

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

Application of Southern California Edison  
Company (U338-E) for Approval of Demand  
Response Programs, Goals, and Budgets for  
2009-2011

Application 08-06-001  
(filed June 2, 2008)

Application of San Diego Gas & Electric  
Company (U 902M) for Approval of Demand  
Response Programs, Goals, and Budgets for  
2009-2011

Application 08-06-002  
(Filed June 2, 2008)

Application of Pacific Gas and Electric  
Company for Approval of the Demand  
Response Programs, Goals, and Budgets for  
2009-2011 (U 39-E)

Application 08-06-003  
(Filed June 2, 2008)

**REPLY BRIEF OF  
THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

Dated: February 11, 2009

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OPERATOR CORPORATION

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**REPLY BRIEF OF  
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The California Independent System Operator Corporation (“CAISO”) submits this Reply Brief regarding the California Public Utilities Commission’s (“Commission”) consideration of the Applications of Southern California Edison Company (“SCE”); San Diego Gas & Electric Company (“SDG&E”), and Pacific Gas and Electric Company (“PG&E”).

**I. THE CAISO SUPPORTS DRA’S ARGUMENT THAT THE COMMISSION SHOULD ASSIGN LITTLE T&D BENEFIT TO DR PROGRAMS**

The CAISO supports the position of DRA that the Commission should assign no or very little deferred T&D benefit, in its evaluation of the DR programs. DRA notes that

Other parties’ comments regarding the allocation of T&D benefits to DR programs emphasize the fact that meeting the ‘right place,’ ‘right time,’ and ‘right certainty’ requirements will be a difficult task. (Opening Brief of DRA [Redacted Version] at p. 17.)

The CAISO believes that meeting these requirements, the ability to identify and trigger demand response resources *when* and *where* they are needed, should be a key consideration in the Commission’s evaluation and investment in demand response programs and infrastructure. As the CAISO touched upon in its Opening Brief, even if the utility is able to demonstrate that the demand response resource resides in a desirable area (e.g. in a transmission-constrained local capacity area), an important component of the resource’s value lies in its ability to be called upon to resolve the constraint. If a demand response program is dispatched through an imprecise system that either triggers all of the resources in the program at once or many resources unrelated to resolving the constraint, then the program is less suitable under the “right place, right time, right certainty” criteria. The Commission should support DRA’s position and be circumspect

about applying any avoided T&D benefit to demand response programs until the underlying demand response resources in the program prove they can be sufficiently relied upon, from an operational and planning perspective, as resources that are available when and where needed.

**II. CAISO SUPPORTS DRA’S POSITION THAT THE UTILITIES SHOULD FREEZE BIP AT CURRENT LEVELS UNTIL THE COMMISSION DETERMINES THE APPROPRIATE LEVEL OF EMERGENCY-TRIGGERED AND RELIABILITY BASED DR IN R07-01-041**

The CAISO supports DRA’s proposal that the Commission should direct the utilities to freeze the Base Interruptible Programs (BIP) until such time as the Commission issues a final decision in Phase 3 of the DR Rulemaking (R.07-01-041).<sup>1</sup> The CAISO is not questioning the utility of the BIP program; rather, the CAISO believes that adding additional customers to the BIP program may not be prudent until the Commission rules affirmatively on the nature and level of reliability-based programs in Phase 3 of the DR Rulemaking. In the current applications, it appears that only SCE expects to increase enrollment (by 10 percent) during the 2009-2011 program cycle.<sup>2</sup> As such, program growth for reliability-based programs should be deferred pending resolution of the issues in R.07-01-041.

**III. THE CAISO SEES NO INCONSISTENCY BETWEEN THE COMMISSION’S RA REQUIREMENTS AND THE COMMISSION’S FOCUS ON “PRICE RESPONSIVE” DEMAND**

The CAISO agrees in principle with TURN’s comments that

Ultimately, demand resources should be properly compensated by appropriately valuing any potential *capacity* benefits due to demand response. Such a valuation can be done either through tariffed energy

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<sup>1</sup> Opening Brief DRA (Redacted Version) at p. 30.

