

Memorandum

To: CAISO Board of Governors

From: Anthony Ivancovich, Assistant General Counsel
Sidney Davies, Assistant General Counsel

Date: January 18, 2007

Re: Regulatory Report

This is an update of key regulatory activities and requires no Board action.

FERC Matters and Related Decisions of the Court of Appeals

Market Redesign and Technology Upgrade (MRTU) tariff docket (ER06-615)

- On December 20, 2006 the CAISO filed a further compliance filing following an expedited stakeholder process in response to three directives of the September 21, 2006 MRTU Order: (1) tariff language concerning the treatment of interruptible imports under MRTU; (2) clarifying tariff language concerning the informational requirements and dispute resolution for the Negotiated Rate Option for Default Energy Bids; and (3) a discussion concerning the appropriateness of changing the 80 % mitigation threshold for eligibility for an adder as a Frequently Mitigated Unit, for which no tariff language was submitted.
- On January 11, 2007, the CAISO filed a motion for extension of time with respect to four compliance requirements to align the compliance activities with the new MRTU implementation date of January 31, 2008 and to avoid multiple tariff filings affecting the same subject matter: (1) the posting of Business Practices Manuals to trigger date for the compliance filing of proposed additional tariff language to support details in the BPMs from January 19 to April 2, 2007 to allow for a more complete set of BPMs to be developed; (2) MRTU definitions from February 20 to August 4, 2007 to allow for refilling of all definitions (draft definitions will be posted by February 20 for stakeholder review; (3) deferral of a compliance filing to identify local area study criteria from February 20 to August 4, 2007 to allow for a comprehensive filing that would also include appropriate Resource Adequacy backstop tools; (4) amendments to section 11 to address defaults of CRR Holders from February 20 to May 2, 2007 so that a comprehensive filing of revisions to section 11 can be made.
- On December 12, the CAISO filed a response to the various parties' comments addressing Demand Response Report filed by the CAISO on November 20, 2006. The CAISO reiterated its support for pursuing effective demand response products in the CAISO's markets.
- On December 14-15, 2006, Governor Cazelet, representatives from the CAISO Executive Team and other CAISO staff attended, and in the case of Yakout Mansour, Chuck King and Mark Rothleder, participated in a FERC Technical Conference devoted to the topic of "seams" between the CAISO and neighboring control areas.

Post-conference comments are to be filed on January 16, 2006 and will be summarized in the next regulatory report.

Responsible Attorneys: Sidney Davies and Anna McKenna

Outage Reporting Tariff Amendment (ER07-127)

On December 28, 2006, the Commission accepted the tariff amendment that amends the outage reporting requirements, subject to minor modifications. The amendment revised tariff provisions that required generators to report "any reduction in capacity," to require reporting only of outages greater than 10 MW and five percent of a unit's unrestricted capacity. The amendment also reduces the amount of information that must be supplied about such outages; detailed reporting will now be required only for derates greater than 40MW and ten percent of unrestricted capacity, or for units taken off line on an unplanned basis. These changes, which were developed through a stakeholder process that was the subject of previous reports to the Board, are intended to reduce the burden of reporting and the risk of sanctions, and yet ensure that the CAISO still receives the data necessary to operate the grid reliably. The Commission also accepted the CAISO's proposed effective date – *i.e.*, 24 hours after completion of software upgrades that are necessary for implementing the revised outage reporting requirements – and granted a request to extend the temporary waiver of sanctions for violating the currently effective outage reporting requirements until March 31, 2007.

The Commission rejected a protest from Southern California Edison, which argued that the amendments did not go far enough to relax reporting requirements, and also protested the CAISO's sanction authority. In its own words, the Commission

disagree[d] with [SCE] that the new outage reporting thresholds are too low and would be burdensome. . . . We find that the CAISO's proposal will serve to reduce the number of outages to be reported thereby alleviating the reporting burden imposed under the current tariff. Furthermore, we note the CAISO's extensive use of the stakeholder process in seeking comments on appropriate outage reporting criteria, and find that the CAISO has balanced the concerns of the stakeholders in developing the outage reporting criteria.

