

## MEMORANDUM

February 19, 2008

To: WSPP Contract Subcommittee  
From: Arnie Podgorsky  
Re: February 5, 2008 Meeting of the Subcommittee

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Thirty-four of you attended the above meeting (at Sempra in San Diego) (sign-in sheet copies available from counsel upon request). The Subcommittee received an update from EC Chair Jeff Atkinson about contingency reserves issues that have arisen in WECC and the related WSPP task force. The Subcommittee then addressed two damages issues arising under the Agreement (see memorandum preceding the meeting for additional background): (1) cuts among multiple transactions; and (2) cuts immediately before or during the hour. A brief discussion about the Agreement notice provision followed.

I will shortly notice a follow-up meeting. The WSPP Contingency Reserves Task Force will meet in San Diego on March 11. I will suggest that this Subcommittee meet on the 12<sup>th</sup> or 13<sup>th</sup>. Are there any industry conflicts on either date? And, do you have suggestions as to a location reasonably convenient to San Diego. (SF, LA, SD, LV, Santa Fe? Other?).

Following is a report about the meeting.

### I. Cuts Among Multiple Transactions

Counsel presented the following language (redlines against the January 22, 2008 pre-meeting memorandum, except redline to a. and b. was added at the meeting). Bracketed language is to facilitate discussion and would not be contract language.

The following language would be added as a new ~~incorporated within~~ 21.3(a)(5).

***[Cmt: First, define the multiple confirmations]***

In the event two Parties (i) entered into multiple Confirmations with each other as to which the same Party is the Purchaser and the other Party is the Seller, (ii), two or more of such Confirmations apply, in whole or in part, to the same date and hour (such Confirmations, the Multiple Confirmations),

***[Cmt: Second, define the problem- non-performed transactions are not obviously matched to respective multiple confirmations]***

(iii) transactions were non-performed under more than one but not all Multiple Confirmations, and (iv) each of the non-performed transactions cannot reasonably be identified to respective ~~a~~ Multiple Confirmations s (identification to occur, for

example, on the basis of product type, delivery points, quantities, or other indicia),

***[Cmt: Third, state methodology to match the non-performed transactions to respective non-identified, non-performed multiple confirmations in order to determine Contract Price and Contract Quantity]***

then, for purposes of identifying each such non-identified Multiple Confirmation that was not performed and, consequently, determining the Contract Price and Contract Quantity for the calculation of damages under this Section 21.3(a), ~~thereof,~~ each non-performed transaction shall be identified to ~~each~~ a non-identified Multiple Confirmation as follows.

- a. The Performing Party shall first match any and all non-performed real-time (same day up to and including the hour of non-performance) transactions to real-time Multiple Confirmations that include such day and hour(s);
- b. The Performing Party shall then match any and all non-performed next-day transactions to remaining next-day Multiple Confirmations that include such day.
- c. The Performing Party shall then match any remaining non-performed transactions to remaining Multiple Confirmations.

Following extended discussion, the Subcommittee strongly favored the concept (unanimous or nearly so), but concluded that the contract language should be modified to achieve the following:

1. The purpose of identifying cuts is relevant not just to calculating damages, but also to identifying which transactions might be excused by force majeure.
2. Clarify that the section applies only to those transactions that cannot otherwise be identified. This is a drafting matter, reflecting no change in substantive intent.
3. Once transactions capable of identification are identified (and removed from application of the section), then: (a) categorize unidentified transactions into the buckets (real-time, next-day, long-term), and seek to reach agreement on identification within each bucket, and then, (b) as to remaining unidentified transactions, if any, utilize the sequence provided for in above language.
4. Assure that all unidentified megawatts are covered.

## II. Measuring Damages for Cuts In or Close to Hour

Counsel set out the following language, redlined against the January 22, 2008 pre-meeting memorandum.

Definition addition (change to existing language in redline): No need for the definition changes to the 21.3 lead in (see January 22 memorandum).

