

**PUC DOCKET NO. 24888**

**PROCEEDING TO ADDRESS** § **PUBLIC UTILITY COMMISSION**  
**MARCH 2002 AND JULY 2002** §  
**CAPACITY AUCTIONS** § **OF TEXAS**

**ORDER**

This Order address issues regarding the implementation of the Capacity Auction Rule, P.U.C. SUBST. R. 25.381. For the reasons discussed in this Order, the Commission approves the *March and July 2002 ERCOT Capacity Auction EEI/NEMA Master Power Purchase & Sale Agreement* (including the cover sheet and the newly-created instruction sheet to accompany that cover sheet), *Schedule CA-ERCOT (March and July 2002 Version)* and *Exhibit CA* together with the three related good cause exceptions to the rule as described below in the findings of fact. Further, this Order approves the *Capacity Auction Mechanics Pursuant to 16 TAC § 25.381, March and July 2002 Version* together with the six related good cause exceptions to the rule as described below in the findings of fact.

**I. Background**

On October 18, 2001, the Commission established this proceeding to review the Capacity Auction EEI/NEMA Master Power Purchase & Sale Agreement, Schedule CA-ERCOT, Exhibit CA, and the Capacity Auction Mechanics that were approved in the Commission's final order in *Proceeding to Implement the Capacity Auction Rule*, Docket No. 23774 (September 6, 2001) and were used in the initial capacity auction held in September 2001. This proceeding was established to address the issues regarding the auctions to be conducted in March and July 2002. Commission Staff (Staff) and stakeholders, including buyers and sellers of capacity auction products, worked together to discuss improvements to the standard Capacity Auction contracts as well as the standard procedures, or mechanics, for conducting the capacity auctions. The parties were successful in addressing all of these issues by agreement.

The Non-Unanimous Stipulation and Agreement Regarding the March and July 2002 ERCOT Capacity Auction Contract and Joint Motion for Good Cause Exception (ERCOT Capacity Auction Contract Stipulation) was filed December 5, 2001. The Non-Unanimous Stipulation and Agreement Regarding March and July 2002 Capacity Auction Mechanics and

Joint Motion for Good Cause Exception (Capacity Auction Mechanics Stipulation) was also filed on December 5, 2001. No party opposed either stipulation.

Section 39.153 of the Public Utility Regulatory Act (PURA)<sup>1</sup> mandates that electric utility subject to customer choice auction entitlements to 15% of its installed capacity in Texas. P.U.C. SUBST. R. 25.381(f)(1)(A)(ii) requires the next two capacity auctions to be concluded on March 15, 2002 and July 15, 2002.

The Signatories to the ERCOT Capacity Auction Contract Stipulation recommended that the Commission approve the *March and July 2002 ERCOT Capacity Auction EEI/NEMA Master Power Purchase & Sale Agreement* (including the cover sheet and the newly-created instruction sheet to accompany that cover sheet), *Schedule CA-ERCOT (March and July 2002 Version)* and *Exhibit CA*. The Signatories requested the Commission grant three good cause exceptions to the rule as described below in the findings of fact.

The Signatories to the Capacity Auction Mechanics Stipulation also recommended that the Commission approve the *Capacity Auction Mechanics Pursuant to 16 TAC § 25.381, March and July 2002 Version*. The Signatories requested the Commission grant six good cause exceptions to the rule as described below in the findings of fact.

The Commission has reviewed both motions and the attached documents. The Commission determines that the motions are in the public interest and are consistent with PURA. The motions should be granted, the good cause exceptions approved, and the described documents should be adopted. The Commission adopts the following findings of fact and conclusions of law:

## II. Findings of Fact

### *Procedural History*

1. On December 1, 2000, the Commission adopted P.U.C. SUBST. R. 25.381 regulating the statutorily required 15% capacity auction and defining the products to be auctioned (capacity auction products).

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<sup>1</sup> TEX. UTIL. CODE ANN. §§ 11.001-64.158 (West 1998 & Supp. 2002).

