

SWIDLER BERLIN SHEREFF FRIEDMAN, LLP

THE WASHINGTON HARBOUR
3000 K STREET, NW, SUITE 300
WASHINGTON, DC 20007-5116
TELEPHONE (202) 424-7500
FAX (202) 424-7643
WWW.SWIDLAW.COM

NEW YORK OFFICE
THE CHRYSLER BUILDING
405 LEXINGTON AVENUE
NEW YORK, NY 10174
(212) 973-0111 FAX (212) 891-9598

July 22, 2003

The Honorable Magalie R. Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

**Re: California Independent System Operator Corporation
Docket No. ER03-____-000
Amendment No. 55 to the CAISO Tariff**

Dear Secretary Salas:

Pursuant to Section 205 of the Federal Power Act ("FPA"), 16 U.S.C. § 824d, and Section 35.13 of the regulations of the Federal Energy Regulatory Commission ("Commission"), 18 C.F.R. § 35.13, the California Independent System Operator Corporation ("CAISO" or "ISO")¹ respectfully submits for filing an original and six copies of an amendment ("Amendment No. 55") to the ISO Tariff. Amendment No. 55 would modify the ISO Tariff in several respects to provide the CAISO with a necessary and effective Oversight and Investigation ("O & I") Program. Two additional copies of this filing are enclosed to be date-stamped and returned to our messenger. The CAISO requests that the Commission make the proposed Tariff changes effective September 20, 2003.

¹ Capitalized terms not otherwise defined herein are defined in the Master Definitions Supplement, Appendix A to the ISO Tariff, as filed August 15, 1997, and subsequently revised.

I. INTRODUCTION

The O & I Program proposed by the CAISO builds upon the CAISO's efforts since start-up to monitor its markets and report the exercise of market power, and is the result of a process the CAISO initiated with its "Oversight and Investigations Activities Review" that was announced by market notice issued on June 14, 2002. The CAISO initiated this Oversight and Investigations Activities Review to provide a forum for the evaluation of the CAISO's authority, responsibilities, and activities in the area of market monitoring, investigation, and enforcement. The O & I Tariff changes proposed herein are designed to enhance market operations and grid reliability, reduce opportunities for gaming, more actively coordinate market investigations with oversight and law enforcement agencies, and increase economic efficiency in the ISO Market. Throughout the process that has led to the Tariff changes proposed herein, Market Participants were provided with extensive opportunities for comment on the various elements of the O & I proposal. These comments were solicited and provided in the course of conference calls and meetings with Market Participants, discussion at Market Issues Forums, and in response to CAISO requests for written responses to its conceptual proposals and draft Tariff language. The chronology of the development and approval of the O & I proposal, including stakeholder involvement, is set forth in Attachment E hereto.

The CAISO believes that several coordinated strategies are necessary to assure Market Participants that prompt action will be taken and effective sanctions will be promptly imposed when the CAISO identifies instances of gaming, market manipulation, and/or non-compliance with ISO Tariff obligations. The CAISO's O & I proposal for new authority is comprised of the following key features:

- (1) a reformation of existing Tariff prohibitions into several defined rules of conduct based largely on the "minimum behavioral rules" specified by the Commission in its Notice of Proposed Rulemaking on Standard Market Design issued in Docket No. RM01-12 ("SMD NOPR");
- (2) pre-defined penalties for breach of these rules of conduct, which penalties the CAISO would have authority to impose directly (in addition to referral to the Commission);
- (3) procedures for routine sharing of market data and other information with certain state and federal oversight and enforcement "partner" agencies;
- (4) procedures for measuring and publicizing Market Participant performance against rules of conduct; and

- (5) programs for regular interaction and cross-training among CAISO representatives and representatives from the partner agencies.

A number of the program features require no action by the Commission and, indeed, some already have been implemented. For example, the CAISO has developed four measures by which to evaluate Market Participant performance, and began phasing in those measures and publishing the results under the ISO Home Page in November 2002 under its Information Release Program. The bulk of the ISO's proposal, however, including most particularly direct authority for the ISO to impose penalties, and changes to existing confidentiality provisions to allow for information sharing with the partner agencies, require amendments to the ISO Tariff. Accordingly, the CAISO seeks approval from the Commission for these changes through Amendment No. 55 to the ISO Tariff. A summary of key O & I Program elements and areas in which the CAISO seeks Commission action are set forth in Table 1.

Table 1		
Summary of CAISO Oversight and Investigation Proposal		
Key Features	Description	Action Requested From FERC
Enforcement Protocol - General Rules of Conduct	Seven general rules of conduct that serve as guiding principles as to the standards of behavior that are expected from Market Participants, with specific penalties for violation of these rules.	Approval of New "Enforcement Protocol," specifically Sections 2.2 through 2.8
Enforcement Protocol – Rules of Conduct on Detrimental Practices and Market Manipulation	Two rules of conduct that prohibit taking unfair advantage of the CAISO's rules and procedures and manipulative behavior, along with specific penalties for violation of these provisions.	Approval of new "Enforcement Protocol," specifically Sections 2.9 and 2.10
Enforcement Protocol – Sanctions	Pre-determined penalties for violations of above rules and authority for the CAISO to implement penalties directly (as contrasted to referral to FERC).	Approval of new "Enforcement Protocol"

Modification of ISO Tariff	Five changes to the existing ISO Tariff (and related protocols) in order to provide for additional remedies targeted to particular trading strategies.	<ul style="list-style-type: none"> ▪ Changes to Sections 2.3.1.2.1, 2.5.21 and 7.3.1.5.2 of the Tariff ▪ Addition of Section 2.2.9 to the Tariff ▪ Addition of Section 7.3.1.5.3 to the Tariff and addition of Section 2.1.7 to the Schedules and Bids Protocol
"Partner" agency coordination	A "regulatory server" and other means for frequent communication and coordination with designated state and federal law enforcement and oversight agencies.	Addition of Section 20.3.5 to the Tariff, relating to confidentiality of market data
Modification of MMIP	Revisions to current Market Monitoring & Information Protocols (MMIP).	Approval of changes to the existing MMIP
Publication	Metrics to evaluate and publicize the performance of Market Participants in relation to their Tariff obligations.	None
Orientation & Training	Programs for cross-training of CAISO staff and staffs of partner agencies on laws and regulations, rules and enforcement activities of the CAISO and partner agencies.	None

As detailed further in the sections that follow, the features of the O & I Program for which the CAISO seeks Commission approval, and which are a necessary condition to implementing the Program fully, are amply supported by the record of the California electricity crisis and the resulting investigations, and are demonstrably just and reasonable. Chairman Wood has noted on several occasions that a rigorous and fair enforcement regime, of the type proposed here by the CAISO, is an important and necessary corollary to efficient market design. Moreover, the centerpieces of the Program – the rules of conduct and pre-determined penalties for their breach – are based on rules proposed by the Commission in its own SMD NOPR, and on provisions implemented by other ISOs in the United States that have been approved by the Commission. The proposed rules on gaming and market manipulation parallel authority granted by the Commission in the context of the gas industry under closely analogous

circumstances. The proposed changes to existing confidentiality requirements continue to offer Market Participants important protections while allowing the CAISO to leverage more effectively the expertise and resources of other authorities responsible for safeguarding the public's interest in just and reasonable market outcomes.

The remainder of this Transmittal Letter is organized as follows.² Section II provides the context and justification for the actions requested herein, describing the electricity crisis in California, the results of recent investigations, which have revealed the extent of gaming and manipulation of market rules, and the reasons why current CAISO and Commission mechanisms are insufficient to address these problems going forward. Section III provides a detailed overview of the O & I Program, the process by which it was vetted by stakeholders, and actions required by the Commission. Section IV reviews key provisions of a proposed new Enforcement Protocol, the primary vehicle through which the O & I Program will be implemented. Section V reviews five additional conduct rules that the CAISO proposes to include within the main body of the ISO Tariff and protocols, because of their close relation to certain existing market operations rules. Section VI reviews proposed changes to the Tariff's confidentiality provisions (Section 20.3) in order to allow for information sharing with partner agencies. Section VII describes several revisions to the current set of Market Monitoring and Information Protocols. The remaining sections (VIII through XI) round out the information required under Commission rules for transmittal letters (Effective Date, Communications, Service, and Supporting Documents).

II. NEED FOR THE O & I PROGRAM

A. The California Electricity Crisis and Initial Commission Response

Many of the details of the California electricity crisis and its ruinous impact on the markets have been well chronicled. Beginning (at the latest) in the Spring of 2000 California was rocked by a number of events that left the electric energy sector in disarray and shattered the confidence of both consumers and State policy makers in California's energy markets. Wholesale electricity prices skyrocketed wreaking financial havoc on the electricity sector. In total, California experienced a \$40 billion run-up in electricity prices in 2000 and 2001. As a result two major utilities were pushed to the brink of insolvency, and one of them – Pacific Gas and Electric Company – filed for bankruptcy. The California Power Exchange Corporation ("PX"), the primary instrument of a competitive market, was forced into bankruptcy and dismantled. Faced with the inability of the two

² A detailed Table of Contents for this Transmittal Letter is provided as Attachment A to the present filing.

major utilities to purchase sufficient power to serve their native loads, the State of California, through the Department of Water Resources, was forced to step in and purchase power on their behalf. Further, during this time period, California faced a significant number of rolling blackouts due to a lack of available generation.

The Commission first took market-wide action in response to this crisis near the end of 2000. In a series of orders issued from late 2000 through the middle of 2001, the Commission, based on a finding that prices in California's wholesale electric market were unjust and unreasonable, imposed market mitigation measures and conditioned suppliers' market-based rate authority. See, e.g., *San Diego Gas & Electric Co., et al.*, 93 FERC ¶ 61,294 at 61,998 (2000); 95 FERC ¶ 61,115 at 61,351, 61,360 (2000); 95 FERC ¶ 61,418 at 62,549, 62,565 (2001); 97 FERC ¶ 61,275 at 62,218 (2001).

On July 25, 2001, the Commission issued an order in which it found that, because prices charged for electricity in California during the period under investigation (October 2000 through June 2001) had been unjust and unreasonable, that suppliers should pay refunds equal to the amount above the just and reasonable price for each hour. *San Diego Gas & Electric Co., et al.*, 96 FERC ¶ 61,120 (2001). The issue of the total amount of refunds actually due was set for hearing, at the conclusion of which the presiding Administrative Law Judge ("ALJ") found that suppliers owed refunds in the amount of \$1.8 billion for the period in question. See *San Diego Gas & Electric Co., et al.*, 101 FERC ¶ 63,026 at PP 7-8 (2002). The Commission largely affirmed the ALJ's initial decision and increased the level of potential refunds in order to account for price manipulation in California's natural gas markets. *San Diego Gas and Electric Co., et al.*, 102 FERC ¶ 61,317 (2003).

B. Documentation of Gaming and Market Manipulation

The actions taken by the Commission in reaction to the California energy crisis, as discussed above, focused on modifying the overall design of the California electricity markets and imposing refunds based on a market-wide finding of unjust and unreasonable prices, rather than investigating and imposing sanctions against individual entities for gaming, market manipulation, physical withholding, fraud, and the exercise of market power.³ Subsequent to the central events of the California electricity crisis, however, *prima facie* evidence of gaming, market manipulation, physical withholding, fraud, and the exercise of market power has come to light.

³ Report of the California State Auditor, "Energy Deregulation: The Benefits of Competition Were Undermined by Structural Flaws in the Market, Unsuccessful Oversight, and Uncontrollable Competitive Forces," (March 2001) p.2.

The CAISO was among the first to detect and report these types of behavior. For instance, in the year 2000, the CAISO prepared several analyses in which it documented the existence and exercise of market power, especially during periods of peak demand.⁴ See, e.g., Price Cap Policy for Summer 2000, filed in Docket No. EL00-97-000 (March 2000). Subsequently, from 2001 through the middle of 2002, the CAISO submitted a series of reports to the Commission demonstrating both the exercise of market power by individual sellers of electricity and anticompetitive bidding behavior.⁵

In response to the mounting evidence of anticompetitive behavior in the California electricity market, the Commission, on February 13, 2002, initiated a Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Prices in the Western U.S., 98 FERC ¶ 61,165 (2002) ("February 13 Order"), in order to gather information on whether any entity manipulated short-term prices for energy or natural gas in the West, or otherwise exercised undue influence over wholesale prices in the West. Accordingly, the Commission directed its Staff to undertake a fact-finding investigation to determine whether any entity had manipulated short-term prices for electricity or natural gas since January 1, 2000.

In connection with this investigation, on May 6, 2002, the Commission made public three memoranda detailing numerous Enron gaming strategies which evidenced an intent by sellers to manipulate California's electricity markets in order to increase prices above competitive levels and "game" market in California to the detriment of other Market Participants.⁶ The Enron Memos also expressly stated that other market participants had employed some of the same

⁴ The CAISO was not alone in concluding that market power had been a significant factor contributing to the high prices of electricity in the California market. For instance, the General Accounting Office, in a June 2002 report titled "*Restructured Electricity Markets-California Market Design Enabled Exercise of Market Power*" ("GAO Report"), found "evidence that wholesale electricity suppliers exercised market power by raising prices above competitive levels during the summer of 2000 and at other times after restructuring." GAO Report at 4; see also *id.* at 11-17.

⁵ See First Quarterly Update of the California Independent System Operator Corporation, Docket Nos. EL00-95-000, *et al.* (September 14, 2001); Second Quarterly Update of the California Independent System Operator Corporation, Docket Nos. EL00-95-000, *et al.* (December 14, 2001); Third Quarterly Update of the California Independent System Operator Corporation, Docket Nos. EL00-95-000, *et al.* (March 26, 2002); Fourth Quarterly Update of the California Independent System Operator Corporation, Docket Nos. EL00-95-000, *et al.* (June 14, 2002).

