

**PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

**ENERGY DIVISION ★**

**RESOLUTION E-3619  
JULY 8, 1999**

**RESOLUTION**

**RESOLUTION E-3619. PACIFIC GAS AND ELECTRIC COMPANY (PG&E) REQUESTS AUTHORIZATION FOR AN EXPERIMENTAL PRICE RESPONSIVENESS PROGRAM, SCHEDULE E-BID, ASSOCIATED CONTRACT, AND MODIFICATIONS TO THE TRANSITION REVENUE ACCOUNT. APPROVED AS MODIFIED.**

**BY ADVICE LETTER 1865-E FILED APRIL 22, 1999**

**Summary**

In Advice Letter 1865-E, PG&E proposes a new rate, Schedule E-BID-*Experimental Price-Responsive Load Program*, and companion contract, Standard Form 79-963-*Supplemental Agreement for Experimental Price-Responsive Electric Service*. It also proposes modifications to the Transition Revenue Account (TRA) in conjunction with Schedule E-BID.

On or before May 12, 1999, the California Large Energy Consumer Association (CLECA), the Office of Ratepayer Advocates (ORA), the California Farm Bureau Federation (Farm Bureau), the Alliance for Retail Markets (ARM), and the California Energy Commission (CEC) filed protests to the Advice Letter.

The Advice Letter is approved with modifications including, but not limited to, reasonableness review and specific conditions wherein PG&E may request customers to curtail.

**Background**

During the rate freeze, most full-service customers pay the applicable fixed tariff rate, independent of the true day-ahead and real-time market price for electricity in the California Power Exchange. Consequently, PG&E claims that customers have no incentive to moderate their consumption when the true market price is high. Under these circumstances, PG&E asserts that it may pay more than \$250/MWh if the Independent System Operator (ISO) real-time market cap is removed, while receiving only \$60-\$80/MWh from customers on Schedules E-19 and E-20 during the on-peak period. According to PG&E, this resulting shortfall reduces the amount of "headroom"

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revenue that would be available to recover transition costs, absent mitigation measures such as those proposed in Advice Letter 1865-E.

In Advice Letter 1865-E, PG&E proposes a new rate, Schedule E-BID-*Experimental Price-Responsive Load Program*, and companion contract, Standard Form 79-963-*Supplemental Agreement for Experimental Price-Responsive Electric Service*. It also proposes modifications to the Transition Revenue Account in conjunction with Schedule E-BID.

Under Schedule E-BID, customers would receive market-based incentive payments for reducing their load during the proposed four-month pilot program, June 1, 1999 to September 30, 1999. PG&E would bid the price-responsive demand schedule in the day-ahead energy market operated by the California Power Exchange (PX). The total load bid into the PX with Schedule E-BID would be lower than without it. Corresponding to a lower total demand is a lower PX market-clearing price<sup>1</sup>, which in turn, increases headroom revenue available for transition cost recovery. The principal cost of the pilot program, i.e., the incentive payments, would be recognized through a debit entry to the TRA.

PG&E proposes to offer the pilot program to its ten largest customers—five firm and five non-firm. To the extent that some of the ten largest customers decline to participate, the additional spaces would be offered to the next largest firm and non-firm customers. PG&E believes this selection process would maximize the potential effectiveness of the pilot program while streamlining implementation considerations. The pilot program would never include more than ten customers or 200 MW.

PG&E proposes to absorb all development, start-up, and administrative costs associated with the pilot program, but incentive payments would be paid by all ratepayers by their inclusion in the TRA.

Schedule E-BID specifies that bundled E-19 or E-20 customers located north of Path 15 PX pricing zone with 500 kW of maximum demand, interval load metering, and an executed Standard Form 79-963 contract would be eligible for the pilot program.

When PG&E initiates a Schedule E-BID curtailment operation, at its discretion, the utility would notify customers by 2 p.m. the day preceding the curtailment of

- the hours during which the load reductions are requested,
- the baseline usage from which load reductions would be determined, and
- the price that PG&E will pay for load reductions realized relative to the baseline usage.

Customers must notify PG&E of their intent to reduce load by 6 p.m. of that same day. The customer's notification is binding. No payment will be made if customers do not provide advance notification of acceptance and/or load reductions are less than 20% of

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<sup>1</sup> All other factors remaining constant.

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the baseline quantity. In the event of non-performance, including reduction of less than 20% of the baseline quantity, customers would be charged a \$200 penalty which would be deducted from their \$600 enrollment fee.<sup>2</sup>

PG&E's payment to customers would be based on the PX day-ahead hourly market clearing price for the zone which the customer receives service less the energy charges under the customer's otherwise applicable tariff. PG&E believes this methodology is appropriate because it reflects the reduced costs incurred by PG&E resulting from customers curtailing their load.

If the customer is also enrolled in one of PG&E's regular non-firm service options, curtailment in those programs would take precedence over Schedule E-BID. According to the Standard Form 79-963 contract, non-firm options are as defined under Section 11 of Schedules E-19 and E-20. The customer will not receive payment for any load curtailment initiated by an ISO order.

### **Notice**

Notice of PG&E's Advice Letter 1865-E was made by publication in the Commission Daily Calendar and by mailing copies to interested parties. The Advice Letter was also mailed to the PX, ISO, and Electricity Oversight Board (EOB).

### **Protests**

On or before May 12, 1999, the California Large Energy Consumer Association (CLECA), the Office of Ratepayer Advocates (ORA), the California Farm Bureau Federation (Farm Bureau), the Alliance for Retail Markets (ARM), and the California Energy Commission (CEC), individually, filed protests to the Advice Letter. PG&E filed a reply to the protests on May 24, 1999.

