

**COMMENTS OF
CONSTELLATION NEWENERGY, INC. and
CONSTELLATION ENERGY COMMODITIES GROUP, INC.
ON BACKSTOP PROCUREMENT**

Submitted to

THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR

Attn: kjohnson@caiso.com

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Constellation NewEnergy, Inc. and Constellation Energy Commodities Group, Inc. (collectively “Constellation”) appreciates the opportunity to submit these brief comments as a follow up to the stakeholder meeting conducted by the California Independent System Operator (“CAISO”) on May 18, 2007 (“May 18 Meeting”). That stakeholder meeting initiated the important effort to design and implement specific measures by which the CAISO will procure capacity and other services that are not made available to the CAISO through resource adequacy requirements (“RAR”) procurement.

Constellation generally concurs with the approach laid out by the CAISO at the May 18 Meeting – that the current Reliability Capacity Services Tariff (“RCST”) provides the right framework for CAISO backstop procurement and that CAISO backstop procurement should replace Reliability Must Run (“RMR”) Agreements. Constellation also generally concurs that the issues raised by the Independent Energy Producers Association (“IEP”) with respect to specific modifications that will improve RCST as a backstop procurement mechanism, including review and reform of the compensation mechanism and retention of appropriate performance metrics for capacity resources, must be addressed.

Constellation believes that in nearly all cases, CAISO backstop procurement should occur only once per year, immediately after Load-Serving Entities (“LSEs”) have made their final annual

RAR compliance demonstrations. At that point in time, the CAISO will know what the committed RAR resources are that will be available to meet the local requirements, including the planning reserve margin. If there are specific, defined shortcomings in the RAR compliance demonstrations, the CAISO should undertake backstop procurement to secure the resources necessary for that coming annual period. Additional backstop capacity procurement throughout the year should simply not be necessary, as the planning reserve margin is intended to provide the resource availability “cushion” in the event of higher than expected loads and/or unexpected outages of generation and transmission. Since backstop procurement by the CAISO in excess of the planning reserve margin will represent an increase in costs to consumers, it is a policy that should be avoided.

If, however, the CAISO backstop procurement mechanism is going to include provisions that allow the CAISO to secure resources throughout the year in response to “Significant Events”, the circumstances under which such purchases will be made must be fully transparent to all market participants. This transparency is necessary so that transactions that LSEs and capacity resource owners have entered into to meet the RAR requirements contain the appropriate provisions with respect to CAISO backstop procurement that may occur. For instance, the CAISO has indicated that an extended transmission outage is an example of the type of “Significant Event” that may trigger CAISO backstop procurement at any time throughout the year, when the transmission outage compromises the ability for the RAR-committed resources to ensure reliability. LSEs and capacity resource owners that have transacted for such resources that are no longer useful to the CAISO will want to structure their transactions so that the risks (costs) of the CAISO “Significant Event” backstop procurement are explicitly provided for in their RAR transactions. For this to occur, the parties must have a clear understanding of just what the circumstances are that will cause the Significant Event backstop procurement, and how those costs are going to be allocated, so that they

can determine, at the time they execute their RAR transaction, which party will bear those risks and costs.

Constellation appreciates the CAISO's attention to these important issues and looks forward to working with the CAISO and market participants in formulating appropriate CAISO backstop procurement mechanisms.