

Energy Choice Matters

March 19, 2008

Ambit Prepares to Enter Illinois Gas Market

Ambit Energy, which has focused on building a multi-level marketing platform in New York and Texas, yesterday applied to become an alternative gas supplier in Illinois serving residential and small commercial customers in the Nicor Gas, Peoples Gas, and North Shore Gas territories.

Ambit serves solely residential electric customers in Texas while in New York it serves residential and small C&I electric and gas accounts, it told the ICC.

Ambit's primary gas trading partner is Shell Trading North America (Coral Energy) and it is also advised by Navigant Consulting and Randolph Risk Management.

Entering the Illinois gas territories gives Ambit access to 2.4 million more households, the retailer said.

Ambit stated on its application that it was not seeking an alternative retail electric supplier license at this time.

California ISO Defends Interim Capacity Procurement Mechanism

The California ISO reminded FERC (ER08-556 et. al.) of a few important points that seem to have been lost in the debate over its Interim Capacity Procurement Mechanism (ICPM).

Generators have attacked the proposal for blunting price signals and other allegedly discriminatory provisions (Matters, 3/3/2008).

First, the CAISO is not attempting to create a centralized capacity market with the ICPM, the grid operator stressed.

Second, the ICPM is not intended as a mechanism to incent new generation, the ISO reported.

Third, the ICPM is not intended to be a referendum on the state's Resource Adequacy (RA) program, or to modify the RA program.

The ICPM is merely an interim, administrative mechanism that will permit the CAISO to efficiently procure backstop capacity on a short-term basis from existing resources that have capacity available, and which are willing to make that capacity available to the CAISO via a forward ICPM designation, the ISO explained.

Given the interim nature of the ICPM (with an automatic sunset of Dec. 31, 2010), the uncertainty as to whether (or when) there will even be any ICPM procurement, and the fact that the ICPM is merely intended to "fill" any gaps in LSE procurement and permit the CAISO to undertake short-term procurement in response to unplanned significant events, the ICPM clearly will not -- and cannot reasonably be expected to -- "drive" new investment or repowering of existing units, CAISO added.

Designations under the ICPM are voluntary, CAISO reminded, and unit owners are not required to accept them.

To the extent protesting parties take issue with the state's RA program, they should raise their issues with the California PUC, the ISO told FERC.

The CAISO has designed its ICPM proposal so that it does not unduly "interfere" with the existing RA program (e.g., by unduly influencing RA prices upwards or downwards) or pre-judge the issues that the CAISO soon will be discussing with stakeholders regarding a long-term capacity procurement mechanism.

Accordingly, the CAISO urged the Commission not to "put the cart before the horse" by

... Continued Page 4

CONE Adjustment Allowed Under PJM Tariff, Generators Say

PJM is not required to revise the Net Energy and Ancillary Services Revenue Offset (E&AS Offset) when modifying the Cost of New Entry (CONE) values used in the Reliability Pricing Model, PJM Power Providers Group (P3) told FERC yesterday (ER08-516).

Opponents of adjusting CONE to reflect what PJM says are higher costs for new generation had argued that raising CONE while not boosting the E&AS Offset which reflects other revenues available in the PJM market would produce unjust and unreasonable prices (Matters, 3/7/2008).

But PJM's tariff already provides for annual adjustments to the E&AS Offset, P3 said.

The RPM settlement explicitly provided that PJM retained all rights to make a filing with the Commission under Section 205 of the Federal Power Act to modify any tariff provisions, including the provisions listing the CONE values, the generators added, rebutting criticisms that the CONE filing was premature.

Additionally, neither PJM's tariff nor the RPM settlement require that changes in the E&AS Offset methodology be made every time CONE values are updated, P3 pointed out.

SCE Attacks IPPs Over Debt Equivalency

Independent generators' objections to using debt equivalency to evaluate PPA bids when utility-owned generation isn't an option are, "unreasonable and without basis," Southern California Edison told the California PUC (R 06-02-013).

SCE and the other utilities had proposed reinstating a debt equivalency factor for all solicitations where there are no utility-owned proposals. The debt equivalency adder could only be used in projects including a utility-owned option if the utility had, "demonstrated, to the satisfaction of the Energy Division, that it has developed a method for fairly evaluating the costs of," utility-own projects.