2. The Commission found it appropriate, as discussed in the preamble<sup>2</sup> to P.U.C. SUBST. R. 25.381, to establish an implementation task force to examine what further provisions may be needed to ensure that capacity auction products are adequately used in ancillary services markets and to address ERCOT settlement issues.
3. On October 18, 2001, the Commission established this proceeding to review the Capacity Auction EEI/NEMA Master Power Purchase & Sale Agreement, Schedule CA-ERCOT, Exhibit CA, and the Capacity Auction Mechanics that were approved in the Commission's final order in *Proceeding to Implement the Capacity Auction Rule*, Docket No. 23774 (September 6, 2001) and were used in the initial capacity auction held in September 2001.
4. On November 12, 2001, a prehearing conference was convened to establish the procedural schedule and identify pending issues in this proceeding. That same day, the Administrative Law Judge (ALJ) issued Order No. 2, granting the Office of Public Utility Counsel (OPC's) motion to intervene and established a procedural schedule.
5. On November 19, 2001, the ALJ issued Order No. 3, granting intervention to TXU Electric Company (TXU), TXU Energy Trading Company (TXU-ETC), Entergy Gulf States, Inc. (EGSI), Coral Power, L.L.C. (Coral), American Electric Power Companies (AEP), Reliant Energy, Incorporated (REI) and Reliant Resources, Incorporated (RRI).
6. On November 29, 2001, the ALJ issued Order No. 4, granting intervention to Brownsville Public Utilities Board (PUB) and Brazos Electric Power Cooperative, Inc. (Brazos).
7. On December 5, 2001 Coral, REI, RRI, AEP, TXU-ETC and TXU filed the ERCOT Capacity Auction Contract Stipulation. The ERCOT Capacity Auction Contract Stipulation recites that the Lower Colorado River Authority<sup>3</sup> and OPC did not oppose the Stipulation.

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<sup>2</sup> *Capacity Auction*, Project No. 21405 (January 4, 2001); 25 Tex. Reg. 12961, 12967 (Dec. 29, 2000).

<sup>3</sup> The Lower Colorado River Authority has not intervened in this Docket.

8. On December 5, 2001, Coral, REI, RRI, AEP, TXU-ETC and TXU filed the Capacity Auction Mechanics Stipulation. The Capacity Auction Mechanics Stipulation recites that the Lower Colorado River Authority and OPC did not oppose the stipulation.
9. On December 5, 2001, Mirant Americas Energy Marketing, LP and Mirant Texas, LP filed a joint motion to intervene in this docket.
10. On December 6, 2001 a prehearing conference was held to address various procedural issues in this proceeding. No party requested a hearing at this prehearing conference. Also at this prehearing conference, EGSI and Staff announced that they did not oppose either the ERCOT Capacity Auction Contract Stipulation or the Capacity Auction Mechanics Stipulation.
11. On December 6, 2001, the ALJ issued Order No. 6, memorializing the prehearing conference and setting a procedural schedule. Pursuant to the procedural schedule, the settling parties were to file a joint Proposed Order by December 17, 2001. The ALJ set December 21, 2001 as the date by which the Proposed Order would be filed for the January 24, 2001 Open Meeting. Order No. 6 required Parties to file corrections and/or exceptions to the Proposed Order by January 11, 2002, with replies due January 17, 2002.
12. On December 13, 2001, the ALJ issued Order No. 6, granting intervention to Mirant Americas Energy Marketing, LP and Mirant Texas, LP.
13. The following documents are admitted into the evidentiary record: 1) the Non-Uniform Stipulation and Agreement Regarding the March and July 2002 ERCOT Capacity Auction Contract and Joint Motion for Good Cause Exception, with the attached Exhibit A that includes (a) the *March and July 2002 ERCOT Capacity Auction EEI/NEMA Master Power Purchase & Sale Agreement* (including the cover sheet and the newly-created instruction sheet to accompany that cover sheet), (b) *Schedule CA-ERCOT (March and July 2002 Version)* and *Exhibit CA*, filed on December 5, 2001; 2) the Non-Uniform Stipulation and Agreement Regarding March and July 2002 Capacity Auction Mechanics and Joint Motion for Good Cause Exception with the attached

Capacity Auction Mechanics Pursuant to 16 TAC § 25.381 (March and July 2002 Version) filed on December 5, 2001.

