006 Local RAR (and "year ahead" System RAR) demonstrations are filed. Subsequently, the CAISO will finalize its RMR contracts. Prior to making any backstop procurement decisions for local deficiencies in 2007, the CAISO will review the Local RAR demonstrations, the RMR resources as finalized, and the effectiveness of any Local or System RA resources that are filed in the "year ahead" demonstrations.

Some parties are interested in having RMR Condition 1 units count towards Local RAR demonstrations for 2007. One important issue that has been

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[11] This statement applies to the September 30th showings; it is conceivable that RMR Condition 2 units might count in the monthly RAR filings.

raised by parties with respect to allowing RMR Condition 1 units to count in 2007 is that they would count for Local RAR, but it is unlikely that they would count for System RAR. In that case, LSEs would get charged for RMR and get issued a "local" credit, but still need to procure additional system RA resources. By allowing RMR Condition 1 units to count, the Commission may invite over procurement. Hence, the staff recommendation to not allow Condition 1 units to count for 2007 system or local RAR.

***b) Dispatchable Demand-Responses Resources***

Dispatchable demand-response resources should count towards meeting Local RAR, provided the demand response resources are located within the defined local areas. The CEC's demand response template did not request resources be defined by local areas, so therefore, if this proposal is adopted for 2007 – then the CEC may need to ask for supplemental information. Parties may wish to provide supplemental information in their comments as to the feasibility of providing such information in a timely manner, or whether it is more appropriate to consider this issue for 2008 Local RAR program implementation.

***c) Distributed Generation (DG)***

New distributed generation (DG) resources should count towards meeting Local RAR. There has been limited discussion on the counting of new distributed generation resources in Local RAR. In D.05-10-042 DG was addressed by adjusting the RAR forecast using a simple DG impact assessment methodology. Staff believes a similar treatment for Local RAR is appropriate.

***d) Effectiveness Factors and Counting Resources outside the Defined Local Area***

Significant workshop time and additional discussion among the parties occurred on this issue. By design, the resources within local areas are more effective at responding to the range of possible contingencies than resources

outside the local areas. In order to implement the program, staff believes that there needs to be a finite list of resources that count for each local area requirement. That list will contain all resources within the local areas. If the CAISO's 2007 LCR report supports including a resource outside the local area or excluding a resource inside a local area, adjustments to the list will be considered at the time the Commission adopts its Local RAR qualifying capacity list. All resources on the list will count 100%, resources not on the list will count 0% toward the Local RAR demonstration.

- As TURN notes on p.5 of their March 13, 2006 comments, it would be a "customer-friendly" policy to allow "generating units that are not located within the boundaries of a local area to contribute toward meeting that local area's LCR if the CIASO's modeling shows that such units meet some minimum 'effectiveness factor'".
- The CAISO's "Meet and Confer" Report on February 22, 2006 appeared to largely support the idea of using effectiveness factors to determine which generation units to meet Local RAR. The CAISO revised its February 22, 2006 report on March 10, 2006, to clarify what type of information on effectiveness the CAISO would provide.

Despite the CAISO's potential offer to show a range of different effectiveness factors for specific units in addressing various contingencies, the staff proposes that the Commission adopt a simplified approach for 2007.[12] The staff recognizes that the effectiveness factor of each generating unit is not a static variable. Instead, each generator has multiple effectiveness factors depending on the reliability level of the system, the transmission contingency that needs to be

[12] This comment is not intended to limit what the CAISO provides on effectiveness, just how the staff expects the Commission might use the information in 2007.

addressed, and which other units are available to the CAISO. In addition, fixing the local area boundaries, and therefore the generation units within the boundaries that can satisfy the Local RAR, will simplify (enormously) the administration of the Local RAR program. If the Local RAR program allows units to count based on effectiveness factors—there will always be a question of "which effectiveness?" under "which system configuration?"

Procuring System RA resources outside a local boundary that have *some* effectiveness for meeting some contingencies within a local area may reduce the need for CAISO backstop procurement. It is the staff's understanding that the CAISO will take into consideration all RA resources (inside and outside the local areas) when determining whether to engage in backstop procurement for 2007. However, for the purpose of implementing a CPUC Local RAR in 2007, staff expects that units not on the local RAR list cannot be used to satisfy Local RAR.