### **Price Spikes**

To varying degrees, ORA, CEC, and Farm Bureau recognize that price-responsiveness schedules such as E-BID could potentially mitigate price spikes that may occur this summer. ORA, however, also states that this potential benefit should be weighed against possible anti-competitive impacts.

### **Appropriate Forum**

ARM and ORA argue that the advice letter process is the inappropriate forum to implement Schedule E-BID because the advice letter process does not provide parties an opportunity to investigate fully the facts and clarify the details of the program compared to the application process. ARM further contends that approval of the Advice

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<sup>2</sup> The enrollment fee is refundable, except for penalties assessed due to non-performance.

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Letter would prejudice the upcoming market structure proceeding which would address the market power issues such as those raised in its protest.<sup>3</sup>

PG&E responded that the advice letter is the appropriate vehicle due to the experimental nature, limited scope, and short duration. PG&E does not believe it is reasonable to defer a program designed for the rate freeze period to be litigated in an unscheduled proceeding dealing with post-rate freeze issues.

#### Lack of Specificity

Farm Bureau, ARM, ORA, and CEC indicate that the filing lacked specificity on a number of issues including, but not limited to: how the incentive payment is calculated, whether PG&E would give net refunds, whether PG&E would bid E-BID demand into the ancillary services market, under what conditions would PG&E call for curtailments, what are the precise hours of the program, and what are the dollar savings associated with the program.

In its reply, PG&E clarifies that the incentive payment would be equal to the PX's market-clearing price less the customer's otherwise applicable tariff energy rate. PG&E intends to submit a substitute sheet with this clarification. Thus, PG&E contends that the incentive payments would be directly offset by the reduced costs of PX power, and that by removing the tariff rate from the incentive payment ensures PG&E's other customers are not adversely impacted by revenue losses associated with the program. Other program costs such as start-up and administrative costs would be borne by PG&E. While PG&E acknowledges that benefits of the program--lower PX market clearing prices-- may be speculative, it claims without the pilot program one cannot determine the cost-effectiveness or desirability of a full-scaled program in the future.

PG&E states that it intends to call curtailment events on any day that the PX market-clearing price exceeds \$250 MWh. It will also consider offering incentive payments at lower market clearing prices.

#### Impact on Competition

ARM, ORA, and CEC assert that Schedule E-BID is potentially anti-competitive. ARM, ORA, CEC, and Farm Bureau argue that the Schedule E-BID is simply another tool for PG&E to retain customers that may be targeted by ESPs or susceptible to distribution bypass. ARM and CEC claim ESPs cannot offer a similar program under the current market structure because the utility can spread the costs of the high incentive payments over a large customer base and/or the costs are more than offset by benefits of that curtailment derived from a lower energy price to its large base of customers. They contend that the utility's large customer base is due to the current market structure which confers default provider status solely on the utility. CEC believes

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<sup>3</sup> In his March 11, 1999 Scoping Memo and Ruling of the Assigned Commissioner in the post-rate freeze proceeding, A.99-01-016 et al., Commissioner Duque announced his intention to propose a proceeding to address post-rate freeze market structure issues.

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it is premature for PG&E to act like an ESP by offering rates such as Schedule E-BID. ARM argues that the costs of the customer retention program for competitive services should not be borne by monopoly services.

PG&E states that the eligibility requirements were not influenced by distribution bypass considerations but dictated by load profile metering capabilities which Schedules E-19 and E-20 customers have. PG&E disputes the conclusion that a four-month pilot program can be an effective customer retention tool.

PG&E sees no reason why the ESPs cannot offer the same program especially since PG&E's program incentive payment is the PX price less the applicable tariff rate. ESPs could recoup the incentive payments by selling the surplus energy into the day-ahead or real-time markets.

ARM argues E-BID would provide the utility the corollary benefit of accelerating its recovery of CTC which ESPs do not have and this benefit motivates the utility to manipulate the PX price to artificially low levels. ARM asserts a low PX price has the additional result of deterring the ESPs from participating in the marketplace. ARM also claims the E-BID program will have a negative impact on the Palo Verde and California Oregon Border (COB) markets where parties have entered into forward contracts, under market assumptions that do not include E-BID, which are often tied to the PX price. Approval of E-BID without adequate advance warning to these parties would undermine their contractual arrangements.

PG&E responds that if the rate freeze ends early, all benefits accrue to ratepayers. Only if the rate freeze lasts until December 2001 would shareholders see any direct benefit from the program in the form of a reduction to the overall level of uncollected stranded costs.

PG&E contends that the impact on other markets is not inappropriate because its program is the equivalent of adding incremental supply, and it is paying customers to curtail at the same price a new supplier would get for offering power to the PX.

#### Program eligibility

CLECA and ARM state that limiting the program to ten customers chosen at the utility's discretion is inequitable. Moreover, ARM believes this discrimination creates the potential for a two-portfolio approach for electricity procurement, one for those who can curtail and another for those who cannot. CEC prefers a PX program in which all energy service providers could participate, rather than a utility-operated program limited to a subset of utility customers. With respect to PG&E's program, CEC recommends that non-firm customers not be allowed to participate in the program because they cannot offer comparable load reductions as firm customers.

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Although it may be reasonable for the PX to have price-responsiveness programs in the future, PG&E claims that the PX is currently not in a position to contract directly with end-use customers and the only presently viable option is utility-operated programs.

PG&E refutes the assertion that the program is discriminatory because all customers can get the same kind of benefits through virtual direct access, although the customer would be exposed to PX price variability at all times.

PG&E responds to the allegation of a two-portfolio approach to electricity procurement by stating that it is required to purchase all electricity from the PX during the transition period.