<sup>2</sup> Ex 201, p. 2-6, line15.

rates that appropriately include generation capacity costs, or through fixed capacity payments analogous to those paid to generators.<sup>3</sup>

TURN remarks that on-peak wholesale prices have been significantly reduced due to resource adequacy (RA) requirements, and “as a result, most incentives or rates derived from actual wholesale market prices do not provide customers with sufficient financial incentives to install expensive equipment or make changes in operations for the limited purpose of reducing load for less than 100 hours in the year.”<sup>4</sup> Thus, TURN concludes that based, on the Commission’s RA policy “...there is a fundamental inconsistency between the Commission’s resource adequacy requirements and the Commission’s focus on “price responsive” demand response.”<sup>5</sup>

Contrary to TURN’s opinion, the CAISO does not believe that there is a fundamental inconsistency between the Commission’s RA requirements and the Commission’s focus on “price responsive” demand response. Rather, the CAISO believes the Commission should pursue price responsive demand that is *consistent* with its RA program and policies.

TURN’s comments do elicit an important issue of whether there is sufficient “revenue adequacy” to support investment in new demand response resources. However, this issue must be addressed in the context of the RA paradigm that we do operate under, and not, as TURN implies, under an “energy-only” paradigm that we do not operate under.

An expert in wholesale market design, Dr. Bill Hogan, framed the “revenue adequacy” issue, often called the “missing money” problem, as follows:

Electricity resource adequacy programs often target the “missing money” problem. The missing money problem arises when occasional market price increases are limited by administrative actions such as price caps. By preventing prices from reaching high levels during times of relative scarcity, these administrative actions reduce the payments that could be

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<sup>3</sup> Opening Brief of TURN, at p. 8 (emphasis in original.)

<sup>4</sup> Opening Brief of TURN, at p. 4

<sup>5</sup> Opening Brief of TURN, at p. 5

applied towards the fixed operating costs of existing generation plants and the investment costs of new plants. The resulting missing money reduces the incentives to maintain plant or build new generation facilities. In the presence of a significant missing-money problem, alternative means appear necessary to complement the market and provide the payments deemed necessary to support an appropriate level of resource adequacy.<sup>6</sup>

As explained above, when operating under a RA paradigm, demand response resources, just like generating resources, are likely to need revenue sources other than from the wholesale spot markets to ensure “revenue adequacy.” This fact does not translate into an inconsistency between the Commission’s RA requirements and “price responsive” demand. Rather, it simply implies that demand response resources potentially suffer from the same “missing money” concerns that certain supply-side resources experience if they are unable to tap into other revenue sources such as resource adequacy capacity payments or other bi-lateral arrangements.

As a case in point, the CAISO’s own Department of Market Monitoring has consistently reported that the total fixed cost recovery, fixed O&M cost, plus the cost of capital were not achieved through spot market revenues, for combined cycle and CT units over certain reported periods.<sup>7</sup> For supply-side resources, revenue adequacy is achieved by earning revenues in the wholesale markets and through other bi-lateral arrangements. Accordingly, it may not be realistic to expect that demand response resources fair any better in recovering costs only through the spot markets, and like supply-side resources, may need to capture additional revenue through RA capacity payments or, as TURN comments, “... through fixed capacity payments analogous to those paid to generators.”<sup>8</sup> For these reasons, the CAISO sees no inconsistency between the Commission’s RA requirements and the Commission’s focus on “price responsive” demand. Instead, in reviewing and approving cost-effective, price-responsive DR programs, the Commission

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<sup>6</sup> W Hogan “On an ‘Energy Only’ Electricity Market Design for Resource Adequacy,” September 23, 2005. This document can be accessed at <http://www.ucei.berkeley.edu/POWER-06/06Papers/8Hogan.pdf>.

<sup>7</sup> California ISO 2007 Annual Report of the Department of Market Monitoring, Section 2.6.4 at p 2.54.

<sup>8</sup> Opening Brief of TURN, at p. 8

must be cognizant of what revenue or incentive opportunities are appropriate for demand response resources to achieve revenue adequacy under the existing RA paradigm.

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Respectfully submitted

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## **CERTIFICATE OF SERVICE**

I hereby certify that on February 11, 2009, I served, on the Service List for Consolidated Proceedings A08-06-001, A08-06-002 and A08-06-003, by electronic mail, a copy of the foregoing

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Executed on February 11, 2009  
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*/s/ Anna Pascuzzo*

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