### I. B. 7. Evaluation of Compliance Demonstrations and Actions Taken Due to Non-Compliance with Local RAR

***a) CAISO Evaluation***

The staff expects that the CAISO will review the Local RAR filings of CPUC-jurisdictional LSEs, as well as non-jurisdictional showings and RMR procurement, to determine whether the amount of RA capacity under contract in each of the local areas exceeds the Commission-adopted Local RAR levels.

- If a local area's Commission adopted Local RAR is satisfied in the aggregate, even if there are some deficient LSEs, the CAISO will not engage in backstop procurement. Deficient filers will be handled through the CPUC evaluation process described below. The staff expectation is that CAISO's definition of being "satisfied in aggregate" is limited to the

procurement of the number of MWs identified in its LCR study, and does not address the technical requirement for maintaining voltage and maintaining frequency. The one exception to the preceding sentence is that the CAISO may do some additional backstop if the CAISO conducts an assessment of the effectiveness of the MWs procured, and finds that additional procurement is required to meet local needs (likely due to effectiveness factors), but such an assessment would also consider units outside the local area that may have been supplied through system RAR demonstrations.

- If a local area's Commission-adopted Local RAR is not met, after considering both System and Local RAR demonstrations, RMR procurement, and any other resources available to the CAISO, then the CAISO may engage in backstop procurement. To the extent that additional units are needed to meet effectiveness factors, the CAISO needs to identify these units, and LSEs should have the first opportunity to engage in this procurement, rather than have no choice but to rely on CAISO backstop procurement mechanisms.
  - If the deficiency is the result of a particular LSE failing to make a compliant Local RAR showing, then the CAISO's costs for local resources procured on behalf of deficient LSEs (both CPUC-jurisdictional and non-jurisdictional) would be billed directly to the Scheduling Coordinators (SCs) responsible for those LSEs.
  - If the deficiency is the result of collective error, i.e. under procurement in a particular local area even though all LSEs were compliant with their own Local RAR, then the costs for local resources procured on behalf of all LSEs would be allocated to all Scheduling Coordinators

responsible for the LSEs in the PTO service territory on a load share basis.

When reviewing the total showing to meet the local capacity requirement, the CAISO will take into consideration all RA resources available to it, even if they are outside the local areas. There may be some instances where qualifying capacity outside the local areas may reduce some of the need for local backstop procurement. The non-local generation may not be used for part of the Local RAR showing, but it may be beneficial to the system overall and reduce some backstop procurement activities.

All LSEs will be notified of the CAISO's backstop procurement actions, in coordination with the CPUC's RA program administration. Any backstop procurement will be made available to LSEs on a load-share basis, consistent with the cost-allocation, as a credit towards their monthly System RAR showings.

***b) CPUC Evaluation***

The staff expects that the Commission will review the Local RAR filings and determine whether each LSE is in compliance with the Commission's RA program requirements. The Commission will base its compliance review (probably via a delegation of authority to staff), and the actions below, on the Commission-adopted Local RAR .

- If a LSE did not meet its Local RAR obligation, but other LSEs within the same IOU distribution service area procured local generation in an amount cumulatively equal to or in excess of the CPUC-adopted Local RAR, then some action is required to prevent continued non-compliance. Two options are:

- The deficient LSE would be required to make a transfer payment to LSE(s) that are "long" on local capacity, as per the Joint IOUs transfer pricing proposal discussed in more detail below. In this case, the deficient LSE would not subject to penalties *in addition to* the transfer pricing payment, assuming there is sufficient "long" capacity to cover the full deficiency, or
- The deficient LSE would be subject to a penalty and no payments to long LSEs.[13]

- If a LSE did not meet its Local RAR obligation, and other LSEs within the IOU distribution service area did not procure local generation in an amount cumulatively equal to or in excess of the CPUC-adopted Local RAR, then the deficient LSE will be subject to (1) CAISO backstop costs directly allocated to its SC as discussed above and (2) Commission penalties if no Commission waiver has been granted. In this case, CPUC penalties shall be in addition to the cost of any required backstop procurement costs that are borne directly by an LSE's SC. The Commission penalties for failure to make the Local RAR showing are discussed below. Also, Commission waivers are discussed in more detail below.