⁶ The Commission released the following memoranda: (1) a December 6, 2000 memorandum from Christian Yoder (of Enron Power Marketing, Inc.) and Stephen Hall (of Stoel Rives, LLP) to Richard Sanders (of Enron) entitled "Traders' Strategies in the California Wholesale Markets/ISO Sanctions"; (2) a December 8, 2000 memorandum from Christian Yoder and Stephen Hall to Richard Sanders also entitled "Traders' Strategies in the California Wholesale Markets/ISO Sanctions"; and (3) an undated memorandum from Gary Fergus (of Brobeck, Phleger & Harrison, LLP) and Jean Frizzell (of Gibbs & Brans, LLP) to Rich Sanders entitled "Status Report on Further Investigation and Analysis of EPMI Trading Strategies," (referred to collectively as the "Enron Memos").

strategies identified in the Enron Memos, e.g., “inc-ing load” and “relieving congestion.” Both the December 6 and the December 8, 2000 Enron Memos discussed the provisions of the MMIP proscribing gaming and anomalous market behavior and the possibility of sanctions under the MMIP. Accordingly, the memos contemplated the linkage between the strategies described therein and the possible consequences under the MMIP should the CAISO discover that the strategies had been employed.

In response to the Enron Memos, on May 8, 2002, the Commission issued data requests to all sellers of wholesale electricity and Ancillary Services to the CAISO and PX concerning their involvement in the gaming and/or market manipulation activities identified in the Enron Memos. On May 21, 2002, the Commission expanded the scope of the investigation by serving data requests on all sellers of wholesale electricity and Ancillary Services in the U.S. portion of the Western Systems Coordinating Council (“WSCC”) during 2000-2001 regarding their participation in “wash,” “round trip,” or “sell/buyback” trading.⁷ The Commission indicated that it was requesting the information because of inconsistent financial transaction data previously submitted by some companies as part of the Commission’s investigation.⁸

Based on the Enron Memos, the CAISO also undertook its own investigation into the trading and scheduling practices described therein, and on October 4, 2002, released its “*Analysis of Trading and Scheduling Strategies Described in Enron Memos*” (“October 4 Report”). The October 4 Report shows that the Enron gaming strategies were prevalent in the California market and were employed extensively by entities other than Enron. In particular, the October 4 Report discusses the potential market impact of three specific behaviors that the CAISO is seeking to address as part of the instant filing: scheduling on zero-rated transmission paths; cutting counter-flow Schedules; and buying back Ancillary Services at a lower Hour-Ahead price (i.e., the “Get Shorty” strategy).⁹ The CAISO later prepared and submitted to the Commission

⁷ At least one major California supplier – Reliant – admitted to phony “wash” trades. See Dennis K. Berman, Julia Angwin, and Chip Cummins, *Tricks of the Trade: As Market Bubble Nears End, Bogus Swaps Provided a Lift*, WALL ST. J., Dec. 23, 2002, at A1.

⁸ Moreover, as a result of the disclosure of the Enron Memos, the U.S. chief energy trader in the West for Enron, Timothy N. Belden, plead guilty to charges of conspiring to manipulate electricity prices. In his plea agreement, Mr. Belden stated that he and other Enron employees undertook schemes that involved providing false information to the CAISO and PX, which allowed Enron to manipulate prices in various markets and receive prices above the price caps set for the CAISO by the Commission. See Rebecca Smith and John R. Wilke, *Enron Ex-Trader Admits to Fraud In California Crisis*, WALL ST. J., Oct. 18, 2002, at A3.

⁹ These specific behaviors are discussed in greater detail in Section V, *infra*. For the years 1999-2002, revenues from the scheduling of counter-flows on out-of-service tie points totaled as much as \$6.5 million. October 4 Report at 26. For the period January 2000 through June 2002, total congestion revenues paid for counter-flow Schedules not cut by the CAISO are estimated to be as much as \$2.7 million. *Id.* at 33. With respect to the “Get Shorty” strategy, the October 4

a supplement to the October 4 Report, containing additional analysis of the various trading and scheduling strategies outlined in the Enron Memos and addressed in the October 4 Report. Supplemental Analysis of Trading and Scheduling Strategies Described in Enron Memos (June 2003).

On August 13, 2002, the Commission Staff issued its initial report pursuant to the direction provided by the Commission in the February 13 Order. *Initial Report On Company-Specific Separate Proceedings and Generic Reevaluations; Published Natural Gas Price Data; and Enron Trading Strategies*, Docket No. PA02-2-000 (Aug. 2002) ("Initial Report"). The Staff concluded that "[m]any of the Enron strategies may have been attempts to manipulate market prices" and "Enron trading strategies may have involved deceit, including the submission of false information, including false schedules." *Id.* Staff also recognized that "[t]here were no shortages of market participants from all sectors of the industry . . . who may have engaged in [the Enron] trading strategies and trading strategies of their own." *Id.* at 78. Staff recommended that the Commission require that all market-based rate tariffs include a specific prohibition against the deliberate submission of false information – or the omission of material information – to independent system operators (among other entities). *Id.* at 5. Finally, Staff recommended that the Commission initiate company-specific separate proceedings against three Enron affiliates, as well as El Paso Electric Company and Avista Corporation, in order to investigate possible violation of their own codes of conduct and the Commission's standards of conduct. *Id.* In response to Staff's Initial Report, on August 13, 2002, the Commission launched formal investigations and hearings concerning the three Enron affiliates, El Paso Electric, and Avista in Docket Nos. EL02-113-000, EL02-114-000, and EL02-115-000.

In December 2002, in the refund proceeding concerning the California markets (Docket Nos. EL00-95-045 *et al.*), the Commission re-opened the record to allow for the discovery and submission of information concerning manipulation in the California electricity market for the period January 2000 through June 2001. On March 3, 2003, the California Parties, comprised of Southern California Edison, Pacific Gas and Electric Company, the California Attorney General, the California Public Utilities Commission and the Electricity Oversight Board, in Docket Numbers EL00-95-000 *et al.* and EL00-98-000 *et al.*, filed over 160 pages of evidence with this Commission citing specific acts of alleged market manipulation and gaming on the part of generators and marketers in the California electricity market.

On March 26, 2003, the Commission Staff issued its final report building on the findings in the Initial Report. See *Final Report on Price Manipulation in*

Western Markets; Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Prices, Docket No. PA02-2-000 (Mar. 2003) (“Final Report”). The Staff stated that its yearlong investigation revealed “significant market manipulation” in the California and Western energy markets during 2000 and 2001. Final Report at ES-1. The Final Report found evidence of various types of market manipulation including economic withholding, raising market clearing prices through inflated bidding, wash trading, and gaming in violation of the MMIP. See *id.* at ES-2, ES-10.¹⁰ Staff also concluded that the MMIP prohibited these types of behavior, and “authorized the imposition of sanctions and penalties by the Commission.” *Id.* at ES-15. Therefore, Staff recommended that the Commission direct more than 30 Market Participants “to show cause why their behavior did not constitute gaming in violation of the Cal ISO and Cal PX tariffs.” *Id.* at ES-16. The Staff further recommended that the Commission direct that nine Market Participants “show cause why their prices from May to October 2000 did not constitute economic withholding or inflated bidding in violation of the antigaming and anomalous market behavior provisions in the Cal ISO and Cal PX tariffs.” *Id.*; see also *id.* at VI-45 to VI-53. Further still, the Staff recommended that the Commission “[i]ssue an order to Enron and the entities with whom it jointly engaged in the Enron trading strategies (both public utilities and governmental entities) to show cause why this did not constitute gaming in violation of the Cal ISO and Cal PX tariffs.” *Id.* at ES-16.¹¹

On June 25, 2003, the Commission issued a number of orders that addressed occurrences and apparent occurrences of improper behavior in the Western electricity markets. First, there was the “Order to Show Cause Concerning Gaming and/or Anomalous Market Behavior,” 103 FERC ¶ 61,345 (“Show Cause Order”). In the Show Cause Order, the Commission determined that over 40 entities identified by the Commission “appear to have participated in activities (Gaming Practices) that constitute gaming and/or anomalous market behavior in violation of” the ISO Tariff (and the PX’s tariff), during the period from January 1, 2000 to June 20, 2001. *Id.* at P 1. The Commission determined that participation in such activities could warrant a monetary remedy of disgorgement

¹⁰ The Commission Staff also noted that the Commission was addressing separately the issue of potential physical withholding. Various entities have submitted evidence to the Commission regarding alleged incidents of physical withholding by various Market Participants in the California markets. See Final Report at ES-2, VI-54 to VI-55.

¹¹ On the same day, pursuant to recommendations in the Final Report, the Commission issued an order directing Enron to show cause to the Commission why its authority to sell power at market-based rates should not be revoked by the Commission in light of its apparent engagement in gaming. *Enron Power Marketing, Inc. and Enron Energy Services, Inc., et al.*, 102 FERC ¶ 61,316 (2003). See Final Report at ES-16. The Commission also issued an order directing Reliant Energy Services, Inc. and BP Energy Company to show cause why their authority to sell power at market-based rates should not be revoked by the Commission in light of their apparent manipulation of energy prices at the Palo Verde, Arizona trading hub. *Reliant Energy Services, Inc. and BP Energy Company*, 102 FERC ¶ 61,315 (2003). See Final Report at ES-17.

of unjust profits and other additional, appropriate non-monetary remedies. *Id.* The Commission instituted public hearings in a number of consolidated dockets, in which “the Identified Entities shall show cause why they should not be found to have employed the above-described Gaming Practices in violation of the CAISO’s and PX’s tariffs; and (2) [in which] the appropriate remedies may be identified and quantified.” *Id.* at ordering paragraph A.¹²

In the Show Cause Order, the Commission agreed with the determinations concerning the MMIP made by the Staff in its Final Report. See Show Cause Order at PP at 23-25. The Commission found that the MMIP “serves as the rules of the road for market participants,” and that:

The MMIP contemplates that, while the ISO may try to correct misconduct on its own, the Commission is to be “the court of last resort” for misconduct committed by market participants, including the gaming and/or anomalous market behavior defined in the MMIP. While Part 2 of the MMIP enumerates suspect practices, MMIP 7.3 authorizes the ISO to impose “sanctions and penalties” or, as particularly relevant here, to refer matters to the Commission for appropriate sanctions or penalties.

Show Cause Order at PP 23, 24.

The Show Cause Order also found that the following practices constitute prohibited gaming practices that violate the MMIP and for which the Commission would seek disgorgement of all unjust profits received as a result of those violations:

- False Import, also known as “Ricochet” or “Megawatt Laundering.” See *id.* at PP 37-39.

¹² On the same day that the Show Cause Order was issued, the Commission, based on the Staff’s Final Report, also issued an order directing Enron and a number of partnership entities to show cause why their behavior during January 1, 2000 to June 20, 2001 does not constitute gaming and/or anomalous behavior as defined in the CAISO and PX tariffs. “Order to Show Cause Concerning Gaming and/or Anomalous Market Behavior Through the Use of Partnerships, Alliances or Other Arrangements and Directing Submission of Information,” 103 FERC ¶ 61,346 (June 25, 2003).

The Commission also issued an order that same day directing the Commission’s Office of Market Oversight and Investigation (“OMOI”) to investigate anomalous bidding behavior and practices in the Western markets for the period May 1, 2000 to October 2, 2000. “Order Requiring Demonstration that Certain Bids Did Not Constitute Anomalous Market Behavior,” 103 FERC ¶ 61,347 (June 25, 2003). *Inter alia*, the Commission found that the MMIP prohibits the bidding behavior at issue in the proceeding. *Id.* at P 2.

- Congestion-Related Practices. *See id.* at PP 41-46. The Commission explained that four types of practices fall into this category:
 - Cutting Non-firm, also known as Non-firm Export.
 - Circular Scheduling, also known as “Death Star.”
 - Scheduling Counterflows on Out-of-Service Lines, also known as “Wheel Out.”
 - “Load Shift.”
- Ancillary services-related practices, collectively known as “Get Shorty.” *See id.* at PP 48-51. The Commission explained that two types of practices fall into the category of prohibited “Get Shorty” practices:
 - Paper Trading, i.e., Hour-Ahead buyback of Ancillary Services.
 - Double Selling.
- Selling Non-Firm Energy as Firm. *See id.* at P 54.

Additionally, the Show Cause Order found that the following practices constitute prohibited gaming practices that violate the MMIP, but as to which the Commission would not seek disgorgement of unjust profits:

- Underscheduling load. *See id.* at PP 56-58.
- Overscheduling load, also known as “Inc-ing load” or “Fat Boy.” *See id.* at PP 59-60.

On the same day that the Commission issued the Show Cause Order, it also issued an order revoking the market-based rate authorities and terminating the blanket marketing certificates of Enron and a number of its affiliates. “Order Revoking Market-Based Rate Authorities and Terminating Blanket Market Certificates,” 103 FERC ¶ 61,343 (June 25, 2003) (“Revocation Order”). As to Enron, one of the reasons provided for these Commission actions was that Enron had engaged in the prohibited gaming strategies discussed in the Show Cause Order. *See id.* at P 53. With regard to some of the affiliates, one of the reasons provided for these Commission actions was that the affiliates had engaged in wash trading that resulted in the manipulation of prices. *See id.* at P 61.

In addition to the practices detailed in the Enron Memos, and addressed in the subsequent Staff investigation and Commission orders discussed above, the physical withholding of energy by suppliers has also been shown to have contributed to the California electricity crisis. On March 21, 2001, the CAISO released a study entitled "Empirical Evidence of Strategic Bidding in the California Real Time Market" ("Strategic Bidding Study"), in which the CAISO found that suppliers engaged in physical and economic withholding to influence market prices in 2000.¹³ The Strategic Bidding Study concluded that economic withholding was the dominant bidding strategy employed by the five major in-state suppliers to inflate prices, but such suppliers also engaged in physical withholding. Strategic Bidding Study at 8-9.

