



PUBLIC UTILITIES COMMISSION

STATE OF CALIFORNIA  
505 VAN NESS AVENUE  
SAN FRANCISCO, CALIFORNIA 94102

MICHAEL R. PEEVEY  
PRESIDENT

TEL: (415) 703-3703  
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July 10, 2008

Senator Don Perata  
Senate President pro Tem  
State Capitol  
PO Box 942849  
Sacramento, CA 94249-0047

Assemblymember Karen Bass  
Assembly Speaker  
State Capitol  
PO Box 942849  
Sacramento, CA 94249-0047

Senator Darrell Steinberg  
Senate President pro Tem Elect  
State Capitol  
PO Box 942849  
Sacramento, CA 94249-0047

Assemblymember Fabian Nunez  
Assembly Speaker Emeritus  
State Capitol  
PO Box 942849  
Sacramento, CA 94249-0047

Senator Christine Kehoe, Chair  
Senate Energy, Utilities, and  
Communications Committee  
State Capitol  
PO Box 942849  
Sacramento, CA 94249-0047

Assemblymember Lloyd Levine, Chair  
Assembly Utilities and  
Commerce Committee  
State Capitol  
PO Box 942849  
Sacramento, CA 94249-0047

Dear Senators Perata, Steinberg and Kehoe, and Assemblymembers Bass, Nunez and Levine:

During my testimony before the Senate Energy Committee earlier this year I explained the premise and objectives of the Commission's current proceeding on direct access. Recent developments suggest, however, that there remain misconceptions about the PUC's activities in this area. For this reason, I am taking this opportunity to reiterate and amplify my previous remarks.

Stakeholders may debate the merits of restoring direct access, but it is indisputable that current law anticipates the eventual resumption of retail competition in California's electricity markets. Under the provisions of AB1X as codified in Water Code § 80110 the Legislature suspended direct access until the Department of Water Resources (DWR) "no longer supplies power."

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This day is approaching, and may arrive sooner than we expect. DWR's recent efforts to renegotiate and transfer responsibility for its wholesale energy contracts are consistent with the agency's stated interest in phasing out of the procurement role it assumed during 2001/02. Governor Schwarzenegger has supported and encouraged DWR's efforts, as do I. And, DWR currently has bond-related reserves of over \$1 billion that, in my view, should be provided as rate relief to California electricity consumers.

The majority of DWR contracts will expire over the next few years. As these contracts expire, DWR will be relieved from the responsibility to perform functions that should be performed by regular market participants, which as stated in D.02-12-069, is one of the CPUC's goals. Transitioning full responsibility for energy market-related activities back to the utilities as soon as possible is consistent with the fact that the utilities, and not DWR, continue to have the statutory responsibility to serve their customers.

We need to be prepared for an orderly return to retail competition at such time that the requirements for the reopening of direct access pursuant to current law have been satisfied. The focus of the CPUC's proceeding is to assess whether and under what conditions reinstating direct access could be beneficial to California electricity consumers. In particular, we will identify the necessary policies and procedures to avoid cost shifting, maintain system reliability, and ensure compliance with all environmental laws. We must have a level playing field, along these and all other relevant dimensions.

In response to the petition filed by direct access providers and customers --- that run the gamut from public universities and school districts to large retailers --- the Commission considered whether it could on its own authority reopen direct access. In D.08-02-033 we rejected the petitioners' legal arguments, concluding that only expiration or novation of the DWR contracts could end the current suspension. At present the Commission is examining the feasibility of novation and the terms and conditions associated with such a strategy. At the forefront of this discussion, as highlighted by the recent workshops, is weighing the potential benefits and costs to California's ratepayers.

The remaining phases of the proceeding, currently scheduled to conclude no sooner than mid-2009, will consider the public policy issues surrounding lifting the suspension of direct access and any and all applicable wholesale market structure issues, as well as development of the rules that should govern a reinstated direct access market. This would include, but not be limited to, entry, exit, switching, default service arrangements, and cost recovery issues and whether any resumption should be limited to the non-residential sector.

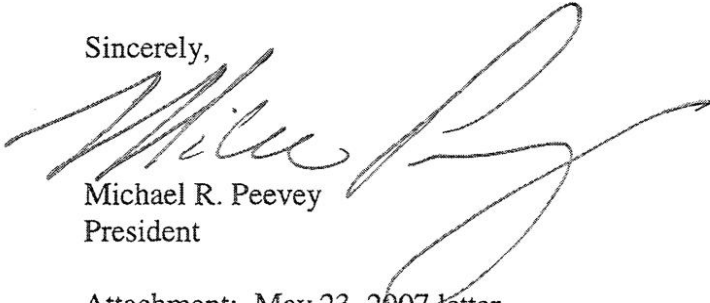
The Commission is moving at a very measured pace, carefully considering each set of issues in turn. At the conclusion of this proceeding the Commission will have established a blueprint for a competitive retail electricity market consistent with California's economic and environmental goals. This framework will provide a concrete basis for the legislative policy debates that will likely precede the actual termination of the suspension of direct access. And, of course, the Legislature can always repeal the direct access statute, if it so chooses.