### I. B. 8. Joint IOU's Transfer Payment Proposal

The Joint IOU Proposal in R.05-12-013 recommends adopting a transfer payment process for instances where an LSE did not meet its Local RAR obligation, but other LSEs within the IOU distribution service area procured local

[13] Public Utilities Code section 2111 provides for penalties of not less than $500 nor more than $20,000 for each offense. Under section 2108, each day of noncompliance may constitute a separate and distinct offense.

generation cumulatively in excess of the Commission-adopted Local RAR. (See Joint IOU Proposal, March 13, 2006 Comments, at p.2). The Joint IOU proposal suggests a payment of $24/kW-year transfer payment from short to long LSEs. (See Ibid, p. 4 for a detailed explanation of the prices.). In addition, the Joint Proposal suggests that the transfer payment proposal is interim (would be revisited beyond 2007) and complimentary to other penalties and backstop.

> *"The total local capacity transfer payment owed by each short LSE would then be allocated to the long LSEs in proportion to the size of the surplus demonstrated by each long LSE. There may, of course, not be sufficient extra local capacity available to transfer from the long LSEs to cover all of the local capacity deficiencies demonstrated by the short LSEs, in which case the short LSEs may face either penalties, backstop procurement by the CAISO, or both for the uncovered deficiency." (Joint IOUs, March 13, 2006, p.5)*

One argument for adopting this transfer payment proposal is that it acts as an incentive to encourage LSEs to procure their own local RA resources, thus encouraging bilateral contracting with entities that have Local RA capacity to sell. Without a transfer payment, long LSEs may be satisfied to hold onto to their long positions and not engage in bilateral contracting for the RA capacity. Under this proposal, if an LSE pays a transfer payment, it would receive the Local RAR benefit of the unit (it would not be considered "short" for Local RAR program penalty purposes), but the LSE would not be able to count the unit for System RAR purposes. Conceivably, such an LSE would prefer to procure local RA capacity resources for itself, which would count towards its System RAR demonstration, rather than purchase non-local system resources and separately make a transfer payment for the Local RA credit. An argument was made at the

March 15th workshop that the very concept of having the transfer price would incent bilateral transactions.

AReM's comments filed on March 13th suggest that the "Commission should require the utilities to sell any 'long' capacity to other LSEs at reasonable prices". (p.3) In requiring LSEs to offer for sale excess local RA capacity, the utilities would not be able to "passively rely on some administrative allocation to sell their excess" (p.3). AReM prefers that long LSEs sell all the rights to Local RA capacity, so that it can count towards a System RAR demonstration, rather than administratively transferring the "local attribute" via a price. AReM argues that if local capacity commands such a high value (price), then presumably the long LSEs would want to sell off their excess local capacity and replace it with less-expensive system RA capacity in accordance with least-cost principles. If RA capacity transactions did occur so that all LSEs can make their demonstrations, and there was still excess local capacity procured, then the excess local would just be a public benefit – and no transfer payment would be made.

There should not be any reason why an LSE wants to keep its excess (presumably more expensive) local RA capacity in lieu of selling it and buying less expensive system RA capacity. Indeed, in the specific case of the IOUs who have CPUC approved procurement plans, staff thinks that IOUs should consider very carefully the "least-cost/best-fit" procurement principle when considering retaining excess local capacity, especially if it is well-known that non-local capacity could be acquired at a reduced price. Just because an IOU has already bought local capacity (perhaps in a bundled capacity and energy transaction) does not mean that forever more it should retain that local RA capacity in excess of its own local RA needs. Staff is unclear why the IOUs would not want to sell

off their long local RA positions, as proposed above by AReM, assuming that such positions could command some premium in the RA market.