~~Additional language for 21.3(a) (placement to be determined)~~ Following would be a new Section 21.3(e) [possibly (d) and make existing (d) an (e)]:

In the event (~~ia~~) a Purchaser terminates receipt or a Seller terminates delivery, of Energy, during an hour of performance required in a Confirmation, or (~~iib~~) the Purchaser is informed that the Seller will not deliver, or a Seller is informed that the Purchaser will not receive, Energy, within [~~xx-~~] minutes prior to the hour of performance required in a Confirmation, and, in the case of either (~~ia~~) or (~~iib~~), the Non-Performing Party, despite performance of mitigation duties under Section 21.3(c), did not enter into a transaction to obtain replacement Energy or resell the Energy, as applicable, then, for purposes of the damages calculation under Section 21.3(a), the Replacement Price or Resale Price, as applicable, shall be determined as follows.

First, the Performing Party shall determine the Replacement Price or Resale Price, as applicable, in a commercially reasonable manner, and give notice of such determination ~~{definition of Notice is needed for the Agreement}~~ to the Non-Performing Party, which notice shall set out the basis for the determination and factual support therefor.

Second, if the Non-Performing Party concludes that the proffered price is not commercially reasonable, the Non-Performing Party shall have five (5) Business Days to reject the Performing Party's determination given by the ~~N~~notice. If the Non-Performing Party rejects the Performing Party's determination, then the Parties shall in good faith consider as the Replacement Price or Resale Price, as applicable, the price stated in the Day Ahead Index ~~daily index~~ of transactions on the Intercontinental

Exchange, Inc. (ICE) for the applicable day, less (if the Performing Party is the Buyer) ten percent (10%) of such price, or plus (if the Performing Party is the Seller) ten percent (10%) of such price, and it is agreed that such ten percent (10%) adjustment reasonably accounts for the difference between the Day Ahead Index price and the actual loss incurred due to the timing of the non-performance hereunder.

Third, if the Parties do not agree to use the ICE Day Ahead Index with such ten percent (10%) adjustment, then each Party shall obtain, from two brokers, two quotations for the price of the applicable quantity, date and hour. [Cmt. Not taking into account the short time] The highest and lowest quotations shall be discarded. If the Performing Party is the Buyer, the average of the remaining quotations less twelve percent (12%) of such average price shall be the Replacement Price. If the Performing Party is the Seller, the average of the remaining quotations plus twelve percent (12%) of such average price shall be the Resale Price, and it is agreed that such twelve percent (12%) adjustment reasonably accounts for the difference between the Day Ahead Index price and the actual loss incurred due to the timing of the non-performance hereunder together with the added administrated burden of obtaining the quotations.

Fourth, at any time until all the required brokers' quotations are obtained, the Non-Performing Party may elect to use the Performing Party's determination provided under the First step.

Following considerable discussion there was minimal support for the above approach. Discussion focused on the practical concern that some parties had a number of these situations (disputes) awaiting resolution, and that the problem was not so much lack of a calculation methodology as the lack of an effective dispute resolution procedure under the Agreement.

Discussion about the WSPP mediation function brought out that members are hesitant to use persons on the mediation panel who represent entities with which they have frequent

dealings. Counsel noted that WSPP could devise a panel of independent mediators. Counsel also suggested that members consider a special arbitration provision (arbitration is binding; mediation is not) to resolve these particular disputes. One participant pointed out that arbitration effectively waives some important legal procedures, including appeal rights, and other procedural rights a party would have in court. Counsel responded that there could be arbitration of claims up to an agreed amount, above which the parties could opt for either arbitration or court. (Few if any of these kinds of claims appear to be in court, thus far.) No approach was settled upon and it was understood that approaches would be presented at the next meeting of the Subcommittee. I would appreciate some further input, ahead of the next meeting, about whether you wish to go down this road.

With respect to the contract language itself, it was suggested that the language possibly could be more acceptable if factors that determine commercial reasonableness were specified.

There was discussion that in chains (very common), the source and sink parties were determining the resolution and then seeking to impose it on the mid-parties. Unfortunately, there is no way to address this problem except for parties to stand on their specific transactions, that is, their own transactions with their own counter-parties, and not concede authority to others who, although in a chain, are contractually outside the transaction.

The discussion concerning chains also comprised a brief discussion about notice. A concern was expressed that parties mid-way in the chain need to be informed of how the source and sink are purporting to resolve non-performance. Counsel explained that because chains may, and often will, involve non-WSPP transactions, it is infeasible to regulate how they act. Again, parties need to emphasize that their duties and rights are with their legal counter-parties.

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Thanks again to Sempra for its generous hospitality in San Diego!

A.B.P.