PG&E continues to advocate that non-firm customers be allowed to participate since it has designed the program to ensure non-firm customers do not get paid twice for reductions ordered by the ISO. PG&E disputes CLECA's recommendation to open the program to a larger set of customers because it would exceed the resources it has to dedicate to the program. The utility also refutes CLECA's claim that the utility has too much discretion in selecting participants for the program. PG&E believes the tariff language as revised by substitute sheets dated April 1999 explicitly establishes the selection criteria.

#### Technical Problems

CEC cites numerous technical problems with the E-BID program and suggests remedies to overcome the deficiencies before the program should be approved. CEC concerns that are not addressed in the preceding issues areas are: timelines associated with customer notification, impact of rebound energy, transfer of information to other entities, and tying arrangements.

CEC believes the program's timelines for notifying and receiving responses from customers would limit the utility to participating in the PX's hour ahead or day-of markets. It suggests PG&E modify its notification/ response schedules so that the utility can bid into the day-ahead market.

PG&E states there is no need to change the timelines because its program is based on a conditional day-ahead demand forecast. That is, its bid into the day-ahead market is based upon what PG&E expects to be the level of curtailment for the forecasted market-clearing price.<sup>4</sup>

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<sup>4</sup> For example, if PG&E's total demand without Schedule E-BID is 1000 MW and it expects 50 MW of curtailment, if the PX price is \$250 and 100 MW of curtailment, if the PX price is \$500, then PG&E would bid 950 MW (its total demand of 1000 MW less 50 MW) at the price of \$250 and 900MW (1000 MW-100 MW) at the price of \$500.

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CEC recommends that customers specify how they plan to curtail, e.g. , through load shifting or conservation. By taking rebound or shifted energy into account, PG&E would avoid paying imbalance charges that it would otherwise incur. PG&E rejects this recommendation because it is outside the scope of a pilot program.

CEC suggests during the operation of the program, PG&E be restricted from transferring customer information to entities within the utility. Otherwise, PG&E would have an unfair advantage over other ESPs. PG&E agrees to reasonable restrictions.

CEC recommends the Supplemental Agreement and Schedule E-BID explicitly state that service on this program is not tied to other utility service/ rates. PG&E agrees provided it is recognized that the program requires bundled customer status and the term is four months.

#### Program Assessment

ORA recommends that approval of Schedule E-BID be subject to reasonableness review in the Annual Transition Cost Proceeding (ATCP) and PG&E provides CEC the necessary data to evaluate the program. CEC provides a list of data requirements to be submitted by October 1999, if the Commission wishes the CEC to assess the effectiveness of PG&E's program. This list is in Attachment A of this Resolution. From an experimental data gathering perspective, the CEC questions the value of a second experimental program which at 200 MW is significantly smaller than that proposed by SCE in AL 1377-E. CEC also indicates that the ISO is developing similar programs for ancillary services for the summer of 1999. Since the draft of the proposed ISO program restricts eligibility to those customers who are not participating in other curtailment programs, the CEC believes it is important to coordinate the various programs. PG&E does not object to the reasonableness review or CEC's data requirements, except where customers object to the release of their specific data. However, because PG&E is paying the PX market clearing price for reductions which is the same as purchasing supply at the market clearing price, it believes the incentive payments should enjoy the same *prima facie* reasonableness that is accorded to ordinary PX power purchases.

#### Recommendations

CLECA recommends approval , if there is increased customer participation and PG&E is not allowed to select among qualified participants.

ORA recommends the Advice Letter be modified so that the program is subject to reasonableness review in the Annual Transition Cost Proceeding and PG&E is required to provide the CEC the necessary data for the CEC to conduct an independent assessment of the program.

The Farm Bureau states the Advice Letter must undergo significant revisions before it can be implemented.

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CEC recommends that (1) there should be changes to program design for the program to be acceptable, (2) even with these changes, the Commission should weigh program benefits against costs in its evaluation of the Advice Letter, and (3) the program should be considered experimental for 1999 and does not prejudice the utility's ability to conduct such programs in the post-rate freeze era.

ARM recommends the Advice Letter be rejected.

## **Discussion**

ORA and the CEC are on point; the critical issue in evaluating this Advice Letter is whether the benefits from the E-BID program, such as mitigating possible price spikes and ending the rate freeze early, outweigh the costs of the program which may include potential adverse impacts on electricity generation or procurement competition as cited by ARM and others.

### **Competition, Price Spikes, and Program Assessment**

The dilemma is that to mitigate price spikes-- which may be due to market distortions resulting from a lack of price responsiveness in a frozen rate environment -- with price responsiveness programs like E-BID, may in turn, confer market power upon the utility. The potential for price responsiveness programs to reduce price spikes is dependent, at least in part, on the level of load that will be curtailed. As the level of the curtailment increases, the total load that is bid into the PX decreases and the corresponding market clearing price also decreases, all other factors remaining constant. However, the larger the load which is subject to curtailment by the utility, the greater are the market power concerns such as those raised by the protestants.<sup>6</sup>

PG&E argues that the utility has no market power because the curtailments are voluntary and the incentive payment is equal to the PX price less the otherwise applicable rate. Although customers may choose whether or not to curtail, it is the utility who decides when to call for voluntary curtailments. Consequently, it is the utility who determines when the market-clearing price will be lowered. However E-BID's incentive payment is unlikely to cause market distortions because it is equal to the PX market-clearing price less the otherwise applicable rate. Ideally these market power issues would be thoroughly discussed and addressed in an application. Even though we have not been able to resolve the market power issues, we will approve the E-BID program with modifications (since it is only 200 MW and its incentive payment is unlikely to

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<sup>5</sup> It is possible for a very small load to have market power, especially if it is the last megawatt need to balance demand and supply on a real-time basis.

<sup>6</sup> It is possible for a very small load to have market power, especially if it is the last megawatt need to balance demand and supply on a real-time basis.