Generators, including the Independent Energy Producers Association (IEP), had

urged the PUC to not bring back the use of discriminatory debt equivalency adders which place merchant projects at a disadvantage to utility proposals (Matters, 2/26/08).

But debt equivalence is an economic cost of contracting for power, SCE claimed, and must be taken into account when evaluating different PPAs in order to enable the utilities to select to the least-cost, best-fit resources in their competitive solicitations.

SCE saw, "no rational basis," for objections to using debt equivalence to compare one PPA to another PPA.

SCE also wants the PUC to allow use of a debt equivalence adder once "appropriate" bid evaluation criteria that reflect utility-owned generation "incremental risks" have been developed.

"One gets the distinct impression that the only RFO process that IEP will ever be satisfied with is one where it reviews all the bids and tells the Utilities which projects should be accepted," SCE complained.

Claiming, as IPPs have done, that rating agencies are not concerned about the growing risks associated with the utilities' increasing reliance on PPAs is "bogus," SCE added, citing California-specific ratings reports.

SCE asserted that a Standard & Poor's report expresses concerns regarding SCE's lack of intentions to procure new utility-owned generation while a Moody's report views ratebase growth from capital investment plans as a long-term ratings positive.

"As is clear from the recent rating agency report on SCE, and the unchallenged findings of this Commission, a significant risk to the creditworthiness of the utilities today is the risk associated with the ever-increasing volume of PPAs — not the hypothetical risk associated with the possibility of procurement of new generation resources," SCE argued.

PJM Urges Stakeholder Review of Duquesne Portable Capacity

PJM urged FERC not to issue a rehearing or clarification regarding "portable" capacity created in the Commission's order ending Duquesne Light's RPM obligations after 2010 (ER08-194).

In the Duquesne exit order, FERC suggested that Duquesne and other LSEs in its footprint could use capacity bid into PJM's RPM auction for delivery years 2008-2010 to satisfy reliability requirements other than those under RPM, such as those in the Midwest ISO.

PJM suggested that it, the Midwest ISO, reliability councils and stakeholders should first have an opportunity to develop a mechanism to allow capacity procured through RPM to meet the Midwest ISO's reliability requirements as required by the January 17th Order before FERC issues any clarification as requested by some stakeholders, such as Exelon (Matters, 2/19/2008).

"Further clarification of the portability concept, before the parties have explored what would constitute a mutually acceptable framework, is unnecessary and unlikely to facilitate crafting an acceptable agreement," PJM said.

PJM pointed to the delay in the start of the Midwest ISO's ancillary services market (Matters, 3/14/2008) as providing further justification for granting stakeholders time to address the matter, "as Duquesne's transition filing may itself be delayed," PJM suggested. PJM did not elaborate on how the filing may be delayed, or what implication a delay would have on Duquesne's RPM obligations.

NERC Working on New Rules for Registering Competitive Retailers

NERC proposed a two-step process to address the potential gap in reliability functions caused by FERC's December decision to reject NERC's inclusion of three competitive retailers on NERC's compliance registry (RC07-4 et. al.)

FERC had found that the inclusion of Direct Energy Services, Sempra Energy Solutions and Strategic Energy on ReliabilityFirst's compliance registry as LSEs was not supported by the registry criteria, since the retailers did not own grid assets. The Commission also concluded NERC failed to adequately identify the reliability standards for which retailers registered as LSEs would be responsible, and found inconsistent application

of the registry criteria among Regional Entities.

But in striking the registrations, FERC told NERC to work on a solution to close any reliability gap caused by excluding competitive retailers from the registry.

In the short-term, NERC will gather comments on revising the registration criteria to define "Non-Asset Owning LSEs" as a subset of Load Serving Entities and will specify the reliability standards applicable to that subset. NERC's board will consider the revisions at its May meeting.

In the long-term, NERC will determine the changes necessary to terms and requirements in reliability standards to address the issues surrounding accountability for loads served by competitive retailers and process them through execution of the three-year Reliability Standards Development Plan.

NERC will start by holding an LSE compliance workshop April 15 in Houston.

Briefly:

PUCT Opens Settlement for Picking CREZ Transmission Builders

The PUCT designated settlement conference procedures to select transmission service providers to build lucrative new lines to competitive renewable energy zones (dockets 35424, 33672, 34560). The Commission will continue its rulemaking process in docket 34560 in parallel to settlement talks. Franchised transmission utilities and merchant transmission providers have split on how the PUCT should select firms to build lines to access remote renewable generation. The PUCT also favored using a streamlined process which collapses the selection and qualification processes for the selection of transmission service providers (Matters, 3/6/2008, 2/5/2008).