In addition, evidence of physical withholding has been presented to the Commission in two proceedings. On January 31, 2003, the Commission issued an order approving a Stipulation and Consent Agreement between the Commission Staff and Reliant Resources, Inc. and other Reliant companies (collectively, "Reliant"), concerning market manipulation by certain Reliant employees intending to raise prices artificially. "Order Approving Stipulation and Consent Agreement," 102 FERC ¶ 61,108 (Jan. 31, 2003) ("Reliant Order"). Under the Stipulation and Consent Agreement, Reliant will pay approximately \$13.8 million to customers of the PX, in order to compensate customers for Reliant's traders having reduced the amount of power they offered to the PX for delivery on June 21 and 22, 2000 below the amount that normally would have been offered under existing market conditions. See *id.* at PP 1-2, 4. The payment reflects "the worst case scenario of the effect of Reliant's withholding on the California market." *Id.* at P 6. Transcripts of the conversations of the Reliant employees showed that the reason they limited the amount of available power was to increase the PX's day-ahead prices in order to mitigate losses in Reliant's existing forward positions. *Id.* at 13.

In Docket No. IN01-3-000, questions were raised concerning whether Williams Energy Marketing & Trading Company ("Williams") and AES Southland, Inc. ("AES") had colluded to manipulate electricity prices by withholding power from the market. See *AES Southland, Inc. and Williams Energy Marketing and Trading Company*, 94 FERC ¶ 61,248 (2001). As detailed in a report that was not made public until November 15, 2002,¹⁴ employees of these companies (1) discussed extending an outage at a California plant for the sole purpose of driving up the prices the state was then paying for electricity, and (2) concocted a reason for shutting down a second plant AES operated for Williams different than the reason communicated to the CAISO. In the proceeding, the Commission

¹³ The Strategic Bidding Study was prepared by Anjali Sheffrin, the CAISO's Director of Market Analysis.

¹⁴ The report is entitled "Non-Public Appendix to Order Directing Williams Energy Marketing & Trading Company and AES Southland, Inc., to Show Cause, Docket No. IN01-3-000."

issued an order directing Williams and AES directing them to show cause, *inter alia*, why they should not be found in violation of the FPA. *Id.* Subsequently, Williams and AES entered into a Stipulation and Consent Agreement with Commission Staff, whereby Williams agreed, *inter alia*, to refund to the CAISO a total of \$8,000,000. The Commission approved the Stipulation and Consent Agreement.¹⁵

C. Inadequacy of Commission and CAISO Authority

The numerous events, investigations, and orders discussed above constitute irrefutable evidence that Market Participants have had opportunities to engage in – and have in fact engaged in – improper and harmful behavior. It is imperative that effective measures be in place to deter such inappropriate behavior going forward. As the Commission stated in the SMD NOPR:

[t]he market monitor must play an important role in the enforcement of the market rules contained in the Independent Transmission Provider's tariff. In this role the market monitor will need to coordinate closely with the Commission's investigative and enforcement staff. However, to ensure effective enforcement, the market monitor must have adequate authority to investigate market participant conduct and the Independent Transmission Provider must have a set of predetermined penalties to apply to conduct that is in violation of the rules of the Independent Transmission Provider's tariff.

SMD NOPR at P 454 (emphasis added).¹⁶

The penalties proposed under the O & I proposal are necessary to deter inappropriate behavior effectively because, as explained in the Commission Staff's Initial Report, the Commission's ability to impose penalties currently is

¹⁵ See *AES Southland, Inc. and Williams Energy Marketing & Trading Company*, 94 FERC ¶ 61,248 (2001); *AES Southland, Inc. and Williams Energy Marketing & Trading Company*, 95 FERC ¶ 61,167 (2001).

¹⁶ Moreover, the SMD White Paper explained:

The [RTO's or ISO's] market power mitigation measures must protect against the exercise of market power At a minimum, the RTO's or ISO's tariff should include rules limiting bidding flexibility where there is localized market power. The RTO's or ISO's tariff must also include clear market rules designed to prevent market manipulation strategies, including the types of anti-gaming tariff provisions in the proposed rule.

SMD White Paper at 8.

very limited. Initial Report at 79.¹⁷ Further, the U.S. Federal Energy Regulatory Commission Fact Sheet ("Fact Sheet") concerning the Initial Report explained that "[c]ivil penalties would prove a more effective means of deterring [the strategies employed by Enron], but the Commission's civil penalty authority is limited and can't be applied in any of the cases discussed in the staff report." Fact Sheet at 3. In the Final Report, the Staff reiterated its recommendation from the Initial Report that Congress expand the Commission's civil penalty authority. See Final Report at ES-17.¹⁸

The United States General Accounting Office ("GAO") also reached a conclusion similar to that of the Commission Staff in a report issued in June 2002 entitled *Energy Markets: Concerted Actions Needed by FERC to Confront Challenges That Impede Effective Oversight* ("GAO Report"). The GAO explained the scope of the Commission's limited penalty authority as follows:

[m]oreover, because FERC's legal authorities for natural gas and electricity are mostly derived from laws enacted when the industries comprised highly regulated monopolies, FERC has been attempting to develop and implement a regulatory and oversight approach for competitive markets, with an outdated legislative framework and using authorities that may not be adequate for today's competitive

¹⁷ Under Section 315(a) of the FPA, a public utility that willfully fails to comply with any order of the Commission, to file any report required under the FPA or any Commission rule or regulation thereunder, to submit any information or document required by the Commission in the course of an investigation conducted under the FPA, or to appear by an officer or agent at any hearing or investigation in response to a subpoena issued under the FPA can be fined an amount of up to \$1,000. In addition, Section 316 of the FPA provides for *criminal* penalties for violations of the FPA, which are imposed by a court rather than by the Commission. Under Section 316(a), a person convicted of knowingly or willfully violating the FPA can be fined up to \$5,000 and/or imprisoned for up to two years. Under Section 316(b), any person convicted of knowingly or willfully violating any rule, regulation or order imposed by the Commission can be fined up to \$500 per day for each day the violation occurs. Thus, the Commission itself has little authority to impose civil penalties pursuant to the express provisions of the FPA. This fact limits the Commission's ability to impose penalties for the following behavior that is addressed in the O & I proposal: physical withholding; submitting false information or schedules; gaming and market manipulation; and failing to cooperate with CAISO investigations. In that regard, all the Commission can do is require the disgorgement profits earned by activity that violates a Tariff. The O & I proposal seeks to overcome these shortcomings by establishing explicit and substantial penalties for violations of such rules of conduct.

¹⁸ The Final Report also noted that the MMIP prohibits gaming and "anomalous market behavior," and that under the MMIP the CAISO can address misconduct on its own or refer instances of misconduct to the Commission, or, alternatively, that the Commission can enforce a tariff or portion of a tariff (such as the MMIP) even in the absence of a complaint or referral (Final Report at VI-7 to VI-9). As detailed in Section IV, *infra*, the O & I proposal builds upon these provisions by adding rules of conduct concerning the CAISO's oversight and investigation authority and sets out specific monetary penalties for engaging in various types of misconduct. Thus, the effectiveness of the O & I provisions in preventing misconduct and penalizing entities that engage in it can be expected to surpass the effectiveness of the MMIP.

markets. For example, the potential for a company to engage in anticompetitive behavior and charge excessive prices for electricity is a significant concern when rates are determined by the marketplace instead of cost-of-service regulation, especially when the markets are still evolving. However, FERC's authority to levy civil penalties if it identifies this type of behavior is limited, because its authority is derived from laws that were enacted in a cost-of-service environment.

GAO Report at 7. The GAO Report went on to note a consequence of the Commission's limited penalty authority:

Without a meaningful range of penalties, FERC lacks adequate enforcement "bite" to deter anticompetitive behavior or other violations of market rules. Such deterrence is an important part of an effective oversight approach, especially because FERC will likely not be able to review all the transactions in detail to identify such behavior or violations.

Id.

The current inadequacy with respect to the policing of inappropriate Participant behavior is further highlighted by the Commission's "Order Seeking Comments on Proposed Revisions to Market-Based Rate Tariffs and Authorizations," 103 FERC ¶ 61,349 (June 26, 2003) ("Proposed Revisions Order"). Therein, the Commission stated that it proposed to identify "more precisely and comprehensively" transactions that would be prohibited as a condition of authorizing sellers to make sales at market-based rates. *Id.* at P 6. The Commission sought comments on the six proposed market behavior rules, titled Unit Operation, Market Manipulation, Communications, Reporting, Record Retention, and Related Tariffs. *Id.* at PP 18-36 and ordering paragraph B. The proposed rule concerning Market Manipulation contains prohibitions of types of behavior similar to those described in the Show Cause Order.

Because the Commission has little authority to impose civil penalties under the FPA, the Commission lacks the statutory tools to effectively deter violations of market rules or inappropriate market behavior. Further, although the Commission has the authority to order disgorgement of profits in instances when a Market Participant engages in behavior that violates the Tariff, such disgorgement only puts the Market Participant back in the position it would have been in had it not engaged in the improper behavior.¹⁹ This does not serve as

¹⁹ A Commission directive that requires a refund to be made is not correctly characterized as a penalty. See, e.g., *Carolina Power & Light Company*, 87 FERC ¶ 61,083, at 61,356 (1999); *San Diego Gas & Electric Co., et al.*, 97 FERC ¶ 61,275, at 61,239 (2001) (disgorgement of amount by which a party has been unjustly enriched is an equitable remedy).

any disincentive for Market Participants to engage in gaming and market manipulation because they essentially can engage in such behavior on a “risk-free” basis. Although the investigations and proceedings by the Commission and other authorities described above are beneficial, they are not an adequate substitute for implementation of the O & I Program. In each of the investigations referenced above, a result was obtained only after considerable time and effort was invested to reach the result. This kind of *ex post* case-by-case effort by the Commission and other authorities cannot serve as (1) a reasonable substitute for a systematic, *ex ante* oversight and investigation program such as that being proposed by the CAISO or (2) an effective deterrent against gaming, market manipulation, and other improper market behavior.

In contrast to the Commission’s limited civil penalty authority, the CAISO can impose penalties as a “term” or “condition” of service in connection with a market participant’s receipt of transmission service or participation in the market. Indeed, on numerous occasions, the Commission has approved penalty provisions for public utilities and natural gas companies. In particular, the Commission has approved penalties in individual public utility company tariffs that exceed the market value of the service or the market benefits received by the market participant that engaged in the improper behavior.²⁰ In that regard, the Commission has regularly accepted penalty provisions as long as they are capped at a level of twice the standard rate for the service at issue. See, e.g., *Alliance Companies, et al.*, 94 FERC ¶ 61,070 (2001) (penalty of twice the stated rate for unauthorized use of regulation and frequency reserve service is consistent with the Commission’s policy of allowing penalties equal to twice the stated rate); *American Transmission Company, L.L.C.*, 93 FERC ¶ 61,267 (2000) (penalty of 200 percent of the applicable charge for unauthorized use of Ancillary Services); *Wayne-White County Electric Cooperative*, 89 FERC ¶ 61,282 (1999) (twice the rate for unauthorized Ancillary Services). The Commission has even approved penalties of up to three times the applicable penalty for violations of market rules that occur during emergencies or if the market participant has shown a pattern of rules violations.²¹ The stiff penalties proposed by the CAISO – and the fact that such penalties will be spelled out up front in the Tariff – will serve as a more effective deterrent of inappropriate behavior than the mere potential for the disgorgement of profits after the fact. Further, compared to *ex post* investigations, the O & I Program will provide more clarity and certainty to Market Participants regarding the behavior that is expected of them. This should foster development of a more efficient and well-functioning market, as well as an environment that promotes investment in additional infrastructure. Finally, the CAISO notes that, oftentimes, the Commission has been able to redress past wrongs only years after the misbehavior occurred. With the rules of conduct,

²⁰ See, e.g., New York ISO Market Monitoring Plan (“NYISO MMP”), Sections 4.3.3–4.3.4.

²¹ See Section 13 of the ISO New England Market Rules and Procedures (“MRP 13”), Section 13.5.3.

investigation process, and applicable penalties spelled out up front, the CAISO should be able to address improper behavior and violations of rules of conduct in a more timely manner, thereby instilling – in both consumers and Market Participants – greater confidence in the operation of the market.²²

D. Relationship Between O & I and Market Redesign

As the Commission is well aware, the CAISO is in the process of undertaking a comprehensive market redesign. In that regard, on May 1, 2002, the CAISO filed its Comprehensive Market Design Proposal (“MD02 Filing”) in Docket No. ER02-1656. The CAISO proposed to implement MD02 in three phases. Phase I includes, *inter alia*, market power mitigation measures designed to prevent physical and economic withholding and penalties for failure to comply with Schedules, as modified by CAISO dispatch instructions. Phase II includes elimination of the market separation rule and balanced Schedule requirement and implementation of simultaneous Congestion Management, a Day-Ahead Energy market, Ancillary Services procurement, and unit commitment on a zonal basis (the “integrated forward market”). Phase III provides for implementation of the full network model and the integrated forward market based on locational marginal pricing (“LMP”) on a nodal basis.

On July 17, 2002, the Commission issued an “Order on the California Market Design Proposal,” 100 FERC ¶ 61,060 (2002) (“July 17 Order”). In its July 17 Order, the Commission ruled on the merits of the CAISO’s Phase I proposal and authorized the CAISO to expend funds for the development of LMP and the full network model, but determined that the specifics of implementation of those elements should be addressed in a technical conference established by the July 17 Order. Since that time, the CAISO has been involved in an ongoing process regarding development of the Phase II and Phase III market design elements. The CAISO will be filing the Phase II and III elements contemporaneously with this O & I proposal.

Given that the CAISO is in the process of implementing a comprehensive market redesign, it begs the following questions: (1) why is O & I necessary given that the CAISO will implement a comprehensive market redesign; and (2) if O & I is necessary, why should O & I be implemented prior to implementation of MD02? With respect to the former question, O & I and MD02 are not mutually exclusive; indeed, they are complementary. The CAISO recognizes that an essential first step to achieving and maintaining markets that function optimally and efficiently is implementing a well-conceived market design.²³

²² Moreover, the O & I proposal will provide market participants with a timely, fair, and adequate opportunity to challenge penalties imposed by the CAISO, and the Commission ultimately will determine whether any CAISO-imposed penalty should be affirmed.