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create market power problems) in order for PG&E to have another tool that could potentially mitigate any price spikes this summer-- which is already upon us.<sup>7</sup>

In addition to being a countervailing force to market distortions due to the rate freeze, price responsiveness programs--by reducing price spikes-- also may result in a shorter transition cost recovery period. Thus, customers would see the benefits of full competition sooner. However, a lower PX price would benefit shareholders if the utility does not recover its stranded cost by the end of 2001.

This Advice Letter should also be evaluated in the context of other options for which the utility is also seeking approval. In Advice Letter 1866-E, PG&E requests authority to recover costs for purchases from the PX Block Forward Market. Since the PX Block Forward Market is another source of potential supply, we expect less demand for the PX day-ahead market and consequently a lower PX price. However, it is not clear what are all the impacts that curtailments called by the utility would have on PX Block Forward prices. In any event, the utility should not be in a position to use its E-BID program to gain an unfair advantage in the PX Block Forward markets. Additionally we should recognize that these two programs are new and untested, may have some interactions which we are currently aware of, and are being implemented simultaneously in a developing market.

In view of the preceding concerns and consistent with the premise underlying PG&E's request for the program, it is prudent to set the following limitations on the E-BID program.

Since a driving force behind the E-BID program is the potentially high price spikes of \$250 MWh or higher, the utility should be allowed to initiate a curtailment event only if the PX market-clearing price is equal to or greater than \$250 MWh *or when the ISO calls a Stage 1 Alert, whichever occurs first. By allowing the utility the flexibility to initiate curtailments when the ISO calls Stage 1 Alerts, the ISO may avoid resorting to more expensive supplies because the curtailments will have reduced the total demand.*

PG&E's E-BID program is not without risk. For example, if PG&E bids the E-BID load in the PX's Day-Ahead market in anticipation that these customers would curtail, but E-BID customers decide not to reduce their load, PG&E may have to pay imbalance energy charges that it would not otherwise incur. Therefore, the E-BID program should be subject to reasonableness review in the ATCP. In the reasonableness review, the CEC, like other intervenors, may submit testimony including its assessment of E-BID. To facilitate CEC's evaluation, PG&E will provide CEC with the necessary data as identified in Attachment A. In its reply, PG&E has already agreed to CEC's information request as contained in Attachment A and the reasonableness review.

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<sup>7</sup> Since PX Block Forward Market is another source of potential supply, it may decrease the demand for the PX day-ahead market and consequently lower the PX price.

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PG&E and CEC should work cooperatively to provide any other data that the CEC may need for its analysis. All data should be provided to the CEC by October 31, 1999.

It is important to note that this is an experimental program whose results will be evaluated not only for reasonableness but also may be used to determine the desirability of such a program in the future. For both purposes, cost-effectiveness is a key issue. It seems the cost-effectiveness of the program would partly depend on what the PX market clearing price would have been had the curtailment not been in effect. It is unclear how the utility would obtain such information. It is also not clear how PG&E would demonstrate cost-effectiveness without considering rebound energy. Although at present PG&E will not be required to track rebound energy as recommended by the CEC, should PG&E undertake the curtailment program, the burden is upon the utility to show cost-effectiveness. The reasonableness review will include, but is not limited to cost-effectiveness and pertinent market power issues.

In light of the CEC protest which indicates there may be some link between the utility's E-BID program and programs under development by the ISO, the E-BID program may be subject to modification, if necessary, to coordinate with the ISO's programs when they are finalized.

Neither the utility nor the protestants raised the issue of the impact of the curtailment program on the PX credit, the price against which ESPs compete. In order to maintain a competitive marketplace, the costs associated with the incentive payment should be included in the PX credit calculation for all customer classes in the same manner. Since PG&E's program is limited to 200 MW, the cost of the incentive payment may have a negligible impact on the observable credit. As a matter of principle, however, PG&E should include the costs of the incentive payment in the derivation of the Schedule PX's hourly forward market costs.

At present, the protestants' arguments regarding ESPs' inability to offer similar programs resulting in the utility inappropriately retaining customers are not persuasive, especially since PG&E's incentive payment is the PX market clearing price less the otherwise applicable tariff rate. Nor are arguments regarding E-BID's detrimental impact on the value of forward contracts in the COB and Palo Verde markets compelling. Since this Advice Letter was filed on April 22, 1999 and will not be resolved until July 1999, the holders of those contracts have the advance warning that ARM believes is necessary for contractual arrangements not to be undermined.

#### Eligibility and Specificity

The protestants raised certain issues regarding equitable treatment for all customers. In its response, PG&E clarified that incentive payments will be equal to the PX market clearing price less the otherwise applicable tariff rate and that payment will be the same for all customers. PG&E indicated that it will be filing a substitute sheet with this clarification. However, PG&E does not intend to change its selection criteria. Although, the criteria are explicitly stated in the tariff as modified by substitute sheets dated April 28, 1999, this does not mean that the selection process is equitable. While recognizing

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PG&E's desire to keep the program manageable within its budget yet making the selection process more fair, the program should be open to the top 100 largest customers on Schedules E-19 or E-20. Of the 100 customers, PG&E would select ten customers on a random basis to offer incentives to curtail. To extent that any one of those customers decline, PG&E should make subsequent offers to other customers who are randomly selected from its remaining 100 largest customers. PG&E shall notify the Energy Division by letter within five days of the selection, the ten randomly selected customers identified by annual load, SIC code, and rank among the 100 customers.

Contrary to CEC's recommendation, PG&E will be allowed to include non-firm customers in its program. Whether non-firm load is a reliable source can be addressed in the reasonableness review. The issue will not be prejudged through exclusion. Since this program is only authorized for the summer of 1999, ARM's fears of a dual portfolio are unwarranted at this time.