***ERCOT Capacity Auction Contract Stipulation***

14. The ERCOT Capacity Auction Contract Stipulation seeks approval of the *March and July 2002 ERCOT Capacity Auction EEL/NEMA Master Power Purchase & Sale Agreement* (including the cover sheet and the newly-created instruction sheet to accompany that cover sheet), *Schedule CA-ERCOT (March and July 2002 Version)* and *Exhibit CA*.
15. This Stipulation is the product of negotiation and compromise among potential buyers and sellers of capacity auction products within the ERCOT market.
16. The non-stipulating parties to this docket were afforded the opportunity to be heard on the merits of the ERCOT Capacity Auction Contract Stipulation.
17. No party to this docket objected to or opposed the ERCOT Capacity Auction Contract Stipulation.
18. P.U.C. SUBST. R. 25.381(e)(1)(F) and (j) allow the Commission to modify the procedures or products of the capacity auction upon a finding that such modifications are required to better value the products or better suit the needs of the competitive market.
19. *Schedule CA-ERCOT (March and July 2002 Version)* Section K.1(a)(iv)(B), allows for up to 3 MW of Ancillary Services to be provided from the Baseload product, in addition to the +/-10% (converted to 2 MW in *Schedule CA*) of energy change in the hour referenced in P.U.C. SUBST. R. 25.381(e)(5)(C)(i).
20. *Schedule CA-ERCOT (March and July 2002 Version)*, Section K.2(a)(iv)(E), allows for a total of 10 MW of ancillary services to be provided by the Gas-Intermediate product, which could cause the energy from this product to change more than the +/-25% (converted to 6 MW in *Schedule CA*) of energy change in the hour referenced in P.U.C. SUBST. R. 25.381(e)(5)(C)(ii).

21. *Schedule CA-ERCOT (March and July 2002 Version)*, Section K.2(a)(iv)(F), provides an option for the Buyer to stop the energy from the Gas-Intermediate product two times per month, subject to certain restrictions, which is different than the provisions of P.U.C. SUBST. R. 25.381(e)(1)(B)(i) imposing a minimum energy take on the Buyer seven days per week and 24 hours per day. If the buyer chooses to exercise its option to stop the energy from the Gas-Intermediate product, the fuel-pricing index used will change from monthly to daily.
22. The portions of *Schedule CA-ERCOT (March and July 2002 Version)* described in Findings of Fact 19 through 21 deviate from the provisions of P.U.C. SUBST. R. 25.381. These requested exceptions to the rule will enhance the value of capacity auction products and better suit the needs of the competitive market. They will benefit buyers by giving them additional flexibility to provide ancillary services, and will not cause any undue adverse effects on sellers. The Commission's Order in Docket No. 23774, *Proceeding to Implement the Capacity Auction Rule* (Sept. 6, 2001) granted the same good cause exceptions for the initial capacity auction.

#### ***Capacity Auction Mechanics Stipulation***

23. The Capacity Auction Mechanics Stipulation seeks approval of the *Capacity Auction Mechanics Pursuant to 16 TAC § 25.381, March and July 2002 Version* (March and July 2002 Mechanics).
24. The Capacity Auction Mechanics Stipulation is the product of negotiation and compromise among potential buyers and sellers of capacity auction products within the ERCOT market.
25. The non-stipulating parties to this docket were afforded the opportunity to be heard on the merits of the Capacity Auction Mechanics Stipulation.
26. No party to this docket objected to or opposed the Capacity Auction Mechanics Stipulation.

27. P.U.C. SUBST. R. 25.381 (e)(1)(F) and (j) allows the Commission to modify the procedures or products of the capacity auction upon a finding that such modifications are required to better value the products or better suit the needs of the competitive market.
28. *March and July 2002 Mechanics* provide that a Capacity Auction Seller apply the credit requirements of P.U.C. SUBST. R. 25.381(e)(5)(D)(i)(I) and (IV), so that the amount of credit available to a Bidder relying on its investment grade credit rating or its guarantor's investment grade credit rating will be determined according to specifically designed standards therein. Currently P.U.C. SUBST. R. 25.381(e)(5)(D)(i)(I) and (IV) does not specify a credit limit if the Bidder or the Bidder's guarantor has an investment grade credit rating. Requiring Capacity Auction Sellers to provide an unlimited amount of credit based only on a Bidder's investment grade credit rating is inconsistent with standard commercial practice in the wholesale market. By allowing Capacity Auction Sellers to apply the designated standards to instances of unsecured credit, Capacity Auction Sellers will be given the proper credit protection and consistency among credit standards will be promoted.
29. *March and July 2002 Mechanics* provide for the provision of unsecured credit to entities that are not publicly rated but that meet certain creditworthiness standards specified in the *March and July 2002 Mechanics*. P.U.C. SUBST. R 25.381(e)(5)(D)(i) does not require the issuance of unsecured credit to entities that are not publicly rated. Requiring unrated, but creditworthy, entities to receive unsecured credit will promote participation in the March and July 2002 Capacity Auctions without unduly increasing Capacity Auction Sellers' credit risks.
30. *March and July 2002 Mechanics* provide that a Bidder's credit limit during a Capacity Auction will be adjusted based on the amount of its bid plus the amount that would be paid to exercise the entitlement for the duration of the entitlement at the *assumed* dispatch for the entitlement specified in the March and July 2002 Mechanics. Currently, P.U.C. SUBST. R. 25.381(e)(5)(D)(i)(II)-(III) measures a Bidder's credit allowance by the sum of the bid amount plus the amount that would be paid to exercise the entitlement for the duration of the entitlement at the *minimum* dispatch required for that product. In

