

July 19, 2005

**The California Department of Water Resources/State Water Project's
Comments to the California Independent System Operator on the Proposed
Local Area Reliability Backstop Contracts**

The California Department of Water Resources/State Water Project (SWP) welcomes the opportunity to provide the following comments to the California Independent System Operator (ISO) on the ISO's proposal for Local Area Reliability (LAR) Backstop Contracts:

1. The California Public Utilities Commission (CPUC) Rulemaking 04-04-003 on Resource Adequacy (RA) has made clear that RA is the responsibility of Load Serving Entities (LSE), not the California Independent System Operator (ISO). The ISO's plan for Backstop Contracts assumes that RA requirements will be insufficient in local areas or pockets within the local areas. SWP disagrees with this assumption and believes that a properly constructed and functioning RA should eliminate the need for Backstop Contracts. As proposed by the ISO, resources under a RA contract with a LSE will be available to the ISO under the ISO's Must Offer. If ISO believes that the CPUC's RA requirements are not sufficient in a local area or pocket then ISO needs to work with CPUC to make RA more stringent or more specific for an area or pocket.
2. If Backstop Contracts are implemented, then the requirements for such should follow WECC/NERC planning criteria for the local areas and pockets within the local areas. The ISO should not confuse criteria to develop the RA obligation, or ISO's attempts to fill missing RA obligation through Backstop Contracts, with the ISO's real-time security obligation, i.e., the ISO should not overlay the operating reserve criteria on the planning criteria for setting the amount of capacity to be met through Backstop Contracts.
3. If Backstop Contracts are implemented, then the RA requirements should be placed on both local areas and specific pockets within local areas, e.g., LA Basin as a local area with one set of requirements is too large and should be broken down on a more granular basis. The ISO local RA assessment should not only answer the question of "how much RA resources are needed in a local area?" but also answer the question of "are those RA resources deliverable to the LSE's load in the pocket areas where they are needed?"
4. If Backstop Contracts are implemented, then the ISO could be confronted with additional and controversial cost causation and allocation issues as well

as extensive litigation before the Federal Energy Regulatory Commission. To avoid these, the ISO needs to develop cost allocation methodologies based on “cost causation” principles under which 100% of the costs for the contracts are allocated to the LSEs that are responsible for the load under the RA requirements. This will also avoid perverse incentives for LSEs to avoid entering into RA contracts or to under schedule load at the ISO Day-Ahead market.

5. If Backstop Contracts are implemented, the ISO procured local resources should only be used to meet the local or pocket RA needs. If each LSE is resource adequate and each local area or pocket area is resource adequate then there should be no system-wide RA needs. If there are system reliability problems then these need to be identified and addressed separately and dealt with by the ISO through its market mechanisms.