Staff is concerned that the proposed transfer payment process creates administrative burdens, and that costs that may exceed any benefits. In order to implement the transfer payment scheme, Commission staff will have to review the confidential RA filings and determine whether a transfer payment needs to be made. Commission staff will have to determine to whom and from whom the transfer payment will be made, track the payments, and take action if the transaction is not completed. The local capacity transfer payment would represent a payment for a "regulatory product" without any physical component. The transfer payment price (i.e. the $24/kw-year) will have to be "settled" or merely considered a "proxy", because as TURN noted: "There is simply no way that a convincing factual case on these issues could be assembled in time for a Commission decision in June of this year." (p. 8, March 13, 2006) While the staff understands the merits of the transfer payment proposal, it is not convinced that it would be possible for the Commission to establish the procedures for adopting such a proposal. The staff does not expect that the Commission could delegate easily to staff the complex administration of the transfer payment system. Parties should further develop procedural proposals, including any alternatives.

### I. B. 9. Enforcement and Penalties for Failure to Meet System or Local RAR Obligations

The Scoping Memo of D.05-12-013 provided that,

> *D.05-10-042 adopted the broad policy that a penalty equal to 300% of the cost for new capacity (150% for 2006 only) is an appropriate sanction for an LSE's failure to acquire the capacity needed to meet its RAR*

*obligation. The OIR provided that this proceeding will consider ways to give definition and clarity to this policy and address concerns that penalties might accrue to the General Fund of the State of California. Providing such definition and clarity, including how penalties and backstop procurement interact, may be particularly important in connection with local RAR.*

Staff recommends inclusion of a penalty regime for failure to make Local RAR showing. Penalties are required to deter non-compliance with the Local RAR program. In the absence of penalties in addition to backstop procurement costs, LSEs would be free to rely on CAISO contracting to meet their Local RAR program obligation. LSEs that have difficulty contracting with particular counterparties would be allowed to ignore their Local RAR obligation in preference to their contracting or counterparty concerns.

Staff suggests that penalties will be applied for failure to meet the Local RAR showing if no waiver has been granted. Penalties are meant to deter a real or perceived deficiency in the MW procured. A deficiency is when an LSE does not procure (and or makes a false representation that MW have been procured).

The Joint IOUs Comments on March 13, 2006 propose $80/kW year as a proxy for the annualized cost of a new entrant for the limited purpose of calculating a penalty consistent with D.05-12-042.

AReM"s comments of March 13, 2006 request that the Commission apply any penalty dollars to offset the costs of CAISO backstop procurement. They also request that the Commission provide clarification on how its compliance process and penalty assessment process will work. (March 13, 2006 Comments, p.7)

General Order 167 Appendix F sets out fines for specified violations of that general order. Of note is the fine for failure to file a formal document at the time or in the manner required; $1000 per incident plus $500 per day for the first ten calendar days the filing was late and $500 for each day thereafter. In addition, there is a fine for negligent submission of inaccurate information; $2000 per incident plus $500 per day for the first ten calendar days the inaccuracy was not corrected and $1,000 for each day thereafter. Staff understands these examples are a good basis for fines in the RA program, but proposes $1000 per day after the first 10 days for failure to file.

It is clear to staff that the time has come for the Commission to adopt more definition regarding RAR enforcement and penalties. Staff recommends that it be tasked with developing a draft General Order, for comment by the parties, to address these issues. A draft General Order would, among other things, assess penalties for failure to meet RAR obligation if no waiver has been granted. Penalties would be imposed for failure to make a demonstration, or when a demonstration reveals a deficiency, either because the LSE did not procure to meet its RAR, or makes a false representation that such MWs have been procured.

As a general matter, staff does not believe that is appropriate for penalties to be applied to defray the CAISO backstop procurement costs of deficient LSEs. First, by statute, all penalties assessed by the CPUC accrue to the State's General Fund, and it is not practical to develop a process to alter this statutory mandate. Second, the CAISO has mechanisms for billing deficient LSEs who for whom it must in engage in backstop procurement, and this mechanism is appropriate. Thus, backstop procurement will occur to compensate for deficiencies, and be charged to the appropriate party, independent of the CPUC's enforcement

process. Third, and most significantly, penalties are necessary, to deter non-compliance with the Local RAR program. In the absence of penalties, LSEs would be free to rely on CAISO backstop procurement (and simply pay the costs of that procurement) to meet their RAR obligation (local or system); further, LSEs that have difficulty contracting with particular counterparties would be free to ignore their RAR obligation, and rely on CAISO backstop procurement, instead of addressing their contracting or counterparty concerns. In either event, discretionary reliance on CAISO backstop procurement mechanisms is not consistent with the CPUC's RA program objectives. Penalties, in addition to CAISO backstop procurement costs, are necessary and will send the appropriate signal that an LSE should bi-laterally contract with resource, rather than rely on CAISO backstop procurement for RA compliance.