some cases, the minimum dispatch for a particular product contemplated in the Capacity Auction Rule will be less than the assumed dispatch specified in the March and July 2002 Mechanics. The *March and July 2002 Mechanics* provide for reasonable assumed dispatch levels that will give Capacity Auction Sellers more appropriate credit protection. In addition, this provision will bring the Capacity Auction credit requirements closer to the standard commercial practice in the wholesale market.

31. *March and July 2002 Mechanics* provide that in any round except the first round of the Capacity Auction, if the total demand for a set of entitlements is equal to the available quantity of entitlements, then the Capacity Auction will not close and will continue into the next round. This provision is contrary to P.U.C. SUBST. R. 25.381(f)(6)(A)(ii), which provides that the Auction will close if in any round the supply of entitlements is equal to (or less than) demand. The provision in the *March and July 2002 Mechanics* will increase the probability that full value is received for Capacity Auction products, creating true and proper market clearing prices for those products.
32. *March and July 2002 Mechanics* require that Sellers use the same opening bid as used in the September 2001 Capacity Auction, unless an exception is granted by the Commission, and specifies the *range* of bid increments that Capacity Auction Sellers are permitted to use to adjust the price of entitlements between rounds of the Capacity Auction. P.U.C. SUBST. R. 25.381(f)(2)(B)(i) and (ii), on the other hand, require each Capacity Auction Seller to specify in its 60 Day Capacity Auction Notice the opening bid price for the Seller's Capacity Auction products, based on a formula adopted by the Seller, and the formula that the Seller will use to adjust the price of entitlements between rounds of the Capacity Auction. The provisions in the *March and July 2002 Mechanics* will maintain uniformity and transparency in Capacity Auction pricing, and will also prevent gaming of the Capacity Auction through the back-calculation of product demand using a Capacity Auction Seller's published bid-increment formula.
33. *March and July 2002 Mechanics* provide that once a Capacity Auction begins it will continue through each business day until the Auction concludes. Currently, P.U.C. SUBST. R. 25.381(f)(1)(A)(ii) requires that the March 2002 Auction conclude by March

15, 2002, and requires that the July 2002 Auction conclude by July 15, 2002. Although it is not anticipated that the March and July 2002 Auctions would extend beyond these dates, considering that they will begin on March 4 and July 9 respectively, it is necessary to reserve the right to continue beyond these dates in order for the Auctions to reach their natural conclusions, thereby achieving the full and proper value for the Capacity Auction products.

34. The portions of *March and July 2002 Mechanics* described in Findings of Fact 28 through 33 deviate from the provisions of P.U.C. SUBST. R. 25.381. These requested exceptions to the rule will provide additional certainty to the procedures that are used to conduct the capacity auctions.
35. The terms of *March and July 2002 Mechanics*, as adopted in the Capacity Auction Mechanics Stipulation, are reasonable and should be approved.<sup>4</sup>

### III. Conclusions of Law

1. The Public Utility Commission of Texas has jurisdiction over the parties and the subject matter in this proceeding, and the authority to adopt the capacity auction implementation plan described herein, pursuant to PURA §§ 14.001, 32.001, and 39.153.
2. The provision of notice in this proceeding complies with P.U.C. PROC. R. 22.55.
3. This proceeding was processed in accordance with the requirements of PURA and the Administrative Procedure Act, TEX. GOV'T CODE ANN. §§ 2001.001-092 (Vernon 2000 & Supp. 2001)(APA).
4. This proceeding is properly resolved by informal disposition pursuant to P.U.C. PROC. R. 22.35 and APA § 2001.056.