The restrictions imposed on the program and PG&E's proposed substitute sheets address most of issues regarding of the lack of specificity. The one element which PG&E has not addressed is the form of the incentive payments. PG&E should file tariffs that explicitly state the form of the payment, e.g. credit to customer's bill.

#### Forum

The E-BID program is an experimental program for the summer of 1999. Given the urgency of PG&E's request to address the potential price spikes that may occur this summer, the E-BID program was reviewed through the advice letter process. It is not the intent of the Commission to continue to review complex and controversial programs through the advice letter process, especially those that are submitted only two months before they are proposed to be implemented. The approval of the experimental E-BID program in no way prejudices the utility's ability or obligation to perform this function in the post-freeze period which is expected be addressed by the Commission in a future proceeding. The E-BID program is also non-precedential with respect to future programs during the rate freeze period.

#### Technical Problems

PG&E agreed to CEC's recommendations to (1) restrict the transfer of customer information to entities outside E-BID's operations staff and (2) not tie service on E-BID to purchases of other PG&E services, except for bundled service. CEC's recommendations are adopted.

CEC's suggestion to change the timeline so that PG&E would be able to participate in the day-ahead market is not necessary based on PG&E's conditional bid approach.<sup>8</sup>

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<sup>8</sup> The PX has ultimate responsibility for determining what is an appropriate bid into the PX market.

Attachment A

1. Hourly load data for the season for eligible rate groups in which the participating customers exist for frozen rate billing purposes.
2. Individual interval hourly metering data for all participating customers for the season.
3. Records of specific customer contacts proposing load curtailment, customer's hour by hour load curtailment agreement, and whether PG&E ultimately requested curtailment for that customer for that event.
4. The hourly PX DA forecasts PG&E prepared that caused PG&E to initiate the customer contacts for a likely curtailment event.
5. Payment history to each customer.
6. The actual bids PG&E submitted to the PX, including designation of the particular energy market.
7. PG&E's program setup and operating costs.
8. Records from PG&E indicating which specific customers were contacted for participation and how PG&E selected particular customers when the aggregate load reduction was less than the capability of the entire pool.

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## Comments

The draft Resolution of the Energy Division in this matter was mailed to parties in accordance with Public Utilities Code Section 311 (g). Comments were filed on June 15, 1999 by PG&E, CEC, and ARM. CLECA and SCE submitted late-filed comments on June 16, 1999 and June 17, 1999, respectively. Pursuant to Energy Division's discretion, we will not consider comments from CLECA and SCE who filed late. We note, however, the concerns raised by CLECA and SCE were also generally represented by the interests of the protestants.

Other than the one procedural issue raised by PG&E, the comments focused on the following substantive issues: market power and conditions for initiating curtailments, reasonableness review, selection of participants, cost recovery, program assessment, and precedential nature of the program.

Turning to the procedural issue first, PG&E states that it should be given the option rather than the obligation to proceed with the advice letter, because PG&E voluntarily proposed to conduct the pilot program to provide a form of service not required by any statutory obligation or Commission decision. They state that issuance of the Resolution in its current form would violate the Commission's own procedures and the Public Utilities Code.<sup>9</sup>

The basis of PG&E's concerns are baseless and unsupported. PG&E has made an *ex parte* request with Advice Letter 1865-E. Under PUCode Section 311(g), PG&E is not only allowed to review the draft Resolution but also file *ex parte* comments for the Commission's consideration. The Commission has the discretion to make this program mandatory or discretionary. In this instance, the Commission will exercise its discretion and allow PG&E the option of implementing the program as modified.

We shall now address the substantive issues.

### Market Power and Conditions for Initiating Curtailments

To mitigate potential market power, we placed certain restrictions on the program, including conditions on the curtailment trigger mechanism. ARM agrees that the limitations are necessary to prevent the abuse of market power, although it still expresses concerns with a monopoly utility providing competitive service such as E-BID. PG&E and the CEC seek to modify the curtailment trigger mechanism in the draft Resolution. PG&E believes that instead of concerning itself with artificially low PX prices, the Commission should focus on artificially high PX prices due to the lack of price responsiveness under frozen rates. PG&E contends that there are no market power issues because the curtailments are voluntary and the incentive payment is equal to the market clearing price; therefore the restrictions on the trigger mechanism

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<sup>9</sup> PG&E does not cite any specific Commission procedure or section of the Public Utilities Code.

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are not necessary. PG&E further states that although it does not expect any demand responsiveness at a price less than \$250 MWh, the hypothesis cannot be tested if there are restrictions on the program. CEC also finds fault with the curtailment mechanism based on its understanding of E-BID's operations.

The high price spikes like those that occurred last summer are problematic for a number of reasons. First, they raised the question of whether the electricity markets are functioning competitively. One reason that the draft Resolution allows PG&E to implement the E-BID program is because we do recognize that market distortions may result when there is no price responsiveness. However, we are also cognizant of ARM's concerns regarding the market power problems associated with the program. Consequently, we attempted to mitigate those concerns by imposing restrictions on the curtailment trigger mechanism, consistent with PG&E's original premise for the program.

In its comments, PG&E argues that the utility cannot exercise market power because the incentive payment is limited to the market clearing price and the curtailments are voluntary. We agree with PG&E that an incentive payment equal to the market clearing price less the otherwise applicable rate is unlikely to cause market distortions. With respect to PG&E's second argument, it is unclear whether or not PG&E would have market power. Market power is the ability to influence the market price.<sup>10</sup> While customers may choose whether or not to curtail, when they make this choice is entirely up to the utility. By initiating a trigger mechanism at its sole discretion, PG&E can effectively control when the market-clearing price decreases, which is clearly the purpose and benefit of the program. Ideally, these market power issues would be thoroughly discussed in an application, but given that the summer months are upon us, and the program is only 200 MW and the incentive payment is equal to PX price less the otherwise applicable rate, we exercise our judgement in favor of attempting to mitigate potential price spikes. We will modify the draft Resolution to reflect the discussion herein.