Staff proposes that the draft General Order address many of the specifics of the enforcement program, including the enforcement procedure, and the penalties for various types of violations.

### I. B. 10. Market Power

Throughout the workshops in both this proceeding and in the prior R.04-04-003 proceeding, it was often discussed that generators within the local areas have market power.

Market power is inherent in the problem that a large amount of generation within a constrained area is necessary to maintain reliability and serve load. Today the local requirements are met through RMR and must-offer resources, neither of which provides a sustainable platform for investment and assuring that resources remain available. Furthermore, neither of the current means for the CAISO to procure local resources seems to be providing the PTOs with the correct incentive to reduce the number of constrained areas.

While the CPUC is establishing the local resources adequacy requirements, FERC has jurisdiction over market power mitigation. The jurisdictional divide on this issue creates uncertainly and potential risks for LSEs. It should be noted, however, that it is easier for FERC to monitor and mitigate centralized markets than the bilateral transactions in the RA market. Nevertheless, adequate local market power mitigation by FERC and strong penalties for non-compliance should influence bilateral transactions. So long as there is not a centralized capacity market that can be monitored and mitigated, long-term contracting and transmission alternatives may be the best means of managing market power.

The Joint IOU proposal on January 24th suggests (p.11) that the CAISO's backstop procurement role is necessary "to address market power and to backfill on behalf of deficient LSEs". The IOUs propose that in the event backstop is used, then it is not necessary for the Commission to charge penalties to deficient LSEs.

AReM January 24, 2006 comments addressing market power proposed that LSEs be required to make Local RAR showings *only* if the following four conditions are met:

- Sellers in the local area have no market power
- Generation is available for purchase
- Creditworthy counterparties are available
- Generation is a cost-effective option compared to transmission upgrades (the CAISO would perform its backstop role until the upgrade is completed.)

As recognized in the R.04-04-003 Phase II Workshop Report, it appears that market power is inherent local load pockets where there is a limited amount of

generation within a transmission constrained area and that generation is necessary to maintain reliability and serve load in the area. Consequently, unless the Commission is prepared to defer Local RAR, AReM's proposal appears to be untenable.

Today the equivalent of Local RAR is met through RMR and the FERC must-offer obligation on all generators in the CAISO control area. Unfortunately, while highly effective at mitigating the exercise of market power, neither mechanism has proven to be a sustainable platform for new investment. Furthermore, neither mechanism appears to provide the PTOs with the correct incentive to reduce the number of constrained areas through transmission upgrades. In order to send the proper investment signal, and create the proper construction incentives for PTO, it is appropriate for the CPUC to move forward with the RA program, to adopt a meaningful Local RAR, and to find other ways to address market power concerns.

Staff proposes, consistent with the Joint IOU proposal, that the CAISO's backstop procurement role will adequately address the issue of market power during the transition period to a fully implemented RA program, and implementation of the CAISO's market redesign ("MRTU"). A CAISO backstop procurement mechanism can mitigate the exercise of market power in the RA contract market by representing a cap for how much generators may expect to receive if they don't execute an RA contract. To the extent such a backstop retains a level of uncertainty - a shorter term than a standard RA contract, and perhaps more uncertain prices terms - it can avoid undermining RA contracting.

It is also important to consider that solutions to the market power issue may be found in parts of MRTU. To the extent that appropriate market mitigation mechanisms are in place for MRTU, these mechanisms should not

only mitigate against the exercise of market power in the CAISO's markets, but should also have a mitigating effect in the RA bilateral contracting markets In summary, staff looks to an appropriately designed CAISO backstop procurement mechanism to address market power concerns on an interim, or perhaps longer, basis. Additionally, MRTU market power mitigation mechanisms may also have a mitigating impact on the bilateral contract market. Consequently, staff does not believe that it is appropriate to adopt a contingent Local RAR, as proposed by AReM. To the extent an LSE believes that a generator is exercising market power in the RA contracting market, it should address the issue through an RA waiver request.