Consumers Withdraws Residential Efficiency Plan

Consumers Energy withdrew its proposal in Michigan PSC Case No. U-15190 to offer a residential natural gas energy efficiency program at the cost of \$9.3 million, proposed to be recovered from residential ratepayers. The original rate case was mostly settled in

the summer, but parties differed on whether the cost of Consumers' residential efficiency program could only be recovered from residential ratepayers (as a settlement had proposed), or whether the costs had to be reflected in general utility rates paid by all classes as the PSC had suggested in its order. With the residential efficiency program withdrawn, Consumers, the Association of Businesses Advocating Tariff Equity (ABATE), PSC staff and the Attorney General agreed in a settlement to close the docket. The National Energy Marketers Association did not oppose the settlement.

Pepco Energy Services Gets Preliminary Conn. Nod

The Connecticut DPUC recommended in a draft decision granting Pepco Energy Services an electric supplier license to serve residential, commercial, and industrial customers (08-01-10). Pepco Energy Services would limit residential marketing to customers whose businesses are supplied by the retailer (Matters, 2/6/2008).

Consumer-Level Smart Meter Hits Euro Market

Energy Optimizers Limited has developed a ZigBee-based plug-in electricity meter that it claimed can help companies and households shave hundreds of dollars off their electricity bills, but the North American market will have to wait before receiving the potentially value-adding product. The device, called a plogg, allows customers to monitor how much electricity is being used by individual appliances simply by attaching it to that appliance. The plogg stores the measured electricity data and wirelessly communicates information to a personal computer or mobile phone and would even allow remote control and shut-off of appliances. The plogg could also support time-of-use metering, but so far is only available for European electrical devices. A North American plogg is being studied.

LS Power Eyes Northern Va. Plant

LS Power wants to build an 873-MW, natural-gas fired power plant in Prince William County, Va., in the D. C. metro area.

CAISO ICPM ... From 1

adopting the multi-year ahead capacity market-type features recommended by the Independent Energy Producers Association (IEP) and others. Rather, FERC should instead direct that those issues be fully vetted in the context of a CAISO stakeholder process to develop a more permanent capacity procurement/pricing mechanism to function in conjunction with the long-term RA design.

The CAISO believes that the proposed ICPM sufficiently meets its goal of enabling the ISO to backstop LSE-based RA capacity procurement from existing resources as needed for reliability using a transparent and efficient tariff-based mechanism.

The pricing of the ICPM is both just and reasonable, and consistent with rate principles previously adopted by FERC, CAISO argued. The proposal essentially permits the procurement of capacity from existing resources that either (a) have voluntarily decided to participate in the forward time frame (i.e. prior to the RA showing for the compliance year) based on the CAISO's ICPM price offer, or (b) after the forward showing for resources, have decided to remain in operation during the year without having an RMR or RA contract, with the expectation of only making market or off-system sales.

FERC precedent states that a program such as the ICPM would promote order and transparency in the market by clearly telling sellers of the maximum price the ISO was willing to pay, and allowing sellers to make informed economic choices on whether to sell to the CAISO or to sell elsewhere, the ISO explained.

If the program fails to meet the CAISO's procurement needs, the CAISO will need to make adjustments.

But the CAISO believes adjustments should not be necessary because the proposal will, at a minimum, cover a resource's going forward costs (plus 10%) -- and in most instances should cover an even larger portion (or even the entirety) of the total fixed costs (including recovery of and return on capital) for many resources for the period of designation-- while allowing resources to retain all market

revenues (i.e., there is no peak energy rent deduction for ICPM capacity).

Thus, the ICPM appropriately values any energy required from the unit by enabling it to retain the market price, including scarcity payments, CAISO said.

The proposed minimum capacity price to be paid to designated units under the ICPM falls at the high end of the range of prices paid to RA resources under bilateral RA contracts used to meet PUC RA obligations, the ISO noted. That will encourage both suppliers and LSEs to enter into RA contracts and not rely on the backstop, CAISO suggested.