²³ Indeed, the CAISO’s June 21, 2002 White Paper on the review of O & I stated, as its first guiding principle, that the CAISO would “[r]ely first on market design to provide proper incentives

Nevertheless, O & I, in and of itself, is extremely important to the CAISO, the State of California and, most importantly, consumers in California, especially given the events of the past couple of years. As the Commission has recognized, “even in competitive markets, it is possible for participants to engage in anti-competitive and deceptive practices.” Revocation Order at P 68. Thus, even under the market design contemplated in MD02, there will still be a need to have the O & I provisions in place to deter anti-competitive behavior and to apply penalties for engaging in such behavior. Indeed, the proposed requirements that Market Participants comply with operating orders, comply with availability requirements, submit feasible schedules and bids, provide factually accurate information, and provide information required by the ISO Tariff are “basic” rules that every independent system operator should have in place to govern interaction between Market Participants and itself regardless of what type of market design it has. With respect to the proposed rules of conduct addressing physical and economic withholding,²⁴ the CAISO is not expanding the scope of existing Tariff obligations. Therefore, the provisions of the O & I proposal are equally important to the CAISO’s existing design as they will be under the MD02 regime.

The need for the O & I provisions is also apparent from the Commission’s SMD NOPR. As noted below, the rules of conduct in the O & I proposal generally correspond to the “minimum behavioral rules” identified in the SMD NOPR. Indeed, in the SMD NOPR, that Commission expressly recognizes that such “basic” behavioral rules are an “important adjunct to the market power mitigation and monitoring plan.” SMD NOPR at P 445. In separate sections of the SMD NOPR, the Commission proposes implementation of an integrated market and LMP – proposals that are substantially the same as those the CAISO is proposing in MD02. This constitutes recognition by the Commission that the “basic” behavioral rules are different than market design and have their own justification for being implemented (and should be implemented). Thus, in the SMD NOPR, the Commission is separately proposing both a new market design and new “minimum” behavioral rules. Similarly, the CAISO is proposing a new market design in its MD02 and new “minimum” behavioral rules in its O & I proposal. In other words, the combination of MD02 and the O & I Program will provide appropriate rules of conduct and enforcement mechanisms, and will serve purposes comparable to those described in the SMD NOPR. Under these circumstances, the Commission cannot reasonably find the implementation MD02 eliminates the need for the O & I Program.²⁵

for behavior that supports reliable operation and market efficiency, using penalties and sanctions only as a backstop.”

²⁴ The CAISO is proposing penalties for physical withholding which the CAISO heretofore has not had.

²⁵ In the Final Report, the Commission Staff stated that supply shortfalls and a flawed market design facilitated the ability of certain Market Participants to engage in market

A second possible objection to the O & I proposal is that O & I should be implemented at the same time MD02 is implemented, not before such time. There is no merit to such an argument. First, the O & I provisions address types of behavior that are not addressed by MD02 – behavior that the Commission itself has acknowledged has harmed California. For example, the O & I provisions address many of the Enron gaming strategies, including “Inc-ing Load” (“Fat Boy”), “Get Shorty,” “Non-firm Export,” “Death Star,” and selling non-firm energy as firm. Forcing California to wait more than one year (until MD02 implementation) before implementing measures designed to address these Enron-type games that admittedly have been occurring in the California market would be unconscionable and would effectively operate to condone such improper behavior – behavior that has led to multiple criminal indictments. For these reasons, the O & I changes should be implemented now and retained in the future as an adjunct to the comprehensive MD02 market redesign.

Second, O & I should not be delayed because it will provide the CAISO with a much needed means for enforcing rules of conduct by granting the CAISO direct authority to penalize those entities that do not cooperate with the CAISO’s market monitoring authority. For example, the O & I proposal includes explicit penalties for failure to cooperate with CAISO investigations, respond to CAISO data requests in connection with CAISO investigations, and provide factually accurate schedules, reports, and communications to the CAISO. In the SMD NOPR, the Commission recognized that “[a] few of the strategies in the Enron memoranda appear to depend on the marketer providing false information to the ISO” and “these strategies rely on evading or violating the market rules rather than market design flaws.” SMD NOPR, Appendix E at 3. Requiring the CAISO to wait until MD02 implementation to implement an effective mechanism for deterring the submission of factually inaccurate information is unjustifiable under these circumstances.

Similarly, as the CAISO has previously advised the Commission, the CAISO has had to deal constantly with the problems caused by Scheduling Coordinators submitting schedules and schedule changes that are not feasible (due to ramping or other technical constraints). See, e.g., Motion for Leave To File Answer and Answer of the California Independent System Operator Corporation, pp. 66-67, Docket No. ER02-1656, filed June 17, 2002. It is incumbent on suppliers to submit accurate ramping and operational (and related) information to the CAISO and Schedules (and Schedule changes) that are feasible. The CAISO should not be required to second guess bids submitted by

manipulation. Final Report at ES-1. However, that is different from a contention that if the conditions had not existed, no market manipulation would have occurred. Even with no supply shortfalls and a satisfactory market design, certain Market Participants might still attempt to engage in market manipulation. The fact that it will be harder for them to succeed does not mean they will not try, or that their efforts do not need to be guarded against.

a Scheduling Coordinator or scramble to ensure reliable grid operations because suppliers have not submitted accurate, up-to-date information regarding the physical capabilities of their units. To deter this type of behavior, the O & I proposal sets forth a specific penalty for the submission of infeasible schedules. The CAISO needs this sanctioning authority to deal with a problem that exists now.

Likewise, as discussed above, there is evidence that many generators in California have falsely reported outages. This is behavior that might be deterred if the CAISO had authority to impose penalties for failure to fulfill availability reporting requirements as proposed herein. Again there is no logical reason for requiring the CAISO to wait until MD02 implementation to have such a tool.

Finally, in the SMD NOPR, the Commission recognizes that market monitors must have the ability to obtain certain market participant data in order to analyze fully the competitiveness of the market operated by an independent transmission provider. SMD NOPR at P 448. The Commission states that, as a condition for participating in the markets and using the transmission grid, market participants must agree to provide the market monitor with any information requested. *Id.* at P 449. The ability of the CAISO's DMA to perform its monitoring role is dependent upon the ability to acquire the necessary information. Accordingly, the CAISO must have the ability to impose penalties for non-compliance with requests for needed information. The CAISO currently lacks this authority, and it has been extremely difficult for the CAISO to obtain needed information in the course of numerous investigations.

Thus, for the foregoing reasons, there is no reasonable basis for the Commission to reject the O & I proposal on the grounds that the problems O & I seeks to address are dealt with in MD02. Likewise, there is no basis for the Commission to defer implementation of O & I until implementation of MD02.

E. Conclusion

As the aforementioned discussion makes clear, gaming, market manipulation, physical withholding, and the submission of false information have been significant problems in the ISO Control Area. Heretofore, the CAISO has not had strong enough sanctions in place to deter Market Participants from engaging in such behavior. The CAISO is proposing to implement rules of conduct and sanctions as part of the O & I proposal that will more effectively combat the many inappropriate behaviors identified above, including many of the Enron games, physical withholding and the submission of false information. In addition, the new rules of conduct discussed in Section IV, *infra*, will address other problems that the CAISO has been confronting, namely the submission of non-feasible schedules and bids and non-cooperation with CAISO investigations. Approval of the CAISO's proposed rules of conduct is necessary so that the

CAISO can have the necessary mechanisms in place to deter parties from engaging in these behaviors in the first place. As the Commission itself has recognized, it is preferable to have effective *ex ante* rules in place that seek to modify and/or deter behavior than to remedy misdeeds on an after-the-fact basis. See, e.g., *San Diego Gas and Electric Co., et al.*, 93 FERC ¶ 61,294 (2000); 93 FERC ¶ 61,121 (2000). The O & I proposal is consistent with that sound philosophy.

The CAISO will discuss many of these events in greater detail below. The bottom line is that the prevalence of such events over the past several years demonstrates a clear and pressing need for the CAISO to possess enhanced oversight, investigation, and enforcement authority in order to deter (1) activities that undermine the transparent, fair, and efficient operation of electricity markets and/or reliable operation of the transmission grid and (2) non-compliance with important rules of conduct.

III. OVERSIGHT AND INVESTIGATION PROGRAM OVERVIEW

A. Program Objectives

The overriding purpose of the O & I proposal is to eliminate any confusion, real or imagined, concerning the behavior expected of Market Participants and to establish the process pursuant to which the CAISO will monitor Energy markets operated by the CAISO. The objects of this effort are to (1) promote reliable operation of the transmission grid, (2) operate dependable, effectively functioning, efficient, fair, and competitive markets, (3) operate markets that produce just and reasonable prices for consumers, and (4) deter behavior by Market Participants that is inconsistent with such objectives.

The CAISO recognizes that its existing MMIP prohibits Gaming and Market Manipulation and authorizes the Commission and in limited circumstances, the CAISO, to impose penalties for such behavior.²⁶ The O & I proposal refines the prohibitions set out in the MMIP by reorganizing general prohibitions into defined rules of conduct and by affording the CAISO enhanced direct sanctioning authority.²⁷ The granting of this enhanced authority will

²⁶ See Brief of the California Independent System Operator Corporation Addressing Staff's Interpretation of ISO and PX Tariff Authority, Docket No. PA02-2-005 (filed Apr. 11, 2003) ("ISO Brief on Tariff Authority").

²⁷ The types of behavior proscribed in the MMIP, namely, "Anomalous Market Behavior," "Abuse of Reliability Must-Run Status," and "Gaming," sufficiently indicate to Market Participants the practices that are prohibited. See *id.* at 3-5, 14. However, the CAISO also believes it can only be beneficial, and certainly not harmful, to provide further guidance through the rules of conduct described above, i.e., to further delineate the "hue[s] and shade[s] of prohibited behavior." See *id.* at 14. This appears especially true in light of contentions by certain Market

provide greater deterrence of violations, and stronger means of enforcing the rules of conduct, than is currently possible under the MMIP. Further, the procedures described in the O & I proposal will result in prompter redress of such violations. The O & I proposal, like the MMIP, continues to contain provisions permitting the CAISO to refer possible violations of the rules of conduct to the Commission. It also permits the CAISO to refer possible violations to other oversight and enforcement agencies. These provisions in the O & I proposal will increase the ability of the Commission and other Oversight and Enforcement Agencies to pursue civil or criminal penalties, as well, where appropriate, thus deterring to an even greater degree violations of the rules of conduct.

Significant events, most notably the gaming strategies employed by Enron, have demonstrated the need for the CAISO to have more effective measures in place – in addition to the market redesign improvements being developed through the CAISO’s Comprehensive MD02 process – in order to deter Gaming, Market Manipulation, and/or non-compliance by Market Participants with certain basic obligations that are essential if the CAISO is to operate its markets and transmission grid effectively. Indeed, the Commission has recognized this need not only in investigations it has initiated, but also in its SMD NOPR and its April 28, 2003 SMD White Paper (“SMD White Paper”). SMD NOPR at P 445, Appendix E at 1-3; SMD White Paper at 2, 8. Consistent with the Commission’s recommendation in the SMD NOPR, the O & I proposal includes penalties for violations of the rules of conduct. The penalties have been set at levels that are designed to deter behavior that is inconsistent with such rules of conduct.

The O & I proposal provides a framework for a comprehensive, umbrella investigation and enforcement program with a level of process and controls sufficient to ensure that CAISO authority for penalties is administered responsibly, without preference or undue discrimination.²⁸

Moreover, the O & I proposal is consistent with the three elements of a strong energy market, as described by Commission Chairman Pat Wood III: “balanced Market Rules, adequate infrastructure and vigilant oversight.” Commission Press Release, “Chairman Wood Outlines FERC Plans for 2003,

Participants that assert they have not been provided adequate guidance on the types of proscribed behaviors. See Coral Power, L.L.C., Brief on Commission Staff’s Interpretation of the Market Monitoring & Information Protocols & Its Request for Issuance of Show-Cause Orders, Docket No. PA02-2-000 (filed Apr. 11, 2003), at 3-6; PacifiCorp’s Brief on MMIP Interpretation Issues, Docket No. PA02-2-005 (filed Apr. 11, 2003), at 9. While the CAISO disagrees with these contentions, it is nevertheless willing to refine the proscriptions first set out in the MMIP, which action by the CAISO should address any such contentions by Market Participants.

²⁸ All penalties administered by the CAISO will be required to meet the standards for documentation and controls specified by the CAISO’s independent auditor for compliance with a Type 2 audit in accordance with Statement of Auditing Standards (SAS) No. 70 Type 2.

SMD White Paper Planned” (Jan. 13, 2003). In particular, the O & I proposal will serve to provide balanced rules of conduct and vigilant oversight for California, thereby facilitating the development of a sufficient electric energy infrastructure in the state.

B. Elements of O & I Program

As noted above, the O & I Program consists principally of five key elements. The first element of the O & I Program is comprised of several defined rules of conduct (and associated penalties) that are patterned on the “minimum behavioral rules” identified in the SMD NOPR, as well as on rules of conduct that the Commission has approved for other independent transmission providers and market operators. Among these rules of conduct – which are set forth in the new Enforcement Protocol – are the following “basic” rules: (1) compliance with operating orders; (2) the submission of feasible Energy and Ancillary Services bids and schedules; (3) prohibition of physical withholding; (4) prohibition of economic withholding; (5) compliance with availability reporting requirements; (6) the provision of factually accurate information; and (7) the provision of information required by the ISO Tariff. These Rules of Conduct²⁹ are set forth in Sections 2.2 through 2.8 of the Enforcement Protocol. The investigation process for potential violations of these Rules of Conduct is set forth in Section 3 of the Enforcement Protocol.

Also included among these conduct rules are more general provisions prohibiting and providing specified penalties for Detrimental Practices and Market Manipulation. These ISO Tariff provisions are found in Sections 2.9 and 2.10 of the Enforcement Protocol. The investigation process for possible violations of these Rules of Conduct is set forth in Section 4 of the Enforcement Protocol.