The Commission also rejected SCE's argument that the CAISO should not have sanction authority, finding it was an improper collateral attack on issues that were resolved in an earlier docket. PG&E, which supported the amendment in its initial filing and commended the stakeholder process, subsequently filed an answer to SCE's protest that echoed some of SCE's concerns. The Commission declined to consider this second answer from PG&E.

There will be two minor revisions to the filed tariff language, both of which stem from comments filed by the Southern Cities. Specifically, the CAISO committed to revise language about reporting requirements for non-participating generators to make it consistent with the new requirements for participating generators, and the Commission directed the CAISO to clarify the provision that outages must be reported the CAISO only if they last fifteen minutes or longer.

Responsible Attorney: Dan Shonkwiler

RCST 2007 Cost Allocation Tariff Amendment (EL07-326)

On December 15, 2006, the CAISO filed a tariff amendment which, *inter alia*, modified the CAISO Tariff with regard to the designation of Eligible Capacity to provide services under the Reliability Capacity Services Tariff ("RCST") to meet local reliability needs and to respond to Significant Events. The tariff filing also included amendments to comply with the directives of FERC Order No. 676 (pertaining to Standards for Business Practices and Communications Protocols for Public Utilities) and certain waivers of such Order granted by FERC. In particular, the proposed tariff language specified methodologies for allocating the costs of (1) 2007 RCST designations to meet local resource adequacy requirement deficiencies, and (2) Significant Event RCST designations in 2007. The CAISO also proposed tariff revisions to enable it to obtain the information that it needs to determine whether any local resource adequacy deficiencies exists. Thus, the tariff provisions will allow the CAISO to obtain the information that it needs to determine whether it can make any forward local RCST designations for 2007.

Responsible Attorney: Anthony Ivancovich

WECC Regional Delegation Agreement (RR07-7)

On January 10, 2007, the CAISO filed a Motion to Intervene and Comments regarding the Regional Delegation Agreement between the North American Electric Reliability Coordination Council ("NERC") and the Western Electricity Coordinating Council ("WECC"). In that regard, NERC proposed to delegate some of its functions under the Energy Policy Act of 2005 ("EP Act") to WECC as Regional Entity. The CAISO indicated its support for WECC's efforts to become the Regional Entity for the Western Interconnection and the need for a strong WECC. However, the CAISO submitted that certain changes to WECC's proposed governance and voting structure were necessary in order to satisfy the requirements of the EP Act and FERC's regulations implementing that Act. In particular, the CAISO requested that FERC require WECC to create a separate Member Class for ISOs and RTOs and not include them in the same Member Class as transmission owners as WECC proposed to do. The CAISO argued that a separate ISO/RTO Member Class should have one (1) representative on the WECC board and should be treated as a separate Member Class for purposes of representation and voting on all WECC committees. The CAISO also requested that FERC modify or reject certain aspects of the WECC Delegation Agreement related to collection of WECC charges from Load-Serving Entities ("LSEs").

Responsible Attorney: Anthony Ivancovich

Participating Intermittent Resource Program Tariff Amendments (ER07-142)

On December 29, 2006, FERC issued an order on CAISO tariff amendments, filed November 1, 2006, that imposed an "export fee" on Energy exported from the CAISO Control Area from Participating Intermittent Resources. FERC concluded that the export fee is just and reasonable as an appropriate mechanism to ensure that customers outside the CAISO Control Area pay the full delivered cost of Energy produced from the Participating Intermittent Resource Program (PIRP). However, FERC directed the CAISO to make a single modification. The modification requires "the CAISO to amend its filing to specify in detail the costs (*i.e.*, the charge types avoided by PIRP resources) that will be used to calculate the export fee." The original filing described the export fee in narrative form, rather than specifying the particular charge types. The compliance filing is due on January 29, 2007.

Responsible Attorney: Grant Rosenblum

Unresolved Issues Proceeding (ER998-3760)

On November 29, 2006, FERC issue an order resolving the remaining issues pending in this docket that were not addressed in the June 7, 2006 and September 30, 2005. The November 29, 2006 order dismissed as moot or as otherwise resolved by the passage of time all remaining issues except to the extent the tariff did not reflect agreed upon settlement of specific issues with the Energy Producers and Users Coalition. Since the tariff already reflected the agreed upon changes, it was not necessary for the CAISO to make any compliance filing.