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<sup>4</sup> Pursuant to Commission order in Docket No. 24469, *Public Utility Commission of Texas Staff Petition to Determine Readiness for Retail Competition in the Portions of Texas within the Southeastern Reliability Council*, EGSI is not currently required to participate in capacity auctions. Should EGSI subsequently be required or authorized to participate in a capacity auction governed by this order, then the Capacity Auction Mechanics as described in the *March and July 2002 Mechanics* shall likewise be applicable to EGSI's capacity auction. EGSI, however, is not subject to the provisions of this order addressing ERCOT Capacity Auction Contract Stipulation, as EGSI's capacity auctions will not be conducted within ERCOT.

5. Good cause exists to grant, pursuant to P.U.C. SUBST. R. 25.3 and P.U.C. SUBST. R. 25.381(e)(1)(F) and (j), the exceptions to P.U.C. SUBST. R 25.381 noted in the ERCOT Capacity Auction Contract Stipulation and the Capacity Auction Mechanics stipulation.

***ERCOT Capacity Auction Contract Stipulation***

6. The terms of the ERCOT Capacity Auction Contract Stipulation are fair, just and reasonable, and supported by the record.
7. The ERCOT Capacity Auction Contract Stipulation is consistent with the requirements of PURA § 39.153, P.U.C. SUBST. R. 25.381 and P.U.C. SUBST. R. 25.3.
8. Pursuant to P.U.C. SUBST. R. 25.381(e)(1)(F) and (j), the capacity auction products and procedures listed in P.U.C. SUBST. R. 25.381 require modification to better value the products and better suit the needs of the competitive market.

***Capacity Auction Mechanics Stipulation***

9. The terms of the Capacity Auction Mechanics Stipulation are fair, just and reasonable, and supported by the record.
10. The proposed capacity auction implementation plan set forth in the *March and July 2002 Mechanics* complies with PURA § 39.153, P.U.C. SUBST. R. 25.381 and P.U.C. SUBST. R. 25.3.
11. Pursuant to P.U.C. SUBST. R. 25.381 (e)(1)(F) and (j), the capacity auction products and procedures listed in P.U.C. SUBST. R. 25.381 require modification to better value the products and better suit the needs of the competitive market.

#### IV. Ordering Paragraphs

In accordance with the findings of fact and conclusions of law, the Commission issues the following Order:

1. The *March and July 2002 ERCOT Capacity Auction EEI/NEMA Master Power Purchase & Sale Agreement* (including the cover sheet and the newly-created instruction sheet to accompany that cover sheet), *Schedule CA-ERCOT (March and July 2002 Version)*, *Exhibit CA* and the *Capacity Auction Mechanics Pursuant to 16 TAC § 25.381, March and July 2002 Version*, consistent with their respective non-unanimous Stipulations, are approved. As to the July 2002 capacity auction, this approval is subject to any future rule that may establish different requirements or conditions for conducting capacity auctions.
2. Together, the *March and July 2002 Capacity Auction EEI/NEMA Master Power Purchase & Sale Agreement* (including the cover sheet and the newly-created instruction sheet to accompany that cover sheet), *Schedule CA-ERCOT (March and July 2002 Version)*, *Exhibit CA* and the *Capacity Auction Mechanics Pursuant to 16 TAC § 25.381, March and July 2002 Version* shall form the ERCOT contract governing the auction and use of capacity auction products in the statutorily required 15% capacity auctions.
3. Consistent with P.U.C. SUBST. R. 25.3 and P.U.C SUBST. R. 25.381 (e)(1)(F) and (j), the Commission grants the good cause exceptions as specifically stated in Finding of Fact Nos. 19 through 21 and 28 through 33.
4. The entry of an order consistent with the Non-unanimous Stipulations does not indicate the Commission's endorsement or approval of any principle or methodology that may underlie the Non-Unanimous Stipulations. The entry of an order consistent with the Non-Unanimous Stipulations should also not be regarded as a binding holding or precedent as the appropriateness of any principle or methodology underlying the Non-Unanimous Stipulations.

5. All motions or requests for entry of specific findings of fact and conclusions of law, and other requests for general or specific relief not expressly granted, are denied for want of merit.

**SIGNED AT AUSTIN, TEXAS the \_\_\_\_\_ day of \_\_\_\_\_ 2002.**

**PUBLIC UTILITY COMMISSION OF TEXAS**

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**BRETT A. PERLMAN, COMMISSIONER**

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**REBECCA KLEIN, COMMISSIONER**