Apart from these Enforcement Protocol provisions, the CAISO purposes to insert additional conduct rules within the main body of the Tariff, because of their close relation to existing market operation rules. These proposed ISO Tariff revisions, which address specific types of behavior are discussed in Section V of this transmittal letter. First, the CAISO proposes to add a new Section 2.2.9 to its Tariff prohibiting submission of Schedules on transmission paths with operating transfer capabilities of zero and allowing the CAISO to reject such Schedules if they are submitted. Second, the CAISO proposes to amend Section 2.5.21 of its Tariff to establish the buy-back price for Ancillary Services sold to the CAISO in the Day-Ahead Market as the greater of the Day-Ahead Market price or the Hour-Ahead Market price. Third, the CAISO proposes to amend Section 7.3.1.5.2 of

²⁹ The capitalized terms “Detrimental Practices,” “FERC,” “Final Market Notice,” “Formal Warning,” “Market Manipulation,” “New Behavior,” “Net Excess Load,” “Oversight and Enforcement Agency,” “Participant Benefits,” “Preliminary Market Notice,” and “Rules of Conduct” are terms defined in the EP. See EP 1.2.2. When used as capitalized terms hereafter in this transmittal letter, these terms have the same definitions as shown in the EP.

its Tariff to provide that when a Schedule in the counter direction of Congestion is not delivered, any Usage Charge payments for the counter-flow that is not delivered will be eliminated. Fourth, the CAISO proposes to amend Section 2.3.1.2.1 of the ISO Tariff, to make clear that Energy and Ancillary Service Schedules and Supplemental Energy bids by resources eligible to supply Imbalance Energy are binding obligations, and that any resource "self-committing" through a Day-Ahead Schedule for Energy is obligated to start and be available for Dispatch by the CAISO. Finally, the CAISO proposes new Tariff Section 7.3.1.5.3 specifically to address the problems caused by circular Schedules.

The second element of the O & I Program consists of predefined penalties for violations of Rules of Conduct, which the CAISO would have direct authority to administer. These penalties are set forth in Sections 2.2 through 2.10 of the Enforcement Protocol, and Appendix A to the Enforcement Protocol. In several cases, the penalties are further subdivided into special penalties for specific types of violations of a Rule of Conduct. The administration of penalties is discussed in detail in Section 5 of the Enforcement Protocol.

The penalties under the Enforcement Protocol consist of fixed dollar amounts, variable amounts, or a combination of the two. The penalties that entail fixed dollar amounts range from \$10,000 to \$110,000 per event, and may include additional amounts such as the allocation of any WECC RMS penalty. The penalties that entail variable amounts are based on items such as MWh of Energy not provided (e.g., for non-compliance with an operating order) or Market Participant benefits received (e.g. for Detrimental Practices or Market Manipulation). These penalties represent the maximum amount that the CAISO would levy against a Market Participant for a particular violation. In determining the actual level of the penalty to impose in a specific circumstance, from zero to the maximum amount, the CAISO may consider any of the various factors set forth in Sections 5.1 and 5.3 of the Enforcement Protocol that are applicable, including aggravating factors such as Rule of Conduct violations during System Emergencies and mitigating factors such as inadvertent behavior. In only two specific circumstances does the Enforcement Protocol authorize the CAISO to triple the maximum amount of a fixed penalty: (a) if the violation occurred during a System Emergency; or (b) if the CAISO determines that the violation is a part of a continuing pattern of the same violation for which monetary penalties have previously been imposed.

The third element of the O & I proposal, which is discussed in greater detail in Section VI, *infra*, is the CAISO's proposal to add a new Section 20.3.5, to the ISO Tariff to permit the CAISO to disclose confidential and/or commercially sensitive information to the federal and state Oversight and Enforcement Agencies (including the Commission) as described in Section 20.3.5. The section requires that each of the Oversight and Enforcement Agencies to which

information is disclosed must be bound, at a minimum, to a legal obligation that sets forth in writing the terms applicable to the treatment of confidential and/or commercially sensitive information, and that obligates the agency not to disclose to any third party information provided under the section without providing at least five business days' notice to the CAISO and the affected Market Participant.

The fourth element of the O & I proposal is the publication of information regarding Market Participants' performance in relation to their Tariff obligations under the CAISO's Information Release Program. As this element does not require action by the Commission, the CAISO began implementing it in November 2003. The Information Release Program consists of publishing various metrics on Market Participant performance, with the philosophy that making this information visible to the market as a whole will encourage Market Participants to comply with their Tariff obligations and discourage gaming and market manipulation. The information the CAISO publishes under this initiative includes:

- Late Schedules Reports: daily summaries of Scheduling Coordinators that submit late or incorrect Schedules that delay the closing of CAISO markets.
- Ancillary Services Non-Performance: weekly summaries of Scheduling Coordinators' "No Pay" adjustments for non-performance of Ancillary Services obligations (scheduled for implementation in July 2003).
- Load Scheduling Accuracy: weekly summaries of Scheduling Coordinators' metered Load compared to scheduled Load (scheduled to be implemented in October 2003).
- Uninstructed Deviation Penalties: weekly summaries of Uninstructed Deviation Penalties incurred by Scheduling Coordinators (to be implemented in coordination with MD02 Phase 1B).

In addition, the CAISO is considering publishing information on Market Participants who violate proposed Rules of Conduct and the details of proposed penalties assessed Market Participants.

The fifth element of the O & I proposal consists of programs for cross-training of the CAISO staff and staffs of the Oversight and Enforcement Agencies on each of their respective laws and regulations, rules, and enforcement activities. In addition to the Tariff changes described in this document, the CAISO is also focusing externally to establish closer relationships with the Oversight and Enforcement Agencies. The CAISO Compliance and DMA staffs have worked extensively in the past with Commission staff, the California Department of Justice, the California Public Utilities Commission ("CPUC"), and

the California Electricity Oversight Board ("EOB"). The CAISO is in the process of visiting each of these agencies plus the United States Department of Justice, U.S. Attorney to introduce members of the CAISO Compliance and Market Analysis departments to the relevant agency officials and to formally present the elements of the O & I Program. The CAISO seeks to establish mechanisms to provide relevant, timely and useful information to these Oversight and Enforcement Agencies, and for the CAISO and the Oversight and Enforcement Agencies staff to become familiar with each other's respective laws, regulations, and rules.

Several steps are underway to better equip CAISO staff to respond to events that may represent non-compliance, gaming, or market manipulation. All employees are required to undergo training on the employee code of conduct, and other meetings are being held by DMA and Compliance staff to explain what kinds of events to look for, how to report suspicious events, and how those referrals are treated. All internal "Non-Compliance" log entries are examined and referred, and an e-mail address for "Compliance Notifications" has been established. Additional efforts to better communicate the actions that the CAISO takes as a result of internal referrals are also underway.

Finally, although not a formal part of the O & I Program, the present filing also proposes several changes to the CAISO's existing MMIP. These revisions are intended to complement the O & I proposal and correct various outdated and erroneous references in the MMIP.

C. Stakeholder Process

The CAISO initiated the Oversight and Investigations Activities Review on June 14, 2002. From the start, the CAISO has been committed to share with the Market Participants the results of the review and provide ample opportunity for comment. The CAISO presented its proposals through many different venues, such as through Market Notices, Market Issue Forum meetings, Market Surveillance Committee meetings, conference calls and open CAISO Board meetings. Attachment E to the present filing provides the timeline for the O & I stakeholder communications.

The CAISO received many comments that in turn helped in the establishment of the O & I Program elements. The CAISO has been responsive to these stakeholder comments by incorporating them into the development of the O & I Program, taking actions that included:

- Revising the proposed confidentiality provision additions to state that Market Participants will be notified of the categories of information that the CAISO will provide to the Oversight and Enforcement Agencies and that Market Participants will have access to their data that is shared with these

agencies. Further, the CAISO agreed to establish a program for orientation of Oversight and Enforcement Agency staff on the format and meaning of data provided to help assure that such data would be appropriately interpreted. In addition, the CAISO added the CPUC as an Oversight and Enforcement Agency with which the CAISO proposes to share information.

- Several factors were added for the determination of penalties for Rule of Conduct violations, including: (1) accommodating reasonable load forecast deviations in determining penalties for over-scheduled load under the Rule of Conduct requiring the provision of factually accurate information; (2) accommodating a Market Participant's adherence to Good Utility Practice as a factor to be considered in the assessment of penalties for failing to provide complete and accurate Settlement Quality Meter Data under the Rule of Conduct requiring the provision of factually accurate information and (3) accommodating the variability of a generator's performance due to climatic variations and emissions, license, and other limitations as a factor to be considered in the assessment of penalties for violations of the Rule of Conduct requiring compliance with operating orders issued by the CAISO.
- Added a provision that parties will be notified when they are being investigated by the CAISO before penalties are assessed and will be provided the opportunity to present facts to explain their actions.
- Made various changes to clarify the meaning of the specific Rules of Conduct.
- Deleted various proposed penalties due to concerns that they could be equitably administered including penalties for submitting late schedules.
- Created explicit Rules of Conduct for physical withholding and economic withholding.
- Modified the process for prohibiting detrimental behavior or market manipulation to provide appropriate notice, including incorporating a proposed two-step market notification process and the posting of market notices under the ISO Home Page.

D. Actions Requested of the Commission

For the reasons set forth above, the CAISO requests that the Commission take the following action with respect to the O & I proposal:

- Approve the new Enforcement Protocol, in particular:

- The seven basic Rules of Conduct set forth in Sections 2.2 through 2.8 of the Enforcement Protocol, and their associated penalties.
- The two rules addressing gaming (i.e., Detrimental Practices) and market manipulation set forth in Section 2.9 and 2.10, respectively, of the Enforcement Protocol, and their associated penalties.
- Approve the following five proposed Tariff modifications that provide for additional rules of Market Participant conduct:³⁰
 - Section 2.2.9 – A new Tariff section created in order to prohibit the submission of Schedules on transmission paths with operating transfer capabilities of zero and allowing the CAISO to reject such Schedules if they are submitted.
 - Section 2.5.21 – Revised to set the buy-back price for Ancillary Services sold to the CAISO in the Day-Ahead Market as the greater of the Day-Ahead Market price or the Hour-Ahead Market price.
 - Section 7.3.1.5.2 – Revised to provide that when a Schedule in the counter direction of Congestion is not delivered, any Usage Charge payments for the counter-flow that is not delivered will be eliminated.
 - Section 2.3.1.2.1 – Revised to make clear that Energy and Ancillary Service Schedules and Supplemental Energy bids by resources eligible to supply Imbalance Energy, as well as “self-commitments,” are binding obligations.
 - Section 7.3.1.5.3 – A new Tariff section created specifically to address the problems caused by circular Schedules.
- Approve the proposed new Tariff Section 20.3.5 to permit the CAISO to disclose confidential and/or commercially sensitive information to the federal and state Oversight and Enforcement Agencies.
- Approve several changes to the MMIP, which fall into the following four categories: (1) “housekeeping” revisions in order to correct certain

³⁰ As described in Section V, *infra*, the CAISO also requests approval of related changes to sections of the protocols and to Appendix A to the ISO Tariff.

outdated and erroneous references in the MMIP; (2) changes to ensure consistency between the MMIP and EP; (3) an explanation that the MMIP provides a general framework for the operation of the DMA and the MSC and is not intended to limit the activities or remedies available to these entities; and (4) modifications involving the authority and responsibilities of the MSC.

IV. THE ENFORCEMENT PROTOCOL

A. The Basic Rules of Conduct

The CAISO proposes new language setting forth seven defined Rules of Conduct – and penalties associated with such conduct rules – that generally are modeled on the “certain *minimum* behavioral rules” identified in the SMD NOPR and are consistent with the market rules that the Commission has approved for other independent transmission providers and market operators.³¹ These Rules of Conduct address the following: (1) compliance with operating orders; (2) schedule and bid feasibility; (3) physical withholding; (4) economic withholding; (5) availability reporting; (6) factual accuracy; and (7) compliance with CAISO information requests. These Rules of Conduct constitute the “bare necessities” that any independent transmission provider must have to perform its core

³¹ As described below, the CAISO has incorporated practices contained in Section 13 of the Market Rules and Procedures (“MRP 13”) of ISO New England (“ISO-NE”), which the Commission has approved. See *New England Power Pool*, 85 FERC ¶ 61,379, at 62,470-71 (1998); *ISO New England Inc.*, 93 FERC ¶ 63,321, at 62,098 n.4 (2000). Below, this transmittal letter cites to specific sections of ISO-NE MRP 13.

In addition, the O & I proposal incorporates Commission-approved practices of the following entities:

-- Northern Maine Independent System Administrator (“NMISA”), the New York Independent System Operator, Inc. (“NYISO”), and PX. See *Northern Maine Independent System Administrator, Inc.*, 91 FERC ¶ 61,060 (2000). These practices are contained in Market Rule 7 (“MR 7”) of the NMISA. Below, this transmittal letter cites to specific sections of NMISA MR 7.

-- The New York Independent System Operator Corporation (“NYISO”). See *New York Independent System Operator, Inc., et al.*, 89 FERC ¶ 61,196 (1999); *New York Independent System Operator, Inc., et al.*, 90 FERC ¶ 61,317, *clarified*, 91 FERC ¶ 61,154 (2000); *New York Independent System Operator, Inc.*, 95 FERC ¶ 61,471 (2001); *New York Independent System Operator, Inc.*, 96 FERC ¶ 61,249 (2001); *New York Independent System Operator, Inc., et al.*, 99 FERC ¶ 61,246 (2002). These practices are contained in the NYISO Market Monitoring Plan (“NYISO MMP”). Below, this transmittal letter cites to specific sections of the NYISO MMP.

-- The PX. See *California Power Exchange Corporation*, 88 FERC ¶ 61,112 (1999); *California Power Exchange Corporation*, 89 FERC ¶ 61,137 (1999). These practices are contained in Schedule 10 of the PX Tariff (“Schedule 10”). Below, this transmittal letter cites to specific sections of PX Schedule 10. The PX’s no longer being in operation does not diminish the fact that the Commission approved the use of Schedule 10.

functions effectively. While the conduct prescribed in the rules is prohibited under existing general provisions regarding gaming and market manipulation, certain market participants have claimed confusion on this point. The rules are designed to eliminate any opportunity for the assertion of such claims. The Rules of Conduct, and the specific prohibited behaviors associated with them, are found in Sections 2.2 through 2.8 of the Enforcement Protocol, and the investigation process associated with these Rules of Conduct is found in Section 3 of the Enforcement Protocol.