Responsible Attorney: Sidney Davies

Lake Elsinore Advanced Pumped Storage (“LEAPS”) Project (ER06-278)

On January 8, 2007 the CAISO filed a Motion for Extension of Time to Submit Response in the LEAPS proceeding seeking a filing date of May 1, 2007 for submission of the response to the November 17, 2006 Order reported in the December 2006 Regulatory Report. The CAISO explained that the stakeholder process necessary to address the issues raised by Nevada Hydro with respect to its proposal to turn operational control of the project over to the CAISO would take much longer than the 60 day period set forth in the Order.

Responsible Attorney: Anthony Ivancovich and Judi Sanders

PG&E—Network Integration Transmission Service Agreement with BART (ER06-902)

On January 4, 2006, the Presiding Administrative Law Judge issued his Certification of Uncontested Settlement of the Offer of Settlement and Settlement Agreement executed by Pacific Gas and Electric Company (PG&E), the San Francisco Bay Area Rapid Transit District (BART), and the California Independent System Operator Corporation (CAISO) (collectively “Parties”) describing modifications to the previously filed and accepted BART-PG&E Network Integration Transmission Service Agreement (NITS Agreement) filed on November 20, 2006. The settlement is not opposed by the Federal Energy Regulatory Commission Trial Staff (Staff). The Settlement Agreement settled all issues in the FERC proceeding regarding the PG&E filing for acceptance of modifications to Service Agreement No. 42 for the NITS Agreement between BART and PG&E. The Settlement Agreement states that PG&E proposed to revise the NITS Agreement between BART and PG&E to reflect the arrangement between BART and PG&E to accommodate BART’s new power supply arrangements with the Northern California Power Agency (NCPA). To accommodate the NCPA power supply arrangements of BART beginning July 1, 2006, the NITS Agreement provided for NP-15 as an “alternate” Point of Receipt (POR) for NCPA residual power when BART’s primary POR at the California Oregon border (COB) is not physically available. The May 2 filing also established the Western Area Power Administration (Western) Cottonwood 230 kV Substation (Cottonwood) as a “backup” POR for Western power when the Western Tracy 230 kV Substation (Tracy) is not physically available as a POR.

Responsible Attorney: Anna McKenna

Calpine Reliability Must Run Rate Proceeding (ER06-268 et al)

On December 29, 2006, FERC conditionally approved the offer of settlement between and among PG&E, the CAISO and the Calpine corporate entities owning RMR Units. The settlement resolves all pending RMR rate matters. FERC conditioned its order on a modification to the settlement that would allow FERC to change rate terms and conditions using the statutory "just and reasonable" standard of review as provided by Section 205 of the Federal Power Act rather than the "public interest" agreed to by the settling parties. The settling parties have agreed to make the modification to the settlement.

Responsible Attorney: Sidney Davies

Mandatory Reliability Standards for the Bulk-Power System (RM06-16-000)

On January 3, 2007 the CAISO filed comments in response to the FERC NOPR in RM 06-16-000 requesting comments on the mandatory reliability standards approved in whole and in part in the NOPR. The CAISO also joined in the comments filed by the ISO/RTO Council on the same date. In both filings, the CAISO largely agreed with the rules approved by the FERC, with certain specific exceptions relating to tagging, outage information reporting and other items. The CAISO also asked the FERC to reconsider its decision regarding a trial period for the implementation of penalties, and urged that the FERC give Regional Entities sufficient flexibility to enable responsible entities to comply with the mandatory standards rather than focusing on the imposition of penalties.

Responsible Attorney: Judi Sanders

SMUD Existing Contract Litigation (SMUD v. FERC, D.C. Circuit 05-1231)

On January 5, the CAISO received a favorable decision from the United States Court of Appeals for the D.C. Circuit, which rejected a petition from SMUD that sought effectively to renew its EHV contract with PG&E. The EHV contract gave SMUD 200 MW of firm transmission over the Pacific Intertie, but expired in 2004. SMUD was appealing FERC's decision that accepted the termination. The CAISO intervened and, together with PG&E, submitted a joint brief in support of the Commission.