## I. B. 11. Waivers

*a) Waivers from Local RAR Requirement*

Several parties requested in the proceeding that the CPUC offer waivers from the Local RAR showing.

It appears that the Commission has two options. One option is to not allow for any waivers from the Local RAR. Under this scheme, an LSE that is unable to bilaterally contract for local capacity to meet its Local RAR obligation would be subject to backstop procurement costs (alone or collectively, depending on the aggregate outcome of all procurement), potentially the IOU transfer price payment, and potentially CPUC penalties.

Alternatively, the Commission may allow waivers from the Local RAR showing if an LSE filed a petition for relief that demonstrates that it has made "every commercially reasonable effort" to contract for Local RA resources. According to the Joint IOU proposal (January 24, 2006, p. 19), "The waiver would have to demonstrate that the LSE actively sought products and either (1) received bids with prices in excess of the administratively determined local

attribute, or (2) did not receive any bids." TURN's comments on March 13, 2006 support the use of waivers, which would allow LSEs to rely on CAISO's backstop procurement, "when certain minimum measures of market power are met or if LSEs cannot procure LCR resources at prices below certain maximum cost thresholds". (TURN, p.4; See also p.7) In Constellation's comments on the February 8 and 9, 2006 workshop, it states "Constellation believes that it is important to provide a fair hearing to any LSE that seeks a RAR compliance waiver, but that the Commission be clear that its granting of waivers will not be done lightly." (p.12)

***b) Waivers from System RAR Requirement***

The Joint IOU Comments (March 13, 2006, p.10) request a waiver from meeting System RAR obligations by petition if an LSE believes undue market power is being exerted by sellers of capacity. The IOU proposal suggests that an LSE petition include a demonstration that it "could not obtain qualified capacity on commercially reasonable terms".

***c) Need to Establish Waiver Process***

There appears to be some consensus among parties that waiver from RAR requirements, whether local or system, may be appropriate in some instances. Staff is concerned with whether it is realistic for the Commission to adopt a waiver process, in sufficient detail, that would allow the staff to effectively administer and implement the RA program. Consequently, parties should comment further on the specifics of a waiver process and criteria for considering such waivers. Most significantly, parties should comment on how the Commission can adopt an upfront standard and process that delegates to staff how to identify the exercise of market power by a generator such that a waiver is warranted.

The staff understands that a waiver process could be upfront (i.e. before the demonstrations are filed) or after-the-fact (i.e. after or concurrent with the filing of the demonstrations). Staff is extremely concerned that any upfront waiver process would create an unrealistic expectation that staff could process waiver requests and subsequent protests in a reasonable time. One option may be for the Commission to adopt penalties for non-compliance with Local RAR. Simultaneously, the Commission could adopt a standard by which it would waive the penalties after-the-fact, if a demonstration is made that a waiver should be granted. An LSE that knowingly failed to make its Local RAR would be at risk for penalties, absent it being able to make a strong showing that a waiver should be granted. In other words, "waivers" would take the form of exemptions from penalties. This type of process would be well-suited to the Commission's long-history of due process proceedings. It would be important for the Commission to set the standard now by which it would judge those penalty exemption cases, and it would be up to LSEs to be confident in their ability to withstand the after the fact review at the Commission, based on the criteria established.

# II. Tradable Capacity Product Issues

## *II. A. Workshop on March 27, 2006*

Staff includes by reference the workshop report submitted by Southern California Edison on April 3, 2006.[14] In that workshop report, SCE reports on the March 27, 2006 workshop which discussed issues related to tradable capacity products. There are 10 issues identified in the workshop report for potential consideration in Phase 1 of R.05-12-013. Parties may comment on the issues 1 thru 10 discussed in Southern California Edison's April 3rd filing.

It should be noted that although a number of parties are actively discussing *other related* issues pertaining to the design of a standardized, tradable capacity product—the CPUC staff expects that most work on this topic is being deferred to Phase 2. The exception to that statement is the issues identified in the workshop report from the March 27, 2006 workshop.