Reducing the level of price spikes may also address the second problem associated with artificially high PX prices, a lengthened period for transition cost recovery. As previously discussed in the draft Resolution, there are potential benefits to customers from ending the rate freeze earlier. However, to the extent that the utility would not recover all of its transition costs by December 31, 2001, shareholders benefit by a lower PX price by recouping more stranded costs than they would have otherwise.

In light of the market power concerns raised by the protestants and consistent with the premise underlying PG&E's initial request, we continue to require the curtailments to be activated when the PX price exceeds \$250 MWh. In the Advice Letter, PG&E was concerned with paying over \$250/MWh as the result of the ISO removing its price cap. We find it disconcerting that PG&E's request would be based on one set of concerns;

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<sup>10</sup> Industrial Market Structure and Economic Performance (Chicago, Rand Mc Nally, 1970) p.10

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then, when granted, PG&E seeks to expand its purpose, in this case to test whether customers would curtail at prices less than \$250 MWh.<sup>11</sup> However, we will no longer require the lifting of the ISO price caps as a condition for activating curtailments. Since PG&E's primary concern is with the impact of lifting the ISO price cap, i.e., high PX prices which are greater than or equal to than \$250 MWh, limiting the curtailments to when PX prices are equal to or greater than the \$250 threshold level is sufficient. Therefore, lifting of the ISO price cap is not a necessary condition. Since PG&E anticipates little demand responsiveness at prices below the \$250 level, the \$250/MWh threshold condition should not be an impediment to the E-BID program. *We will, however, allow PG&E the flexibility to initiate curtailments when the ISO calls a Stage 1 Alert or the PX price is equal or greater than \$250 MWh, whichever occurs first. By doing so, all customers benefit from the ISO avoiding more expensive supplies since the total demand will presumably be lower.*

CEC's criticism of curtailment trigger mechanism is based on a misunderstanding of PG&E's program design. CEC indicated that it would be unfair to have a curtailment trigger mechanism based on the PX market-clearing price exceeding \$250 MWh because it believes that PG&E calls for curtailments prior to knowing the market-clearing price. This is an incorrect perception. PG&E's proposed tariff clearly states that the utility would request for curtailments by 2p.m. of the day prior to the curtailment event. PG&E chose 2 p.m. because the day-ahead market-clearing price will have already been set by then since the market closes at approximately at 1p.m. If at 2p.m. PG&E finds the market-clearing price is less than \$250 MWh, it would not issue a request for curtailments.

#### Reasonableness Review and Program Assessment

PG&E objects to the breadth of the reasonableness review, the burden of proof being upon the utility, and the data requirements needed by the CEC. CEC recommends changes to the reasonableness review based on its proposed changes to the curtailment trigger mechanism. It also seeks clarifications on the data requested from PG&E.

We have not specified the scope of the reasonableness review except for cost-effectiveness and pertinent market power issues. These two issues are appropriately included in the reasonableness review because they are the very same critical issues raised in the protests. We decline PG&E's request to eliminate these two elements from the reasonableness review.

Contrary to PG&E's comments that rebound energy (e.g., energy that is not consumed due to the curtailment which is then shifted and consumed in another time period) is included in the reasonableness review, we have not ordered the issue of rebound

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<sup>11</sup> In its reply to the protests, PG&E first raised the possibility that it would consider offering payments at market-clearing price less than \$250 MWh. We did not interpret that consideration to be a driving force or a condition of the program.

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energy to be included in the reasonableness review. We have only pointed out that in a comprehensive cost-effectiveness review, it is reasonable to expect that all costs associated with the program, including costs associated with rebound energy, if any, would be examined.

In its comments, PG&E criticizes the draft Resolution for placing the burden of proof upon PG&E in the reasonableness review process. While the precise nature of and basis for that criticism is not clear, we would note that there is nothing inappropriate in placing the burden of proof upon PG&E for the incentive payments and any other costs that are ratepayer-funded.

Since the CEC's proposed changes to the reasonableness review are predicated upon its misunderstanding of E-BID program mechanics, we will not make the requested changes.

PG&E objects to the items 3,4, and 8 in Attachment A to the draft Resolution because they are not pertinent to the E-BID program. Since PG&E had agreed to comply with CEC's request in PG&E's reply to the protests, we will not remove those elements from Attachment A. CEC seeks clarification as to when it will receive the data from PG&E and the type of data. PG&E shall submit the requested data by October 31, 1999, one month after the end of the program. CEC seeks clarification as to whether the data from PG&E will be limited to Attachment A. However, CEC has not specified what are its additional data requirements. CEC and PG&E should work cooperatively to provide the additional data necessary for CEC to conduct its analysis. We will make modifications to address both issues. CEC also requests technical clarifications to Attachment A which came from its protest. We will make the suggested technical changes since they provide more specificity on the type of data that CEC requires.

#### Cost Recovery and Precedent Setting

PG&E states the draft Resolution is incorrect in assuming that PG&E would double collect incentive payments, if the payments are included in both the TRA and Schedule PX. After a more thorough review of the tariffs, we agree with PG&E that including incentive payments in the TRA will not result in double recovery. We will revise the language in the draft Resolution where appropriate to reflect this change. We will also clarify that the costs of the incentive payments should be reflected in the PX credit for all customer classes in the same manner.