As a threshold matter, SMUD argued that the Commission's decision accepting the termination of the EHV contract erred in applying a "just and reasonable" standard, and that PG&E should have been required to show that the termination serves "the public interest." The court rejected this argument, concluding that the just and reasonable standard applies, and that the precedents cited by SMUD were inapplicable.

In addition, SMUD attacked the substance of FERC's decision on two grounds. First, it argued that service termination was unjust because it would subject SMUD to greater risk of price fluctuation under the CAISO tariff. SMUD argued that it would be "unable to secure firm delivery of power it has purchased under long-term firm supply." The court disagreed, explaining that "[t]he CAISO tariff . . . does not deny transmission service to the company. . . . SMUD can always access the power it purchased through long-term supply contracts, though it may have to pay congestion pricing to do so." The court therefore found that SMUD's argument was an improper collateral attack on the CAISO tariff itself. In connection with this issue, the court twice mentioned that "FERC acknowledges the significant financial risks of congestion pricing, . . . and is now addressing these concerns through a comprehensive market redesign proceeding." But the court did not expressly rely on this representation as a basis for its decision.

Second, SMUD argued that the Commission's decision was unduly discriminatory in light of its approval of a 2004 agreement between the CAISO and Western known as the "Transmission Exchange Agreement." That agreement gave Western 400 MW of rights on the intertie in exchange for 1200 MW on the western line of the AC intertie. SMUD argued that it was entitled to the same treatment as Western – despite the fact that it could not offer the same amount or type of transmission in exchange – because it could instead compensate PG&E financially. The court rejected this argument on the basis that SMUD and Western were not similarly situated, as the CAISO and PG&E explained in their joint brief. Unlike Western, SMUD does not own any portion of the intertie, and thus could not offer a capacity exchange similar to what Western offered. This exchange provided additional capacity to CAISO's participants, and FERC had found that fact crucial when approving the Transmission Exchange Agreement. The court emphasized this point, and used it to distinguish the authorities cited by SMUD.

Responsible Attorney: Dan Shonkwiler

CPUC Matters

Resource Adequacy Proceeding Phase 2 – (CPUC Docket No. R05-12-013)

On December 22, 2006, President Peevey of the CPUC issued an Assigned Commissioner's Ruling and Scoping Memo for Phase 2 (ACR) that identifies the issues to be considered in Phase 2 of the CPUC's pending resource adequacy (RA) proceeding. The ACR also sets forth a detailed schedule for submissions and other procedural matters for completing Phase 2. Phase 2 is divided into three "tracks," which are summarized as follows.

- Track 1 Issues – those affecting the RA program for 2008 and 2009 (Final Decision on or about June 21, 2007)
 - Local RA, including (1) review of study methodology and (2) changes to accommodate monthly compliance filings to facilitate tracking of load migration.
 - Probabilistic local reliability analysis (Loss of Load Probability) – CAISO to provide a report on March 9, 2007 that (1) discusses how probabilistic analysis can be incorporated into future local reliability studies, (2) recommendations on this topic, and (3) actions the CPUC can take to facilitate development of a probabilistic analysis.
 - Zonal RA requirements – identification of capacity, in addition to local capacity, needed in zones to ensure compliance with reliability criteria.
 - CAISO to provide proposal by January 26, 2007
 - Demand Response – refine how such resources are counted
 - Load forecasting refinements
 - Consider further coordination between RA and CAISO backstop procurement, i.e., RMR
- Track 2 Issues – longer-term RA market decision proposals (Final Decision on or about January 17, 2008).
Proposals filed on March 9, 2007.
 - Capacity markets
 - Multi-year forward commitments
 - LSE opt-out from cost allocation mechanism
 - Coordination with MRTU as necessary
 - Procurement obligations for resource mix
 - Planning reserve margin
- Identified Track 3 Issues – extension to small CPUC jurisdictional LSEs (Final Decision on or about January 17, 2008)

Responsible Attorney: Grant Rosenblum

Palo Verde – Devers #2 500 kV Transmission Line Application for Certificate of Public Convenience and Necessity (CPUC Docket No. A.05-04-015)