CAISO sees no logical, economic or legal basis for using cost of new entry pricing (CONE) for ICPM capacity (as proposed by IEP) given the following facts:

(1) the interim nature of the ICPM and the fact that new entry cannot compete with existing resources to provide ICPM service, because the ICPM is not a multi-year forward capacity market;

(2) the fact that ICPM procurement is not intended to and will not incent new generation given the uncertain and short-term nature of ICPM procurement;

(3) the adoption of CONE pricing will result in payments to ICPM resources that are significantly higher than the prices that are being paid to RA and RMR resources and would likely interfere with the existing RA program and attempts to design a more permanent long-term RA framework and capacity pricing mechanism;

(4) for 2008 a capacity surplus exists systemwide in seven of the ten local capacity areas and, for 2009, a capacity surplus exists in eight of ten local capacity areas, and in those areas of deficiency most of the capacity is either owned by the investor-owned utilities or is under long-term contract; thus CONE pricing will not benefit the California generators for the short period of time that ICPM will be in effect;

(5) CONE pricing will allow resource owners in local areas where ownership is concentrated to increase prices even though there is a surplus of capacity and new entry is not needed in those areas; and

(6) CONE pricing is wholly inappropriate for

short-term ICPM designations due to unexpected and transitory Significant Events where new generation cannot provide the service and there is no indication that new resources should even enter the market at that particular location in the long-term due to the transient nature of the event.

In short, IEP's proposal, "would result in significant over-procurement of capacity due both to amount of capacity required to be procured and to the duration of the designation (which would be wholly unrelated to the period of time that the capacity is actually needed or expected to be needed) at prices that far exceed the total fixed costs of most existing units (oftentimes by many multiples)," the ISO cautioned.

Moreover, IEP's proposed pricing does not consider the existing surplus in the sub-markets of the RA program (i.e., the local area RA requirements), and in particular the local areas where there is a surplus of capacity, but ownership of units is concentrated.

"In these circumstances, IEP's and California Generators' proposals would only serve to substantially increase forward RA prices without incenting new entry," the ISO added.

Thus the proposals, "essentially become an insurance policy for resources that have failed to secure RA contracts and would unfairly and unreasonably burden ratepayers and should be rejected by the Commission," the ISO warned.

Calpine Protests "Administrative" Solution

However, Calpine, in a motion to lodge, sought to use CAISO comments in California PUC docket R.05-12-013 to press FERC on the need for transparent, competitively determined capacity prices.

The, "CAISO Comments disclaim that the ICPM represents a solution for backstop capacity procurement that would fit with an integrated, market-based approach to resource adequacy," Calpine claimed.

ICPM, Calpine complained, does not include a market-based pricing methodology but rather is an "administrative compensation mechanism untethered to competitive markets," which uses a pre-determined price.

During the interim period, capacity compensation will remain non-transparent and non-compensatory, Calpine asserted.

“In light of this reality, Calpine reiterates its proposal, set forth in its Protest, that the Commission affirm non-RA generators’ right, under Section 205 of the Federal Power Act, to elect out of the ICPM and to seek and receive compensation for capacity services under a cost-of-service-based mechanism.”

Calpine urged FERC to wait on ruling on ICPM until a scheduled May 15 final decision by the California PUC on the approach the PUC will take on resource adequacy. Given the Market Redesign and Technology Upgrade’s delay, waiting for the vote won’t cause problems, Calpine argued, and will allow FERC to follow the PUC’s course.

“California has reached the proverbial fork in the road,” Calpine explained.

“Either the CPUC decides to develop robust, centralized, auction-based forward capacity markets that can procure primary and backstop capacity at transparent, competitively determined prices, or the CPUC decides to rely on bifurcated capacity procurement through non-transparent RA bilateral contracts and arbitrary administrative designations by CAISO of backstop capacity. One path leads to competitive outcomes supporting both new and existing capacity, whereas the other path dead-ends with the present combination of unduly discriminatory and noncompensatory RA and non-RA mechanisms for capacity procurement,” Calpine wrote.

“For it is only after the CPUC decides whether to embrace the CAISO Comments’ recommendations for centralized, auction-based forward capacity market procurement of both primary and backstop capacity, that it can be determined how best to modify the ICPM to incorporate a transitional market-based pricing methodology for valuing backstop capacity in the interim period prior to implementation of California’s new capacity market structure,” Calpine asserted.