ARM suggests changes to text, findings, and ordering paragraphs to clarify that the shareholders will absorb all development, start-up and administrative costs associated with the program, that these costs be included in the PX credit calculation, and the program is non-precedential with respect to future programs during the rate freeze period. Since the first and last clarifications are consistent with PG&E's program and/or our goals for the program, we will make those clarifications. We will not include costs paid by shareholders in the PX credit since those costs are not paid by ratepayers.



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### Customer Selection

PG&E agrees with the draft Resolution that the first ten customers would be selected randomly from its largest 100 customers. It proposes that to be consistent with a random approach, subsequent offers should also be made on a random basis. We agree and will modify the draft Resolution accordingly.

### Findings

1. In Advice Letter 1865-E filed on April 22, 1999, PG&E proposes a new rate, Schedule E-BID-*Experimental Price-Responsive Load Program* and companion contract, Standard Form 79-963-*Supplemental Agreement for Experimental Price-Responsive Electric Service*. It also proposes modifications to the Transition Revenue Account in conjunction with Schedule E-BID.
2. On or before May 12, 1999, the California Large Energy Consumer Association, the Office of Ratepayer Advocates, the California Farm Bureau Federation, the Alliance for Retail Markets and the California Energy Commission filed protests. The protests focused on anti-competitive, customer equity, and appropriate forum concerns.
3. PG&E filed a reply to the protests on May 24, 1999.
4. During the rate freeze, most bundled customers pay the applicable fixed rate, independent of the true day-ahead and real-time market price for electricity.
5. Due to the rate freeze, PG&E claims that customers have no incentive to moderate their consumption when the true market price is high. Under these circumstances, PG&E asserts that it may pay \$250/MWh or more if the Independent System Operator real-time market cap is removed, while receiving approximately only one-third of that amount in revenues from customers on Schedules E-19 or E-20.
6. According to PG&E, this resulting shortfall reduces the amount of "headroom" revenue that would be available to recover transition costs, absent the E-BID program proposed in this Advice Letter.
7. Under Schedule E-BID, customers would receive incentive payments based on the PX day-ahead market clearing price less the otherwise applicable tariff charges for reducing their load during the four-month pilot program, June 1, 1999 to September 30, 1999.
8. PG&E proposes to call curtailments at its discretion.
9. PG&E would bid the price-responsive demand schedule into the day-ahead energy market operated by the Power Exchange. The total load bid into the PX with Schedule E-BID be would lower than without it.

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10. All other factors remaining constant, a lower total demand results in a correspondingly lower PX market clearing price, which in turn, increases headroom revenue available to recover transition costs.
11. PG&E proposes the costs of incentive payments would be recognized through a debit entry to the TRA.
12. PG&E proposes to absorb all developmental, start-up and administrative costs associated with the program.
13. The proposed curtailment program would be limited to 200 MW and the ten largest bundled E-19 or E-20 customers located North of Path 15 with loads greater than 500 kW and load interval metering capabilities.
14. The critical issue is whether the benefits from the E-BID program, such as mitigating possible price spikes and ending the rate freeze early, outweigh the costs of the program which may include potential adverse impacts on electricity generation or procurement competition.
15. Price spikes which occurred last summer may be due to market distortions which result from a lack of price responsiveness in a frozen rate environment.
16. The dilemma is that the potential for curtailment programs like E-BID to reduce price spikes is partly dependent on the level of load that will be curtailed, but the larger the load which is subject to curtailment by the utility, the greater are the market power concerns such as those raised by the protestants
17. PG&E states that it has no market power because the curtailments are voluntary and the incentive payment is equal to the PX price less the otherwise applicable rate.
18. While customers may choose whether or not to curtail, when they make their choice is up to the utility. By initiating curtailments solely at its discretion, PG&E can effectively control when the PX market-clearing price will be lowered.
19. An incentive payment, which is equal to the PX market-clearing price less the otherwise applicable rate, is unlikely to cause market distortions.
20. While we will not resolve these market power issues which would ideally be addressed in an application, we approve the E-BID with modifications since the program is only 200 MW and its incentive payment is equal to the PX market-clearing price less the otherwise applicable rate.

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21. To the extent that a price responsiveness program reduces price spikes, ratepayers may benefit from a shorter transition cost recovery period. However, if the utility does not recover its stranded costs before the end of 2001, shareholders benefit from a lower PX price.
22. This Advice Letter should also be evaluated in the context of other options which the utility is also seeking approval including Advice Letter 1866-E which would allow PG&E to recover costs associated with purchases from PX's Block Forward Market. Since the PX Block Forward Market is another source of potential supply, we expect less demand for the PX day-ahead market and consequently lower prices. However, it is not clear what impacts curtailments called by the utility would have on the PX Block Forward market. The utility should not be in a position to use its E-BID program to gain an unfair advantage in the PX Block Forward market.
23. Both the PX Block Forward and E-BID programs are untested and are being implemented simultaneously.
24. Given the concerns regarding potential market power problems and consistent with the premise underlying PG&E's request it is prudent to impose restrictions on the E-BID program.
25. The utility should only initiate a curtailment event if the PX market-clearing price is equal to or greater than \$250 MWh *or when the ISO calls a Stage 1 Alert, whichever occurs first.*
26. Since the E-BID program is not without risk the E-BID program should be subject to reasonableness review in the ATCP or other appropriate proceeding. The CEC, like other intervenors, may submit testimony including its evaluation of E-BID in the reasonableness review. The reasonableness review should include, but is not limited to, cost-effectiveness and pertinent market power issues. In the reasonableness review, the burden of proof is upon the utility.
27. PG&E agrees to the reasonableness review and to provide CEC with the necessary data to evaluate the E-BID program. PG&E and the CEC should work cooperatively to provide the CEC the necessary data in addition to those listed in Attachment A. PG&E should provide all data to the CEC by October 1, 1999.
28. The E-BID program may be subject to modification, if necessary, to coordinate with the ISO's demand responsiveness programs.
29. PG&E should include the costs of the incentive payments in the calculation of the Schedule PX hourly forward market costs. The costs of the incentive payment should be reflected in the PX credit for all customer classes in the same manner.

