

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

Order Instituting Rulemaking to)	
Integrate Procurement Policies and)	
Consider Long-Term Procurement)	R. 06-02-013
Plans)	
_____)	

**COMMENTS OF
THE CALIFORNIA INDEPENDENT
SYSTEM OPERATOR
ON THE JUNE 20, 2006
DRAFT DECISION**

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Dated: July 10, 2006

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In accordance with Rules 77.2, 77.3 and 77.4 of the Commission’s Rules of Practice and Procedure, the California Independent System Operator Corporation (“CAISO”) respectfully submits its comments on Administrative Law Judge (“ALJ”) Brown’s draft decision entitled “Opinion on New Generation and Long-Term Contract Proposals and Cost Allocation,” mailed June 20, 2006, in the above-referenced proceeding (“Draft Decision”).

I. INTRODUCTION AND OVERVIEW

The Draft Decision aptly recognizes the importance of balancing the competing interests in this proceeding so as to provide reasonable assurances that the generation needs of California consumers will be met while at the same time continuing to move towards a competitive market and customer choice. The CAISO applauds the efforts of the ALJ in structuring a modified cost allocation mechanism containing both incentives and safeguards, and supports its adoption on an interim basis until such time as a functioning capacity market and other market institutions (such as the CAISO’s Market Redesign and Technology Update (“MRTU”) program) are implemented.

The CAISO focused its participation in Phase I on the issue of generation “needs” criteria from the perspective of network planning, operations and grid reliability. It is anticipated that these issues will be addressed in detail when the Commission initiates Phase II of this proceeding through the scoping memo described in footnote 2 of the Draft Decision. The Draft Decision touches on several important procurement

considerations that were raised by the CAISO and that should be given greater emphasis in the final order. Finally, the Draft Decision identifies many implementation details and policy decisions that will be considered in other proceedings. Because the modified cost allocation mechanism is intended to be transitional, the CAISO looks forward to working with the Commission in resolving these issues on an expeditious basis so that the next steps can be taken as quickly as possible.

II. THE COMMISSION SHOULD CONSIDER PLACING GREATER EMPHASIS ON DETERMINING RESOURCE NEEDS BEYOND 2009

The CAISO concurs with the Draft Decision's finding that California has a need for new generation to be brought on line as early as 2009. However, the CAISO is concerned about resource needs for 2010 and beyond, which is the timeframe to be addressed in the upcoming 2006 long-term procurement plans ("LTPP"). At several places in the Draft Decision, the Commission has indicated that additional system needs will be considered in Phase II, which presumably will be initiated by the scoping memo described above (Draft Decision, 7; Finding of Fact No. 5, 49). The CAISO urges the Commission to include, in the scoping memo describing the 2006 LTPP, detailed directions as to the information that the IOUs should provide regarding their anticipated resource needs starting in 2010. This information should take into consideration the comments and guidelines submitted by the CAISO regarding the "right amount, right mix and right location" of resources necessary for system reliability which included operations and historic data that should be factored into any analysis of resource adequacy (CAISO comments, 16-19).

III. THE COMMISSION SHOULD NOT MAKE FUNDAMENTAL STRUCTURAL CHANGES TO THE MODIFIED PROPOSAL, PARTICULARLY IF CHANGES WOULD DELAY THE COMMISSION'S FINAL DECISION

The Draft Decision has taken a "middle of the road" approach to the comments and proposals submitted by the parties by taking the basic framework of the Joint Parties' proposal, making modifications suggested by parties who would "stay the course" and adding elements of the revisions suggested by the Indicated Parties. (Draft Decision, 25-26). While the CAISO would not have recommended that the IOUs be designated to procure new generation within their service territories on behalf of all customers, this

aspect of the framework, as modified, is acceptable on an interim basis. It is important that the Commission now “stay the course” with its modified mechanism, and not be persuaded to make further revisions that would push the new generation procurement process back in the direction of reintegration.

For example, at the June 28, 2006 All Parties Meeting, the IOUs expressed concerns about a number of items, including the exclusion of utility-owned or built generation. This aspect of the modified mechanism, while described by the IOUs as creating an unfair disadvantage against them, is a feature that is intended to promote competition and should not be revised. Additionally, “tinkering” with the Draft Decision to provide additional cost recovery certainty should also be avoided at this point. Furthermore, the unbundling of capacity and energy from the new resources, with the costs and benefits of the capacity assigned to all ratepayers on the IOU’s distribution system and the energy component subject to an auction process, is critical if this process is truly to be a stepping stone on the way to a robust wholesale market.