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I hope this letter has addressed the issues raised in your May 23, 2007 letter and has allayed any lingering concerns you may have about the Commission's direct access proceeding. Please contact me if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Mike R. Peevey". The signature is fluid and cursive, with a large, sweeping flourish at the end.

Michael R. Peevey  
President

Attachment: May 23, 2007 letter

FVI

# California Legislature

RECEIVED

MAY 24 2007

May 23, 2007

Commissioner PEEVEY'S OFFICE

Commissioner Michael R. Peevey, President  
California Public Utilities Commission  
505 Van Ness Avenue  
San Francisco, California 94102

Dear President Peevey:

We are writing to request that you do not open a new rulemaking to consider the reopening of direct access while DWR continues to supply power to the customers of the major California Investor Owned Utilities (IOUs). This rulemaking contemplates actions which contravene existing statutes and are not within the discretion of the California Public Utilities Commission (CPUC). Specifically, your proposed decision suggests that Water Code §80110 could permit the CPUC to lift the direct access suspension as individual contracts executed by the California Department of Water Resources begin to expire.

Earlier this year, Commissioner Peevey provided the legislature with responses to questions submitted by the Senate Energy, Utilities, and Communications Committee. In those responses he noted that, consistent with the provisions of AB1X (Keeley, 2001),

It appears that the suspension of direct access could not be lifted until 2015, when the last power purchase contracts expire.<sup>1</sup> A consideration at this point, however, is whether the statute would permit the Commission to phase out the suspension of direct access as the DWR power purchase contracts expire, rather than wait until all the power contracts expire. In this respect, the Commission would appreciate any direction and guidance provided by the Legislature.

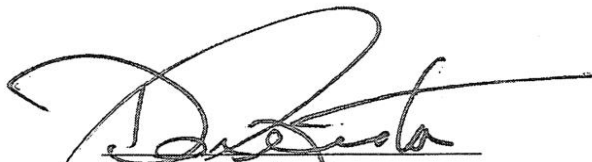
In this letter, we provide the guidance requested by the Commission. The prohibitions enacted in AB1X are not ambiguous. The CPUC is prohibited from removing the direct access suspension until DWR no longer serves as a supplier of any power to utilities and their customers. There is nothing in this language to suggest that the legislature intended to allow the suspension to be lifted as individual DWR contracts expire. When AB1X

<sup>1</sup> Commissioner Peevey noted that certain DWR contracts may extend until 2017, causing the direct access suspension to extend through that date.

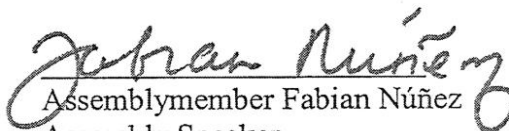
was enacted, the legislature could not have known the quantity or duration of the contracts that DWR would execute. Accordingly, the statute provides no indication that the length of the suspension could be linked to the duration of a subset of the DWR contracts. The suspension can only be lifted once DWR no longer supplies any power at all.

If stakeholders (including the Commission) favor a premature end to the direct access suspension, proposals must be brought to the Legislature for consideration. The Legislature spoke to your lack of authority to work independently in this area when both the Senate and Assembly budget subcommittees recently rejected the CPUC's request for funding to study electricity markets. As the Legislative Analyst noted in commenting on the CPUC's budget request, "it is premature and beyond the jurisdiction of CPUC to begin investigation and evaluation of a market design without further statutory direction from the Legislature." More generally, we believe that the reopening of direct access is a fundamental policy change that should be considered only by the Legislature. We look forward to considering the full ramifications of this change to determine if it is in the best interest of customers. In the meantime, we strongly urge you to reject this proposed rulemaking.

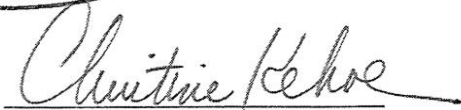
Sincerely,



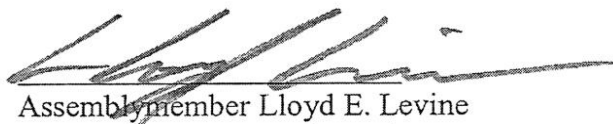
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