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30. PG&E should modify its tariff to clarify that the incentive payment will be equal to the PX market-clearing price less the otherwise applicable rate. PG&E should also modify its tariff to explicitly state the form of the incentive payment.
31. For a more equitable selection process, E-BID should be open to the largest 100 customers on Schedules E19 or E-20 rather than the largest ten customers.
32. To keep the program manageable, PG&E should randomly select ten out of the 100 customers.
33. To the extent that any of the first ten randomly selected customers decline to participate, PG&E may make subsequent offers to customers who are randomly selected from its remaining largest 100 customers.
34. PG&E should notify the Energy Division by letter within five days of the selection, the ten randomly selected customers identified by annual load, SIC code, and rank among the 100 customers.
35. Customer information should not be transferred to entities outside E-BID's operations staff.
36. PG&E should modify its tariff to clarify that customers taking service on E-BID are not obligated to purchase other PG&E services.
37. The E-BID program as modified is approved through the advice letter process only because the program is expected to be operational this summer.
38. Approval of the experimental E-BID program in no way prejudices the utility's ability or obligation to perform this function in the post-freeze period; that will be addressed by the Commission in a future proceeding. The E-BID program is also non-precedential with respect to future programs during the rate freeze period.
39. The CEC and ORA protests are granted in part. ORA's request for a reasonableness review is granted. CEC's requests that (1) customer information remain solely with the program's operations staff and (2) service on E-BID not be tied to other services offered by PG&E are granted. ORA's and CEC's requests for PG&E to provide CEC the requested data for the California Energy Commission to assess the program are granted. In all other respects, protests are denied.

**Therefore it is ordered that:**

1. Advice Letter 1865-E is approved subject to the following modifications:

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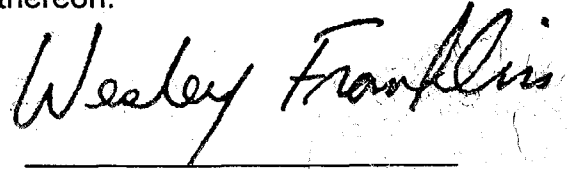
- a) The utility shall only initiate a curtailment event if the PX market-clearing price is equal to or greater than \$250 MWh *or when the ISO calls a Stage 1 Alert, whichever occurs first.*
- b) The E-BID program shall be subject to reasonableness review in the ATCP or other appropriate proceeding. The reasonableness review shall include, but is not limited to, cost-effectiveness and pertinent market power issues. The CEC, like other intervenors, may submit testimony including its evaluation of E-BID in the reasonableness review. In the reasonableness review, the burden of proof shall be upon the utility.
- c) The E-BID program may be subject to modification, if necessary, to coordinate with the ISO's demand responsiveness programs.
- d) PG&E shall include the costs of the incentive payments in the calculation of the Schedule PX hourly forward market costs. PG&E shall modify its Schedule PX tariff to reflect this calculation. The cost of the incentive payments shall be included in the PX credit for all customer classes in the same manner.
- e) PG&E shall modify its tariff to clarify that the incentive payment will be equal to the PX market-clearing price less the otherwise applicable rate and identify the form in which customers would receive payment.
- f) Schedule E-BID shall be open to the largest 100 customers on Schedules E-19 or E-20. PG&E shall randomly select ten out of the 100 customers. To the extent that any of the first ten randomly selected customers decline to participate, PG&E may make subsequent offers to customers who are randomly selected from its remaining 100 largest customers. PG&E shall make the necessary tariff modifications to reflect these eligibility and selection criteria. PG&E shall notify the Energy Division by letter within five days of the selection, the ten randomly selected customers identified by annual load, SIC code, and rank among the 100 customers.
- g) Customer information shall not be transferred to entities outside E-BID's operations staff.
- h) PG&E shall modify its tariff to clarify that bundled customers taking service on E-BID are not obligated to purchase other services from PG&E.
- i) PG&E shall provide the CEC the necessary data, including those listed in Attachment A, to evaluate the E-BID program by October 31, 1999. PG&E and CEC shall work cooperatively to provide CEC the necessary data in addition to those data listed in Attachment A.

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- j) PG&E shall absorb all start-up, developmental, and administrative costs associated with the experimental E-BID program.
2. Should PG&E choose to implement Schedule E-BID as modified, it shall file a supplemental advice letter with tariff sheets consistent with this Resolution within ten days. The tariff sheets shall be effective after Energy Division has reviewed them for compliance with this Resolution.
3. The approval of the experimental E-BID program in no way prejudices the utility's ability or obligation to perform this function in the post-freeze period; that will be addressed by the Commission in a future proceeding. The E-BID program is also non-precedential with respect to future programs during the rate freeze period.
4. The CEC and ORA protests are granted in part. ORA's request for a reasonableness review is granted. CEC's requests that (1) customer information remain solely with the program's operations staff and (2) service on E-BID not be tied to other services offered by PG&E are granted. ORA's and CEC's requests for PG&E to provide CEC the necessary data for the California Energy Commission to assess the program are granted. In all other respects, protests are denied.
5. This resolution is effective today.

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I certify that the foregoing resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the State of California held on July 8, 1999; the following Commissioners voting favorably thereon:



WESLEY M. FRANKLIN  
Executive Director

RICHARD A. BILAS  
President  
Henry M. Duque  
Josiah L. Neeper  
Joel Z. Hyatt  
Commissioners

I abstained.  
/s/ Carl W. Wood  
Commissioner