On December 22, 2006, Administrative Law Judge Terkeurst of the CPUC issued a proposed opinion, which recommends granting Southern California Edison's application for a Certificate of Public Convenience and Necessity to construct the Palo Verde-Devers #2 500 kV and Devers-Valley 500 kV transmission lines (PVD2). The proposed decision finds that PVD2 provides economic and reliability benefits to California electricity consumers and adopts a maximum cost for the project of approximately \$545 million. The proposed decision also identifies preferred routes in accordance with the CPUC's authority to perform an environmental review of the project. Comments on the proposed decision are due on January 11, 2007. The Commission will consider the proposed decision at its January 25, 2007 meeting.

The proposed decision did not apply a rebuttable presumption in favor of the CAISO's analysis because the CAISO's submission on PVD2 occurred prior to the adoption of the CPUC's rebuttable presumption opinion.

Responsible Attorney: Grant Rosenblum

Sunrise Powerlink proceeding (A.06-08-010/05-12-014)

On January 8, 2007 the CAISO filed a Motion for Extension of Time to complete its evaluation of the alternatives to the Sunrise Powerlink project presented by intervenors to the proceeding. Various parties, and the environmental consultants for the CPUC, have requested that the CAISO conduct additional reliability and economic studies and submit the results in testimony due on January 26, 2007. The CAISO has agreed to evaluate certain alternatives by that date, and complete the rest of the studies by June or July, 2007. This request will not delay the projected date for issuance of a final order in the case, although the testimony and hearing schedules might be impacted.

Responsible Attorney: Judi Sanders and Bill Di Capo

Rulemaking Regarding Greenhouse Gas Implementation Standards (R.06-04-009)

On December 13, 2006, the CPUC issued a Proposed Decision (PD) adopting interim Greenhouse Gas (GHG) Emissions Performance Standards (EPS) for new long-term financial commitments to baseload generation by all LSEs. The interim EPS was promulgated in compliance with SB 1368 and serves as a bridge until an enforceable load-based GHG is adopted and enforceable. At that time, as required by SB 1368, the CPUC will re-evaluate the EPS in a rulemaking proceeding and in consultation with the CEC and California Air Resources Board (CARB). The PD states that an EPS standard is necessary on an interim basis to prevent "backsliding" in compliance with the GHG emissions standard as California transitions to a statewide emissions cap; without such standards, if LSEs enter into long term commitments for units that do not meet emissions requirements, the California ratepayers will be forced to pay the high cost of retrofits or other expenses associated with compliance.

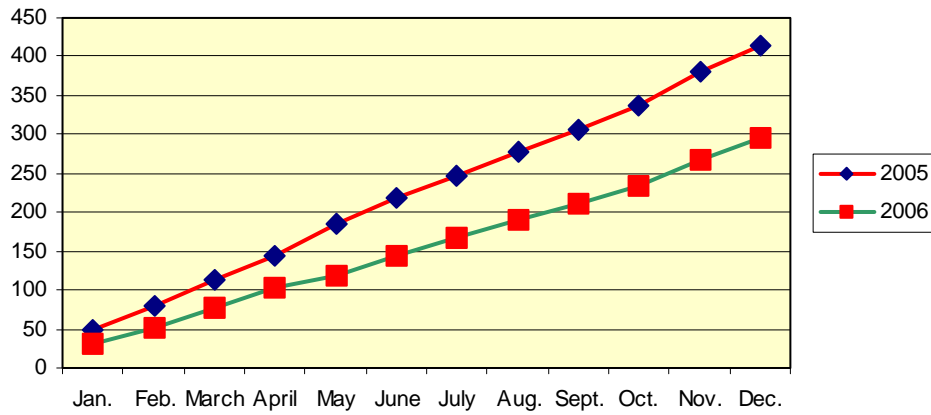
Briefly stated, the interim EPS establishes a minimum performance requirement for any baseload generation facility (defined by the statute as powerplants designed to operate at an annualized plant capacity factor of 60%) that is subject to a long-term financial commitment. For LSE-owned generation, the requirement is triggered when there is "new ownership investment" in an existing baseload facility. For LSE generation procured pursuant to contract, the requirement is triggered by any new or renewed five year contract. "New ownership investment" was interpreted to include investment

that would extend the life of existing baseload generation for five years, or would increase the nameplate rating of the unit.