The seven "basic" Rules of Conduct provide additional guidance concerning expected behavior, either by identifying specific actions or identifying specific outcomes that are prohibited. In general, these "basic" Rules of Conduct address behaviors that jeopardize reliable grid operations, threaten the competitiveness and efficiency of CAISO markets, or hinder CAISO investigations of abnormal and potentially improper behavior. In other words, they address behaviors that strike at the heart of the CAISO's core functions. Over the past several years, the CAISO has encountered numerous instances where Market Participants have engaged in behavior that is inconsistent with the proposed "basic" Rules of Conduct. The establishment of a standardized set of sanctions should encourage all CAISO Market Participants to comply with "basic" terms and conditions of service by holding out the possibility of financial penalties for non-compliance. The seven "basic" Rules of Conduct and prohibited behaviors under the Rules of Conduct are discussed in greater detail below.

1. Summary of Each Rule

a. Compliance with Operating Orders

Section 2.2(a) of the Enforcement Protocol contains a Rule of Conduct requiring Market Participants to comply with operating orders issued by the CAISO. In accordance with this Rule of Conduct, Section 2.2(b) of the Enforcement Protocol specifies that, unless otherwise provided in Section 2.2, a violation of this Rule of Conduct is subject to a maximum standard penalty of \$10,000 per event and allocation of any WECC RMS penalty incurred by the CAISO due to such event (pursuant to Section 2.5.26.5 of the ISO Tariff) and an amount equal to the Market Clearing Price multiplied by the quantity of energy called for in the operating order that was not provided. As described in Section 2.2(b), examples of events that may constitute a violation of the Rule of Conduct include (but are not limited to) events that include the following: failure of a Generating Unit, System Unit, or System Resource owned or controlled by a Participating Generators without a bid for available Generation to comply with an order to start-up, increment, or decrement output pursuant to Section 5.6.1 of the ISO Tariff; and failure by a Must-Offer Generator to operate a Generating Unit on-line and at minimum load so that it is capable of providing all of its available capacity in compliance with the must-offer obligation, as set forth in Sections

5.11 *et seq.* of the ISO Tariff, unless such a unit has been granted a waiver or exception pursuant to Section 5.11.6 of the ISO Tariff. Section 2.2(c) describes the special penalties applicable to the following: failure of a UDC to implement an order issued by the CAISO to curtail Load in order to manage a System Emergency, pursuant to Section 4.5.3 and Section 2.3.1.2.1 of the ISO Tariff; and any failure to comply with an operating order that contributes to or prolongs an outage as described in Section 2.3.2.9.3 of the ISO Tariff. Section 2.2(d) provides an exception stating that violations of the Rule of Conduct that are subject to the Uninstructed Deviation Penalty under Section 11.2.4.1.2 of the ISO Tariff are subject to penalty under the Rule of Conduct only to the extent that the CAISO has issued a separate and distinct non-automated Dispatch Instruction to the Market Participant.

Market Participants at times refuse to comply with operating orders, which can cause significant operational difficulties. These events of non-compliance can threaten the reliable operation of the grid. The proposed revisions to Tariff Section 2.3.1.2.1, described below in Section V.D, as well as the new Tariff provisions in Section 2.2 of the Enforcement Protocol, address these problems. Because there are currently no specified penalties associated with a Market Participant's failure to comply with operating orders, there is little incentive for Market Participants to comply with CAISO operating orders. As indicated above, the mere potential that profits will be disgorged as a result of inappropriate behavior is not sufficient to deter such behavior. For example, there is presently little risk of financial penalty to UDCs that fail to comply with orders to curtail firm load if, for example, they do not believe that curtailment is necessary. It is essential that the CAISO have the authority to impose adequate penalties on Market Participants that fail to comply with operating orders and UDCs that fail to comply with curtailment orders so that any behavior that may threaten reliable grid operations is deterred. The penalties proposed by the CAISO herein should serve as a more effective deterrent.

The provisions requiring compliance with CAISO operating orders are comparable to ISO-NE MRP 13.4.1, which proscribes failure to provide energy and services in response to ISO-NE instructions, and ISO-NE MRP 13.4.3, which proscribes failure to follow ISO-NE instructions, including routine ISO-NE transmission dispatch instructions, ISO-NE operating instructions during a System Emergency with respect to transmission facilities, and rules for scheduling or rescheduling transmission maintenance. The provisions are also comparable to NMISA MR 7.4.3, which proscribes failure to follow routine NMISA transmission instructions, operating instructions during a System Emergency with respect to transmission facilities, and rules for scheduling or rescheduling transmission maintenance. Additionally, the provisions are comparable to PX Schedule 10, Section 4.1.6, which proscribed failure to a PX participant to comply with PX instructions for generation and/or intertie changes if it results in penalties or charges to the PX or its participants. The provisions are also

comparable to the market rule in the Proposed Revisions Order concerning Unit Operation. See Proposed Revisions Order at P 18.

Further, the CAISO notes that the Commission approved a system of substantial penalties and sanctions for the Midwest ISO to ensure compliance with operating orders and instructions. See *Midwest Independent Transmission System Operator*, 84 FERC ¶¶ 61,231 at 62,161 (1998). These included penalties of up to \$10,000 per day per violation, as well as the ability to withhold transmission revenues from a transmission owner until a violation ceases.³² The Commission found such system of fines and penalties to be sufficient to ensure compliance with operating orders and instructions.

In addition, the requested authority is consistent with the authority the Commission has granted to individual public utilities, i.e., the authority to impose penalties on parties that refuse to curtail load when requested by the utility. See, e.g., *Sierra Pacific Power Company, et al.*, 101 FERC ¶ 61,201 (2002); *Southwest Power Pool, Inc.*, 86 FERC ¶ 61,090 (1999); *Allegheny Power Systems, et al.*, 80 FERC ¶ 61,143 at 61,545-46 (1997), *order on reh'g*, 85 FERC ¶ 61,325 (1998); see also *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Service by Public Utilities; Recovery of Stranded Costs by Public Utilities*, Order No. 888, FERC Stats. & Regs. ¶ 31,036 at 31,749 (1996).

Non-compliance with CAISO operating orders can jeopardize the reliable operation of the transmission grid. For the same reasons the Commission has authorized other independent transmission system and market operators to impose penalties for non-compliance with operating orders, the Commission should authorize the CAISO to impose penalties for failure to comply with CAISO operating orders and instructions.

b. Submission of Feasible Energy and Ancillary Service Bids and Schedules

Section 2.3(a) of the Enforcement Protocol contains a Rule of Conduct requiring Market Participants to bid and schedule Energy and Ancillary Services from resources that are available and capable of performing at the levels specified in the bid and/or schedule. Section 2.3(b) provides that a violation of the Rule of Conduct is subject to a maximum standard penalty of \$10,000 per event, subject to the exceptions described in Section 2.3(c). These exceptions provide that violations of the Rule of Conduct for which an Uninstructed Deviation Penalty under Section 11.2.4.1.2 of the ISO Tariff has been assessed or for

³² The Commission authorized the Midwest ISO to impose a \$50 per kW charge on a transmission customer that fails to curtail load in response to a Midwest ISO directive.

which payments under Section 2.5.26 of the ISO Tariff have been eliminated are not subject to penalty under Section 2.3 of the Enforcement Protocol.

The provisions requiring the submission of feasible bids and schedules incorporate and build on language from the market rule in the SMD NOPR requiring feasible bids and schedules. See SMD NOPR at P 445. The CAISO desperately needs authority to impose penalties for non-compliance with a feasible schedule requirement. As indicated in Section II.D, *supra*, the CAISO has experienced operational difficulties due to the submission of infeasible Schedules.

Moreover, the proposed Tariff provisions are comparable to ISO-NE MRP 13.4.2, which proscribes the provision of inaccurate bid or operating information, understatement of a resource's operating limit, misrepresentation regarding operating conditions, and misrepresentation of resource availability. Such Tariff provisions also are comparable to NMISA MR 7.4.2, which proscribes the provision of inaccurate operating information, misrepresentation regarding operating conditions, and misrepresentation of resource availability. Further, the provisions are comparable to PX Schedule 10, Section 4.1.4, which proscribed failure of a PX participant to submit a schedule equal to the amount awarded in the day-ahead auction.

c. Physical Withholding

Section 2.4(a) of the Enforcement Protocol contains a Rule of Conduct providing that Market Participants may not engage in physical withholding of the output of a Generating Unit, in whole or in part. The Rule of Conduct provides that physical withholding occurs when an entity fails to offer to sell or schedule into the ISO Market the output of or services of a Generating Unit capable of serving a CAISO market, in a manner consistent with the ISO Tariff. Section 2.4(b) of the Enforcement Protocol provides that, subject to the exception in Section 2.4(c), a violation of the Rule of Conduct is subject to a maximum standard penalty of \$25,000 per event and an amount equal to twice the Participant Benefits received by the offending party as a result of such behavior. The exception in Section 2.4(c) provides that behavior otherwise falling under this Rule of Conduct that is the particular focus of another provision in the ISO Tariff specifically designed to address such behavior (e.g., Appendix A to the MMIP is not subject to penalty under Section 2.4. As the Tariff currently includes specific provisions addressing most, if not all forms of physical withholding (such as Appendix A to the MMIP, for example), few penalties are likely to be assessed under this rule, at least pursuant to the Tariff as it is currently comprised. Nonetheless, the rule makes explicit the impropriety of the behavior, and the penalties serve as a backstop in the event that the current Tariff provisions change or are overturned and/or an unanticipated form of physical withholding not currently addressed is identified.

The provisions concerning physical withholding incorporate and build on language from the market rule in the SMD NOPR prohibiting physical withholding. See SMD NOPR at P 445. Moreover, the CAISO's proposed definition of physical withholding is similar to the definition of physical withholding in the NYISO MMP, Section 2.4(a)(1). Additionally, the provisions are comparable to ISO-NE MRP 13.4.2 and NMISA MR 7.4.2 which proscribe the submission of inaccurate bid or operating information, understatement of a resource's operating limit, misrepresentation of operating conditions, and misrepresentation of resource availability. As indicated in Section II.B, *supra*, there is clear and convincing evidence that physical withholding has occurred in the CAISO markets. The CAISO needs a Rule of Conduct to prohibit such behavior, as well as corresponding sanctions for non-compliance in order to deter such behavior.³³

d. Economic Withholding

Section 2.5(a) of the Enforcement Protocol contains a Rule of Conduct providing that Market Participants may not engage in economic withholding of the output of a Generating Unit. The Rule of Conduct further provides that economic withholding occurs when an entity (1) submits bids for a Generating Unit that are not consistent with the bid caps or thresholds specified in the ISO Tariff or any applicable agreement, or (2) submits bids for a Generating Unit that are unjustifiably high (relative to the known operational characteristics and/or the known operating cost of the resource) and the Generating Unit is not or will not be dispatched or scheduled, or the bids (which are unjustifiably high) will set a Market Clearing Price. Section 2.5(b) states that, subject to the exception in Section 2.5(c), a violation of this Rule of Conduct is subject to a maximum standard penalty of \$25,000 per event and an amount equal to twice the Participant Benefits received by the offending party as a result of such behavior. The exception in Section 2.5(c) provides that behavior otherwise falling under this Rule of Conduct that is the particular focus of another provision in the ISO Tariff specifically designed to address such behavior (e.g., the Automated Mitigation Procedure set forth in Appendix A to the MMIP) is not subject to penalty under Section 2.5. As is the case with the Rule of Conduct concerning physical withholding, few penalties are likely to be assessed under the Rule of Conduct prohibiting economic withholding, at least pursuant to the Tariff as it is currently comprised. Nonetheless, the rule makes explicit the impropriety of the behavior, and the penalties serve as a backstop in the event that the current Tariff provisions change or are overturned and/or an unanticipated form of economic withholding not currently addressed is identified

³³ The CAISO notes that the Commission recently approved the Midwest ISO's proposal to impose financial penalties for physical withholding in the real-time market. *Midwest Independent Transmission System Operator, Inc.*, 102 FERC ¶ 61,280, at P 96 (2003).

The provisions concerning economic withholding incorporate and build on language from the market rule in the SMD NOPR prohibiting economic withholding. See SMD NOPR at P 445. Moreover, the proposed definition of economic withholding is virtually identical to the definition of economic withholding in the NYISO MMP, Section 2.4(a)(2).

e. Compliance with Availability Reporting Requirements

Section 2.6(a) of the Enforcement Protocol contains a Rule of Conduct requiring that Market Participants comply with all reporting requirements governing the availability and maintenance of a Generating Unit or transmission facility, including proper Outage scheduling requirements. The Rule of Conduct further requires that the responsible entity (Scheduling Coordinator or Participating Transmission Owner) must immediately notify the CAISO when capacity changes or resource limitations occur that affect the availability of the unit or facility or the ability to comply with Dispatch Instructions. Section 2.6(b) provides that a violation of this Rule of Conduct is subject to a maximum penalty of \$10,000 per event, subject to the exception in Section 2.6(c). The exception provides that violations of the Rule of Conduct for which an Uninstructed Deviation Penalty under Section 11.2.4.1.2 of the ISO Tariff has been assessed are not subject to penalty under Section 2.6.

One of the most common sources of operational difficulties facing the CAISO is inaccurate data regarding resource availability. If a Generating Unit is known to be out of service, and the CAISO's outage scheduler is properly updated, then that Generating Unit will not be dispatched by the CAISO. However, if the resource is shown to be available, either because an outage was not promptly reported to the CAISO or due to a delay in updating the CAISO's systems, then Dispatch Instructions may be needlessly sent to that resource, increasing the uncertainty of Imbalance Energy response. These problems will be mitigated when the CAISO implements Phase 1B of MD02, which includes an electronic interface for reporting outages. Nonetheless, this rule will make explicit the obligations of Market Participants to provide consistent, timely, and complete reports of changes in resource availability.