IV. THE IOUS SHOULD BE REQUIRED TO EXPLORE REPOWERING OPPORTUNITIES AS PART OF THE RFO PROCESS, AS EARLY AS PROCUREMENT FOR THE YEAR 2008

The CAISO is pleased that the Draft Decision specifically acknowledged its recommendation regarding the facilitation of repowering as part of the long-term procurement process. (CAISO Comments, 15-16; Draft Decision, 3, 28). The importance of using existing facilities, in whole or in part, to develop cleaner, more efficient sources of generating capacity cannot be overemphasized. Rather than simply encouraging the IOUs to include repowered brown sites in the competitive bid process, the CAISO would like to see the Commission go a bit further and establish a state policy to encourage the repowering of facilities. This policy could require the IOUs to explore, and give preference to, repowering opportunities. The Commission should consider going as far as establishing a specific requirement that the parties must procure some percentage of their resources from repowered facilities within some time-certain time frame. The CAISO encourages the Commission to provide incentives to repower or expedite the construction of a reasonable portion of such resources as early as the year 2008 (it may be too late to do much about the year 2007, but it is certainly realistic to

provide such a requirement and a complementary incentive mechanism for the year 2008). The Draft Decision correctly cautions the IOUs to be flexible with online dates so that these potential valuable resources are not excluded from their portfolios, while noting that RFO procedures will be addressed in more detail in Phase II. (Footnote 23) Nonetheless, the CAISO suggests that repowering be given a higher priority at this point in the proceeding, and that the language of the Draft Decision be modified as follows:

- Each IOU may fill its new generation need by way of a competitive RFO, which is open to any fuel type or technology from both green and repowered brown sites. In D.04-01-050, we strongly encouraged repowering, if possible, and we continue to believe that repowered projects are beneficial. Given the potential economic benefits of such projects, we explicitly require IOUs to give preference to repowerings as part of the RFO evaluation procedures. ~~We do not explicitly require IOUs to give preference to repowerings, but we expect that IOU RFO evaluation procedures will value the economic benefits of repowering.~~ The IOUs should be flexible with the on-line dates so that potential viable resources, especially repowered sites, are not excluded if there is a short gap in which an existing power plant continues to produce power, before the new plant gets built and comes on-line.

(Draft Decision, Section IV.B., 28-29)

V. THE COMMISSION MUST MOVE QUICKLY TO END THE TRANSITIONAL PERIOD

As noted above, the CAISO appreciates the daunting task that faced the Commission in evaluating the proposed policies for the development of new generation to come online in a 3-4 year time period, and supports the proposed approach for an interim period. Unfortunately, the interim period has no defined termination date, and is contingent upon a host of policy decisions that must be resolved in Phase II of R.05-12-013, in particular the capacity market design or development of other market institutions that will replace this cost allocation mechanism.¹ In addition, there are numerous details concerning the cost allocation methodology and long-term procurement plans that need to be addressed in Phase II of this proceeding before the process can even be put in place. Quite candidly, the Commission and its very capable Staff have a considerable amount of

¹ Other equally important policy issues have yet to even be assigned to a docket, such as reinstating DA, and yet these matters must also be included in the continuum of progress towards a competitive energy market.

work ahead of them, with tasks that must be accomplished promptly. The CAISO intends to provide as much assistance and support as possible as the Commission and interested parties work together through the myriad details confronting them. The CAISO looks forward to actively participating in the Commission's continued development of the wholesale market and coordinating these efforts with its MRTU implementation and resource adequacy initiatives.

**VI. RESOURCES THAT HAVE BEEN PROCURED BY THE IOUs
PURSUANT TO THE TRANSITIONAL COST ALLOCATION
MECHANISM MUST BE IDENTIFIED FOR RAR OBLIGATION
PURPOSES.**

If the IOUs procure resources on behalf of benefiting customers, these resources should be made available for resource adequacy purposes. However, the Draft Decision does not specifically address the process by which LSEs will be made aware that the IOUs have procured resources that would be available for meeting local and system RAR obligations. If such resources are identified late in the RAR annual process, it is possible that there could be under-procurement or double-counting. The CAISO recommends that these details be addressed in Phase II of this proceeding.

Respectfully submitted,

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