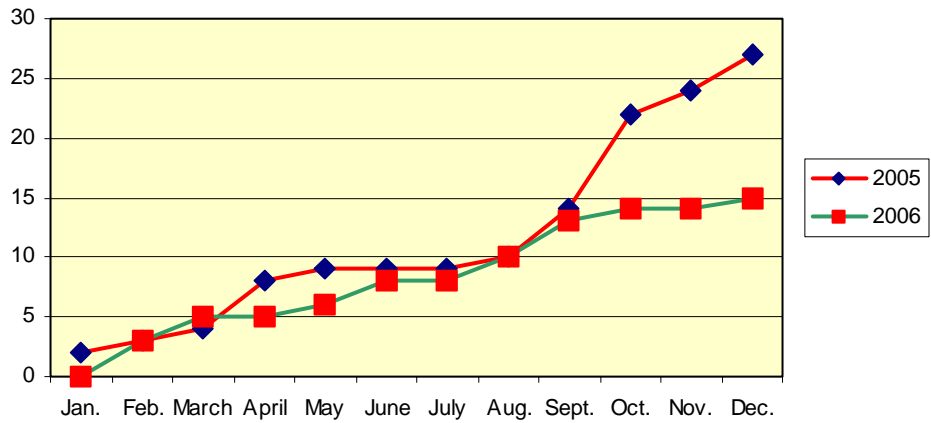
The CAISO provided information to the CPUC for use in the PD and is not participating in the proceeding as a party at this time.

Responsible Attorney: Judi Sanders

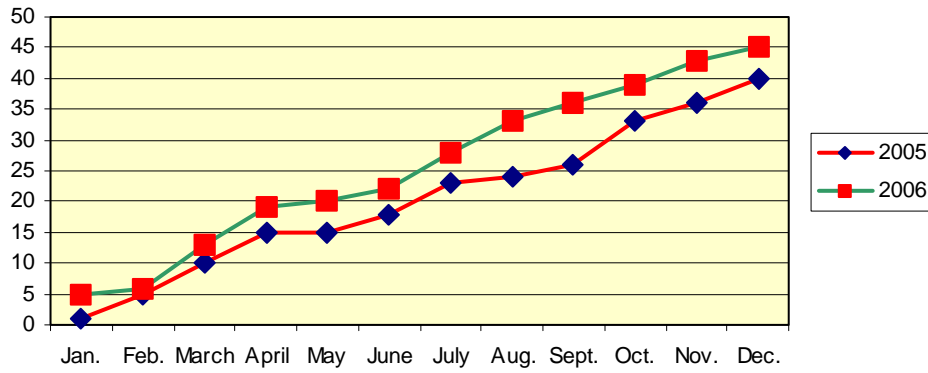
FERC Filings



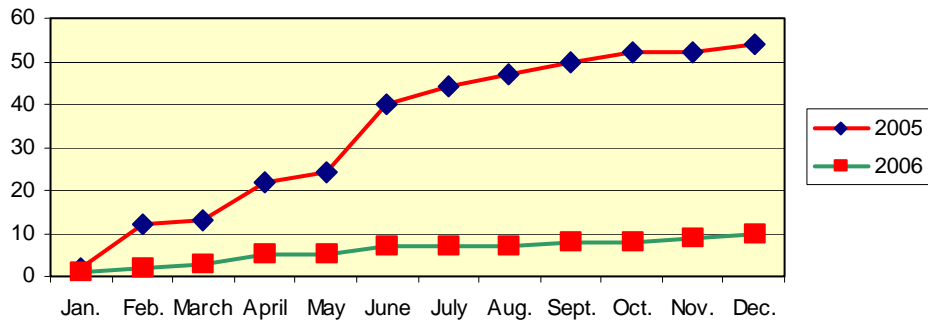
FERC Agreements



CPUC/Other Commission Filings



Court Filings



Total Filings