The provisions concerning availability reporting requirements incorporate and build on language from the market rule in the SMD NOPR concerning availability reporting requirements. See SMD NOPR at P 445. Moreover, the provisions are comparable to ISO-NE MRP 13.4.2 and NMISA MR 7.4.2, which proscribe the submission of inaccurate bid or operating information and misrepresentation of resource availability. The provisions are also comparable to ISO-NE MRP 13.4.4 and NMISA MR 7.4.4, which proscribe failure to provide timely and accurate information, including routine reports, information in

response to inquiries about System Emergencies or disturbances in its Control Area, information in response to special information requests, market settlement information, and resource information. In addition, the provisions are comparable to PX Schedule 10, Section 4.1.3, which prohibited changes by PX participants to scheduled resource availability after data is transferred to the CAISO. Finally, the proposed provisions are similar to PX Schedule 10, Section 4.1.7, which proscribed failure by a PX participant to communicate changes in its resource availability in a timely manner.

f. Factual Accuracy Requirement

Section 2.7(a) of the Enforcement Protocol contains a Rule of Conduct requiring that all applications, schedules, reports, and other communications to the CAISO by a Market Participant or agent of a Market Participant, including maintenance and outage data, bid data, transaction information, and load and resource information, be submitted by a responsible company official who is knowledgeable of the facts submitted. The Rule of Conduct further requires that all information submitted be true, complete, and consistent with the operational plans of the company to the best knowledge of the person submitting the information.³⁴

Section 2.7(b) of the Enforcement Protocol provides that, unless otherwise provided in Section 2.7(c), a violation of this Rule of Conduct is subject to a maximum standard penalty of \$10,000 per event. Section 2.7(c) provides special penalties that are applicable as follows:

(1) Submitting Load Schedules that are substantially in excess of metered Load served by a Scheduling Coordinator is subject to a maximum special penalty equal to the Net Excess Load multiplied by the applicable Market

³⁴ In the Show Cause Order, the Commission explained that False Import and Selling Non-Firm Energy as Firm constitute a prohibited gaming practice. See Show Cause Order at PP 37-39, 54. These practices also violate the Rule of Conduct requiring the provision of factually accurate information, and will be reported to the appropriate Oversight and Enforcement Agencies. The Commission also explained that Overscheduling Load also constitutes a prohibited gaming practice (though not one for which disgorgement of unjust profits would be sought). See Show Cause Order at P 59. This practice likewise violates the Rule of Conduct requiring the provision of factually accurate information, and will be reported to the appropriate Oversight and Enforcement Agencies.

Further, in the Show Cause Order, the Commission determined that each of the four Congestion-Related Practices (Cutting Non-firm, Circular Scheduling, "Wheel Out," and "Load Shift") "violated the MMIP because the market participants submitted false schedules to the ISO." Show Cause Order at P 46. Thus, these practices also constitute violations of the Rule of Conduct requiring the provision of factually accurate information, which Rule of Conduct, as described in this section, requires the submission of accurate schedules.

Clearing Price.³⁵ The CAISO will determine Net Excess Load by calculating the amount by which scheduled Load exceeds actual Load plus a reasonable tolerance band established by the CAISO from time to time and posted under the ISO Home Page. The CAISO intends to initially establish this tolerance band at 10% more than a Scheduling Coordinator's actual Load within each congestion zone or 25 MWh, whichever is greater, with an additional allowance for actual transmission losses associated with the Generation or imports scheduled to serve the scheduled Load. The CAISO will phase out the allowance for the component of transmission losses associated with Generation when a specific mechanism to explicitly schedule such losses is implemented as part of MD02 Phase 1B. The CAISO will monitor scheduling performance with this initial tolerance band and revise as appropriate, giving consideration to stakeholder input. ;

(2) Failing to provide complete and accurate Settlement Quality Meter Data as provided in Section 10 of the ISO Tariff and Section 4.1 of the Meter Service Agreement, that results in an error that is discovered after issuance of Final Settlement Statements is subject to special penalties as described in Appendix A to the Enforcement Protocol;

(3) Engaging in a Circular Schedule is subject to the rescission of the Usage Charge in accordance with Section 7.3.1.5.3 of the ISO Tariff and an additional maximum penalty equal in value to the Usage Charge so rescinded.

A factual accuracy requirement such as that proposed by the CAISO is essential for any independent transmission provider or market operator. The CAISO needs to be able to rely on the information and schedules/bids submitted by Market Participants to reliably operate the grid, maintain the integrity of CAISO investigations, and coordinate outages. The Commission recognizes in the SMD NOPR that several of the Enron games depended on the marketer providing false information to the CAISO. SMD NOPR, Appendix E at 3. A factual accuracy requirement, as well as sufficient penalties for non-compliance with such requirement, is necessary to deter such behavior in California in the future.

The provisions in this Rule of Conduct build on the factual accuracy requirement from the related market rule in the SMD NOPR. See SMD NOPR at P 445. Moreover, the provisions are comparable to ISO-NE MRP 13.4.2 and NMISA MR 7.4.2, which, as described above, proscribe the submission of inaccurate bid or operating information, understatement of high operating limit,

³⁵ Failure to submit an accurate load schedule encompasses the practice of "Load Shift," which the Show Cause Order determined is a prohibited gaming practice. See Show Cause Order at P 45. The practice of "Load Shift" may also be considered a violation of the Market Rules concerning gaming and market manipulation, and will also be reported to the appropriate Oversight and Enforcement Agencies.

misrepresentation of operation conditions, and misrepresentation of resource availability. The provisions are also comparable to ISO-NE MRP 13.4.4 and NMISA MR 7.4.4, which proscribe failure to provide timely and accurate information, including routine reports, information in response to inquiries about System Emergencies or disturbances in its control area, information in response to special information requests, market settlement information, and resource information. Additionally, the provisions are comparable to PX Schedule 10, Section 4.2.2, which proscribed failure to provide accurate meter data to the PX pursuant to the PX tariff and operating manual. The CAISO also notes that the Rule of Conduct concerning the factual accuracy requirement is comparable to the market rule in the Proposed Revisions Order concerning Communications. See Proposed Revisions Order at P 26.

g. Compliance with Obligations to Provide Information Required by the ISO Tariff

Section 2.8(a) of the Enforcement Protocol contains a Rule of Conduct stating that all information that is required to be submitted to the CAISO under its Tariff, its protocols, or jurisdictional contracts must be submitted in a complete, accurate, and timely manner. The section also requires that Market Participants comply with requests for information or data by the CAISO that are consistent with the ISO Tariff, including timelines specified in the ISO Tariff for submitting Schedules or other information. Section 2.8(b) of the Enforcement Protocol explains that, except as otherwise provided in Section 2.8(c), a violation of this Rule of Conduct is subject to a maximum penalty of \$500 for each day that the required information is late. Section 2.8(c) specifies that failure to provide timely information in response to written requests by the CAISO for information reasonably necessary to conduct an investigation, or in response to an audit authorized by the Tariff, is subject to the following special penalties: a first event of noncompliance is subject to a maximum penalty of \$1,000 per day that the required information is late; a second such violation by the same Market Participant within a rolling three-year period is subject to a maximum penalty of \$2,500 per day; and any subsequent such violations by the Market Participant within a rolling three-year period are subject to a maximum penalty of \$5,000 per day.

The provisions concerning obligations to provide required information incorporate and build on language from the market rule in the SMD NOPR concerning obligations to provide required information and to cooperate in investigations and audits. See SMD NOPR at P 445. As the Commission recognizes in the SMD NOPR:

[s]ince the ability of the market monitor to perform his or her monitoring role is dependent upon the ability to acquire the necessary information, the monitor must have the ability to require

market participants to provide information. This is an important enforcement tool.

SMD NOPR at P 449. The CAISO wholeheartedly agrees with this conclusion and believes that “[a]s a condition for participating in the spot markets and using the transmission grid, market participants must agree to provide the market monitor with any information requested.” *Id.* As indicated in Section II.D, *supra*, the CAISO has encountered numerous instances in which Market Participants have refused to cooperate, or have cooperated only begrudgingly, in CAISO investigations. The CAISO needs a rule that imposes a cooperation requirement and an information obligation, as well as associated penalties, in order to facilitate the conduct of CAISO investigations and deter non-cooperation.

The CAISO also notes that the information obligation provisions of the Enforcement Protocol closely track similar provisions in ISO-NE MRP 13.4.4 and NMISA MR 7.4.4. Moreover, the information obligation provisions are comparable to PX Schedule 10, Section 4.1.1, which proscribed failure to meet the timelines established by the PX in accordance with the PX tariff, as well as PX Schedule 10, Section 4.4.1, which proscribed failure of a PX participant to provide information as requested by the PX’s compliance unit.

2. The Rules of Conduct are Consistent with the Proposed Standard Market Design and Other Commission Initiatives

The CAISO’s O & I proposal builds on the direction provided by the Commission in its SMD NOPR regarding the investigation and enforcement provisions that should be included in the tariffs of independent transmission providers. The Commission explained as follows:

[a]n important adjunct to the market power mitigation and marketing plan will be a clear set of rules governing market participant conduct with the penalties for violations clearly spelled out. The Commission proposes to require the Independent Transmission Provider to include in its tariff certain minimum behavioral rules, which will be monitored by the market monitor.

The Commission also required that these minimum behavioral rules “be accompanied by predetermined penalties.” SMD NOPR at P 446. With regard to penalties, the Commission explained that:

The market monitor must play an important role in the enforcement of the market rules contained in the Independent Transmission Provider’s tariff. In this role the market monitor will need to coordinate closely with the Commission’s investigative and

enforcement staff. However, to ensure effective enforcement, the market monitor must have adequate authority to investigate market participant conduct and the Independent Transmission Provider must have a set of predetermined penalties to apply to conduct that is in violation of the rules of the Independent Transmission Provider's tariff.

As a condition of participating in the markets operated by the Independent Transmission Provider and using the transmission grid operated by the Independent Transmission Provider, the Commission proposes to require market participants and transmission customers to agree to predetermined penalties that would apply to violations of the tariff rules. Since the tariff rules are intended to ensure the fair and efficient operation of the markets, the penalties should be designed to deter conduct that is inconsistent with fair and efficient operation of the markets. Specifically, the penalties should deter conduct that results in an economic benefit derived from a violation of the rules. The penalties should, at a minimum, require payment of the economic benefit derived by the violator from violating the rules. Where the violation could result in conduct that could be harmful to the reliability of the grid, it would be appropriate for the penalty to be significantly higher to serve as a deterrent for the conduct. The Independent Transmission Provider's tariff must specify the conditions that would apply for each level of penalty.

It may be appropriate to build into the tariff standards for mitigating the penalty. Some standards that could be used are: the impact on the operation of the grid, the financial impact on the violator, and any good faith efforts to maintain compliance. The Commission requests comment on the conditions that would justify mitigation of the penalty.

Id. at PP 454-56.

In the SMD White Paper, the Commission reiterated the importance of appropriate market power mitigation measures. It noted that such measures "are necessary for effective wholesale power markets." SMD White Paper at 2. The Commission also explained that:

For customers to benefit from wholesale power markets, it is critical that market prices fairly reflect the conditions of supply and demand rather than the exercise of market power. Each RTO or ISO would have an independent market monitor either for the individual RTO or ISO or for a larger region.

The market power mitigation measures must protect against the exercise of market power without suppressing prices below the level necessary to attract needed investment in new infrastructure in the region. At a minimum, the RTO's or ISO's tariff should include rules limiting bidding flexibility where there is localized market power. The RTO's or ISO's tariff must also include clear market rules designed to prevent market manipulation strategies, including the types of anti-gaming tariff provisions in the proposed rule.

Id. at 8.

The seven "basic" rules also satisfy another of the goals of the SMD NOPR because they will serve to deter certain of the Enron gaming strategies. Appendix E to the SMD NOPR, entitled "Standard Market Design and Trading Strategies Encountered in the Independent System Operators," describes the various Enron gaming strategies, discusses how the gaming strategies are harmful to the market, and indicates how the Standard Market Design is responsive to each strategy. The CAISO agrees with the Commission that use of the Enron gaming strategies needs to be curtailed. The seven "basic" Rules of Conduct address certain of the Enron games by (1) requiring that Market Participants provide factually accurate information and schedules and (2) submit feasible schedules and bids. In addition, the seven "basic" rules address other improper behavior that has been occurring in the ISO Market (as discussed in Section II, *supra*) such as physical withholding, failure to cooperate in CAISO investigations, and failure to provide the CAISO with information it requests and failure to comply with availability reporting requirements.

Also, the CAISO's proposed Rules of Conduct are consistent with the Commission's recent Proposed Revisions Order. Notably, several of the market behavior rules proposed by the Commission in that order are comparable to Rules of Conduct that the CAISO proposes in this filing. For instance, proposed Market Behavior Rule # 1 would require that sellers "operate and schedule generating facilities, undertake maintenance, declare outages, and commit or otherwise bid supply in a manner that complies with the rules and regulations of the applicable power market." This is consistent with Section 2.2 of the Enforcement Protocol, which requires that Market Participants comply with operating orders of the CAISO, and Section 2.3 of the Enforcement Protocol, which requires that Market Participants submit feasible Energy and Ancillary Services bids. Proposed Market Behavior Rule # 3 would require that sellers "provide complete, accurate, and factual information, and not submit false or misleading information, or omit material information, in any communications with the Commission, market monitors, regional transmission organizations, independent system operators, or similar entities." This is similar to Section 2.7

of the Enforcement Protocol, which would require the submission of factually accurate information by Market Participants. Moreover, the Commission made clear in this order that these proposed Market Behavior Rules were intended to complement, not supercede, individual RTO and ISO market rules and tariff conditions that apply to sellers in various markets.

3. The Rules Are Consistent with Commission Staff Recommendations

In addition to being consistent with the “minimum” market rules proposed in the SMD NOPR, the CAISO’s proposed “basic” Rules of Conduct are in accord with the recommendation of Commission Staff in the Initial and Final Reports. In the Initial Report, in discussing the provisions that should be included in market-based rate tariffs in order to combat the Enron gaming strategies, the Initial Report stated:

In a market environment, one expects that traders, working within Commission-approved market rules, will utilize various strategies in order to maximize profits. But a fundamental aspect of some of the Enron trading strategies is the deliberate use of false information. A market cannot operate properly without accurate information. Implicit in Commission orders granting market-based rates is a presumption that the power marketer’s behavior will not involve fraud or deception.

