



Yakout Mansour
President & Chief Executive Officer

June 2, 2008

Mayor Gavin Newsom
City Hall, Room 200
1 Dr. Carlton B. Goodlett Place
San Francisco, CA 94102

Dear Mayor Newsom:

Thank you for your attention to the electricity reliability needs of the City of San Francisco. As we have discussed, consistently reliable service is essential to the area's public health and welfare as well as San Francisco and the State's economy.

Below are the California Independent System Operator's (CAISO) responses to questions posed by your office related to the San Francisco Board of Supervisor's ongoing deliberations about how to meet the area's reliability needs.

- 1) *When Trans Bay Cable comes on line, will CAISO remove Reliability Must-Run (RMR) status from Potrero Unit 3 even if the Mirant retrofits are not in service?*

Yes. When Trans Bay Cable comes on line, the Mirant retrofits do not have to be in service in order for the CAISO to remove the RMR status from Potrero Unit 3. This is true even though the Mirant diesel units will have to be retrofitted one at a time, and work will have to be carefully phased.

- 2) *Will CAISO assess its designation of the peakers as RMR units on an annual basis?*

The CAISO designates RMR units in an annual process that takes into account infrastructure changes, data provided by the local utility, other available information, and the CAISO's own analysis. The designation requires approval by the CAISO Board of Governors in a publicly noticed meeting open to all interested parties.

- 3) *With regard to the 4th CT at the airport:*
 - a. *Is it still necessary?*

The San Francisco Action Plan approved by the CAISO Board of Governors in 2004 contained three peakers in the City and one peaker at the airport.

The in-City peakers were needed to meet San Francisco reliability requirements, and the peaker at the airport was needed to address San Mateo area reliability. With the addition of the Trans Bay Cable Project, however, only the in-City peakers continue to be required to comply with reliability requirements.

b. Does it matter whether the in-City generation is provided by the SF peakers or the Mirant retrofitted peakers?

It does not matter whether the in-City generation is provided by the SF peakers or the Mirant retrofitted peakers.

4) *Will the CAISO allow the cost of the Mirant peaker retrofits to be recovered through the RMR contract? Must PG&E and the California Public Utilities Commission (CPUC) agree?*

The cost of the proposed peaker retrofits would be eligible for recovery under the terms of an RMR contract. The CAISO routinely includes cost recovery for capital improvements in RMR contracts, including improvements needed for environmental compliance. In conducting its review of Mirant's retrofits, the CAISO will consult carefully with PG&E and the CPUC, as required by the RMR contract. For projects costing more than \$5 million, the contract also requires the consent of the responsible utility – in this case PG&E.

5) *What will the run hours be for the Mirant retrofitted peakers?*

From 2003 through 2007, the capacity factors for Potrero Units 4, 5 and 6 have ranged from 1 to 4 percent. This translates into a range of approximately 100 to 400 hours per year for each unit. We would expect the similar requirements in the future unless emergency conditions arise. In that case, the CAISO could call on the peakers to run many more hours than in past years.

Also, please keep in mind that the project owner has an annual choice regarding whether to operate under "Condition 1" or "Condition 2" of its RMR contract. In making its election, the plant owner selects whether to have an incentive to operate for more hours than those required by the California System Operator.

Condition 1 units are allowed to participate in the CAISO's markets and to engage in bilateral sales. As a result, the CAISO (and Responsible Utility – in this case PG&E) only pay a percentage of the units' fixed costs. The exact percentage is unique to each unit and RMR Contract. Condition 2 units, on the other hand, cannot participate in the market unless the CAISO has called on them through an RMR Dispatch. Condition 2 units recover 100% of their

fixed costs under the contract and cannot keep market revenues above the contract rate for energy.

I hope our answers will help you deal with the difficult choices facing San Francisco. Also, please know that similar issues exist elsewhere in the state. As California seeks additional renewable resources, considers new water quality regulations for coastal power plants, and limits greenhouse gas emissions, important reliability issues must also be addressed. It is necessary and possible to balance the urgent need to improve our environment with the need for reliable electricity service, as the steps taken to enable the closure of the Hunters Point power plant in 2006 illustrate.

The California ISO applauds your commitment to environmental goals and will continue to support the effort to achieve the closure of Potrero Unit 3 by providing impartial information and expertise to decision makers and the community.

Thank you for your leadership. If you have any questions, please do not hesitate to call.

Sincerely,

A handwritten signature in black ink, appearing to read "Y. Mansour", with a horizontal line extending to the right.

Yakout Mansour
President & Chief Executive Officer