The Joint Comments on March 13, 2006 of APS, CLECA, CMTA, Coral, DRA, EUF, J Aron & Company, TURN, SVLG, and Strategic ask that the Commission should immediately hold "workshops to identify and resolve any regulatory issues that affect development of standard commercial terms and conditions". To the extent that these issues have not been addressed by the March 27th workshop report, but must be addressed in Phase 1, parties should raise those issues in their comments. Otherwise, the Commission will plan on hosting future workshops in Phase 2 to address the other issues related to standardized terms and conditions of tradable capacity products.

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[14] See "Submission of Tradable Capacity Product Workshop Report of Southern California Edison Company (U-338-E)", filed in R.05-12-013 on April 3, 2006.

**II. A. 1. Issue 1: Forced Outage Impact on Qualifying Capacity**

**II. A. 2. Issue 2: Derates and Qualifying Capacity**

**II. A. 3. Issue 3: Penalties for Non-Performance**

**II. A. 4. Issue 4: Maintenance and Repair Obligations**

**II. A. 5. Issue 5: Bulletin Board and Centralized Title Clearing**

**II. A. 6. Issue 6: Clarity on Import Requirements**

**II. A. 7. Issue 7: Creditworthiness**

**II. A. 8. Issue 8: Intermediaries**

**II. A. 9. Issue 9: Pooling Of Assets and Substitution**

**II. A. 10. Issue 10: Regulatory Uncertainty**

# III. Implementation Issues

## *III. A. Filing Guide and Templates*

Implementing the first cycle of year-ahead RAR compliance filings for 2006 and the first round of month-ahead RAR compliance filings for 2006 may reveal RAR program gaps or deficiencies that must be resolved by the Commission before 2007 compliance filings are due. Parties are permitted to comment on all of the appendices, including the Energy Division's recently issued Resource Adequacy Filing Guide (including related "FAQs") for the 2006 year-ahead and month-ahead compliance guides. Included in the appendices are the erratas, frequently asked questions, and templates.

The staff proposes that the Commission acknowledge the current System RAR filing guide, monthly RAR filing guide, and associated templates as appropriate representations of the current program. The staff proposes that the Commission authorize the staff to continue to revise and refine the filing guides in accordance with Commission decisions and changing needs of the program.

## *III. B. Maximum Cumulative Capacity Buckets Based on 100% of Planning Reserve Margin*

SCE Comments on March 13, 2006 (see p. 10) request that the CPUC adjust the year-ahead templates so that the Maximum Cumulative Capacity (MCC) calculation be 103.5% (90% of 115%) of the peak hour load of an LSE's load forecast. In addition the MCC's should be "based upon 115% of peak hour load for both year-ahead and month-ahead for consistency". (p.10)

Staff suggests 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).

## *III. C. Accounting for Transmission Losses*

SCE Comments on March 13, 2006 (see p.11) request that for the 2007 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". The current method uses a simplifying assumption – increasing an LSE's load forecast by a flat 3%.

## *III. D. Process for Resolving Discrepancies*

AReM's Comments on March 13th request that the Commission determine a process for resolving discrepancies between the CAISO's Monthly Supply Plan submitted by generators and the LSE's monthly showing.

# IV. Other Issues

Since we have asked parties to use this Staff Report as an outline for comments, parties may comment here on any other issues within the Scope of Phase 1 (but not yet raised in this outline.) Issues can be added at the end of each section, as appropriate, or included here as Section IV.

# V. Appendices: Resource Adequacy Filing Guides and Templates

## *V. A. APPENDIX A: RA Year-Ahead Filing Guide and Cover Letter and MCC Errata*

## *V. B. APPENDIX B: Resource Adequacy Year-Ahead Filing Template and Instructions*

## *V. C. APPENDIX C: Resource Adequacy Liquidated Damages Contract Template and Instructions*

## *V. D. APPENDIX D: Resource Adequacy FAQ Sheet*

## *V. E. APPENDIX E: Resource Adequacy Advice Letter Primer*

## *V. F. APPENDIX F: Resource Adequacy Month-Ahead Filing Guide and Cover Letter*

## *V. G. APPENDIX G: Resource Adequacy Month-Ahead Filing Template and Instructions*