However, in light of the wide-spread nature of the Enron trading strategies, Staff recommends that the Commission require that all market-based rate tariffs include a specific prohibition against the deliberate submission of false information, or the omission of material information, whether to the Commission or to an entity such as an independent system operator, regional transmission organization, public utility, or market monitor. This tariff requirement should be worded broadly to cover any and all matters relevant to the wholesale markets, including maintenance and outage data, bid data, price and transaction information, and load and resource data. By including these specific prohibitions, any revenues generated from transactions associated with such activities would be subject to refund under the FPA. This refund provision would be an effective means by which the Commission can better ensure that the conduct of public utilities is consistent with the public interest.

Initial Report at 79. Similarly, in the Final Report, the Commission Staff recommended that the Commission expressly prohibit the use of false information as a condition for granting all market based rate authorizations and

add such a condition to all open access transmission tariffs. Final Report at VI-3. As described in greater detail above, the CAISO's proposed "basic" Rules of Conduct include a specific prohibition against the submission of false information.

4. The Rules are Consistent with Commission-Approved "Best Practices"

In preparing the O & I proposal, the CAISO reviewed the Commission-approved oversight and investigation provisions of other independent system operators and market operators and has incorporated the "best practices" of those entities into the O & I proposal. In particular, as discussed in greater detail above, the CAISO has incorporated Commission-approved practices contained in MRP 13 of ISO-NE. In addition, the O & I proposal incorporates Commission-approved practices of NMISA, the NYISO, and the PX. Consistent with its determinations in other proceedings, the Commission should grant the CAISO oversight and investigation authority similar to that which it has granted to other independent system operators and market operators.

B. Detrimental Practices and Market Manipulation

1. Summary of the Rules

In addition to the basic Rules of Conduct, Sections 2.9 and 2.10 of the Enforcement Protocol reaffirm prohibitions on "gaming" and "market manipulation," referred to in the Enforcement Protocol by the defined terms Detrimental Practices and Market Manipulation. These provisions build upon the existing provisions of the MMIP pertaining to "Gaming" and "Anomalous Market Behavior." As discussed in greater detail in Section IV.B.2, *infra*, the EP sets forth a new notice process pursuant to which the CAISO may prospectively prohibit specified activities as gaming or market manipulation and impose penalties on Market Participants that engage in such behavior. The CAISO will be permitted to impose penalties for these behaviors only by following specified procedures. However, the Commission will be able to impose the specified penalties *sua sponte* without having to undertake such a notice process. In other words, the Commission will retain the authority it currently has under the MMIP to find that certain behavior constitutes gaming or market manipulation, and the Commission can impose penalties for such behavior dating back to the date on which such behavior commenced.

In addition, the EP will provide for stiffer penalties for gaming and market manipulation than would otherwise be available. In that regard, acts of gaming and/or market manipulation would each be subject to a maximum standard penalty of \$25,000 per event and an amount equal to two times the Participant Benefits received by the offending party as a result of such behavior. EP 2.9(b), 2.10(b). These penalties should serve as a more effective deterrent than the

mere potential for the disgorgement of profits. As the Commission is well aware and as discussed generally in Section II, *supra*, gaming and market manipulation have occurred in the California market, and the existence of such behavior is well documented. Accordingly, in its proposed EP, the CAISO is proposing Rules of Conduct and associated penalties that should be more effective at deterring such inappropriate behavior than the existing rules. As discussed in greater detail in Section IV.B.2, *infra*, there are separate procedures for investigating and penalizing gaming and market manipulation.

Section 2.9(a) of the Enforcement Protocol contains a Rule of Conduct prohibiting Market Participants from engaging in Detrimental Practices as defined therein. For the purposes of the Rule of Conduct, Detrimental Practices mean behavior that meets both of the following requirements: (1) such behavior as takes unfair advantage of the rules and procedures set forth in or pursuant to the ISO Tariff to the detriment of System Reliability, other Market Participants, or the efficiency of CAISO markets; and (2) such behavior or behavior substantially similar to it that has been proscribed in a Final Market Notice in accordance with the procedures outlined in Section 4.6 of the Enforcement Protocol.

Section 2.10(a) of the Enforcement Protocol contains a Rule of Conduct prohibiting Market Participants from engaging in Market Manipulation, which is as defined therein as behavior that meets both of the following requirements: (1) such behavior as is fraudulent, deceptive, or manipulative and is intended to create artificial or distorted market prices or outcomes, including prices or outcomes that do not reflect or are not consistent with supply and demand conditions; and (2) such behavior or behavior substantially similar to it that has been proscribed in a Final Market Notice in accordance with the procedures outlined in Section 4.6 of the Enforcement Protocol. The CAISO notes that, in the Proposed Revisions Order, the Commission also proposed a market rule concerning market manipulation, which applies to transactions that "include, but are not limited to" some of the same prohibited practices that are described in the Show Cause Order. See Proposed Revisions Order at P 20.

2. Safeguards

The mechanisms by which the CAISO may investigate, prohibit, and ultimately impose penalties for Detrimental Practices or Market Manipulation are the Formal Warning, Preliminary Market Notice, and Final Market Notice. The CAISO will follow a "two-notice" process, whereby it will first file with the Commission a Preliminary Market Notice or Formal Warning identifying the specific Detrimental Practices or Market Manipulation behavior (defined as New Behavior in the EP) that it is investigating. At the conclusion of its investigation, the CAISO will issue (and file with the Commission) a Final Market Notice prohibiting the specified behavior. The CAISO can impose penalties only after

the CAISO issues a Final Market Notice prohibiting a specified type of behavior.³⁶ The specific procedures applicable to the CAISO's investigation of Detrimental Practices and Market Manipulation are set forth in Section 4 of the Enforcement Protocol.

After identifying a Detrimental Practices or Market Manipulation opportunity that may be exploited by one or more Market Participants, the CAISO may issue either a Preliminary Notice or a Formal Warning describing the Detrimental Practices or Market Manipulation opportunity,³⁷ specifying the New Behavior under investigation, providing an example of the behavior, and identifying the Rule of Conduct potentially violated by the behavior (Section 2.9 and/or Section 2.10 of the Enforcement Protocol).³⁸ The Preliminary Market Notice or Formal Warning also may contain a directive to Market Participants to cease and desist from engaging in the suspected behavior, on the terms specified in Section 4.5 of the Enforcement Protocol, pending conclusion of an investigation. EP 4.3, 4.4, 4.5.³⁹

The CAISO will post under the ISO Home Page all Preliminary Market Notices, along with related documents that provide clarifying information, and will concurrently e-mail such notices to all Market Participants included on the CAISO's e-mail distribution list. A Preliminary Market Notice becomes effective as of the time it is posted under the ISO Home Page. EP 4.3. If the CAISO is concerned that publicly identifying a Detrimental Practices or Market Manipulation opportunity would exacerbate the potential detriment of the behavior, the CAISO may issue a Formal Warning to the particular Market Participant(s) engaging in the activity rather than issuing a public Preliminary Market Notice. A Formal Warning will be transmitted to the affected Market Participant(s) by e-mail and also by overnight mail, and will become effective for

³⁶ The CAISO wishes to make it clear that these procedures apply *only* to the CAISO's investigation of Detrimental Practices and Market Manipulation and enforcement of the Rules of Conduct applicable to Detrimental Practices and Market Manipulation (including the imposition of penalties). As explained in further detail below, the Commission is not required to follow the market notice procedures to find that certain behavior constitutes Detrimental Practices or Market Manipulation and to impose penalties.

³⁷ As described in Sections 4.3 and 4.4 of the Enforcement Protocol, the Preliminary Notice or Formal Warning will be filed with the Commission within forty-eight hours of issuance, or, if the Commission office is not open for business at that time, by 10 a.m. Eastern Standard Time on the next business day thereafter. A Final Market Notice, described below, will be filed with the Commission within twenty-four hours of issuance, or, if the Commission office is not open for business at that time, by 10:00 a.m. Eastern Standard Time on the next business day thereafter. EP 4.6.

³⁸ New Behavior means conduct that is neither the subject of a prior market notice under the Enforcement Protocol nor substantially similar to conduct addressed in a prior market notice under the Enforcement Protocol. EP 4.2(a).

³⁹ The CAISO will uniformly provide the affected Market Participant(s) to present data, information, and/or written comment relevant to the event or behavior being investigated. The CAISO will consider all such information or data presented. EP 3.4.

a Market Participant as of the time the e-mail is transmitted to that Market Participant. A Formal Warning may be filed with the Commission under seal. EP 4.4.

Following the issuance of a Preliminary Market Notice or Formal Warning, the CAISO will undertake an investigation to determine whether the behavior warrants proscription under Section 2.9 and/or 2.10 of the Enforcement Protocol. EP 4.2(c). At the conclusion of the investigation, the CAISO will issue a Final Market Notice to all Market Participants and to the Commission. EP 4.2(d). A Final Market Notice may not be issued until at least 48 hours after issuance of a Preliminary Market Notice or Formal Warning. EP 4.6.

Thus, the Commission will be fully apprised of all investigations that the CAISO is conducting that ultimately could lead to the prohibition by the CAISO of activities found to constitute Detrimental Practices or Market Manipulation. The Commission would then be in a position to intervene – before the CAISO proscribes specific behavior or imposes any penalties – if it determines that such behavior should not be prohibited.

The Final Market Notice will contain a concise statement of the CAISO's findings and conclusions, including whether the suspected behavior thereafter will be deemed to be a violation of Section 2.9 and/or Section 2.10. Where the behavior is found to violate a Rule of Conduct, the Final Market Notice will state the possible consequences of such violation, including applicable penalties. The Final Market Notice will be posted under the ISO Home Page, will be e-mailed to all Market Participants included on the CAISO's e-mail distribution list, and will be effective as of the time it is posted under the ISO Home Page. A Final Market Notice prohibiting the suspected conduct will be deemed to cover the behavior described therein, and conduct substantially similar to such behavior. EP 4.6. The CAISO may not assess penalties under Sections 2.9 and/or 2.10 of the Enforcement Protocol until behavior under one or both of those sections, or behavior substantially similar to it, has been proscribed in a Final Market Notice. EP 2.9(c), 2.10(c). Moreover, the CAISO may not assess penalties under those sections for New Behavior until twenty-four hours after it has filed a Final Market Notice with the Commission concerning the New Behavior. Thereafter, the CAISO may assess penalties from the time of the issuance of the Final Market Notice, going forward. But at any time, the CAISO may refer suspicious behavior to the Commission or other authority for action. EP 4.8.⁴⁰ Moreover, the CAISO, in addition to imposing penalties under the Enforcement Protocol, may

⁴⁰ Additionally, a Preliminary Market Notice or Formal Warning may contain a directive to Market Participant(s) to cease and desist from engaging in the suspected behavior, pending conclusion of an investigation. In the event that a Market Participant does not comply with a cease and desist directive by the CAISO, and the suspected behavior subsequently is prohibited, the CAISO may refer such noncompliance to the Commission or other authority for corrective action. EP 4.5.

recommend that the Commission or other authority impose additional sanctions upon the Market Participant on a going-forward basis. EP 5.7.

As set forth in Section 4.7 of the Enforcement Protocol, the CAISO will consider the following factors, among others, in determining whether a behavior should be deemed a violation of Sections 2.9 and/or 2.10:

- (a) Whether the specific type of behavior meets the definition of Detrimental Practices and/or Market Manipulation stated in Sections 2.9 and/or 2.10.
- (b) Whether the specific type of behavior adversely impacts market prices in ways that are inconsistent with market supply and demand conditions.
- (c) The impact of the specific type of behavior on market efficiency.
- (d) Whether the specific type of behavior tends to make prices in comparable market converge, as in the case of most forms of arbitrage, or tends to make prices diverge from levels consistent with supply and demand in different markets.
- (e) Whether the specific type of behavior is sustainable, and the extent to which other Market Participants can replicate the behavior.
- (f) Whether other Market Participants are able to protect themselves from the specific type of behavior.
- (g) Whether the specific type of behavior negatively impacts System Reliability, considering the transparency of the specific type of behavior to the system operator, the impact of the specific type of behavior on prediction of real-time system performance, and the impact of the specific type of behavior on transmission availability.
- (h) Whether the specific type of behavior conflicts with legal or regulatory requirements.

These criteria build upon the Commission-approved criteria for "Gaming" and "Anomalous Market Behavior," as specified in the MMIP. See MMIP Sections 2.1.1, 2.1.2, and 2.1.3. In addition, these criteria are comparable to the Commission-approved factors that the CAISO can consider in evaluating whether a Forced Outage may have been the result of gaming. *San Diego Gas and Electric Co., et al.*, 98 FERC ¶ 61,202 (2002). The CAISO will apply the aforementioned general criteria to determine whether a behavior should be considered Detrimental Practices or Market Manipulation. However, as

explained above, in any Final Market Notice proscribing a particular activity, the CAISO will describe the specific behavior being prohibited and provide an example of such behavior. Thus, there will be sufficient specificity in the process.

It is also important to recognize that the notice requirements of the Enforcement Protocol only apply to action taken by the CAISO. The Commission would not be required to follow the market notice procedures to find that certain behavior constitutes Detrimental Practices or Market Manipulation and to impose penalties. Rather, the Commission can simply enforce the provisions of the Enforcement Protocol *sua sponte*. Further, if the Commission determines that certain conduct constitutes Detrimental Practices or Market Manipulation under the Enforcement Protocol, the Commission would have the authority to impose the specified sanctions back to the date the Market Participant first engaged in such unlawful behavior. EP 1.9. On the other hand, the CAISO itself can impose sanctions only prospectively, as discussed above. This is consistent with the authority that the Commission possesses under the current provisions of the MMIP.

The proposed procedures will enable the CAISO to address improper Detrimental Practices or Market Manipulation promptly on a case by case basis as the CAISO uncovers new types of Detrimental Practices and Market Manipulation behavior. This is important because opportunities for Detrimental Practices and Market Manipulation can arise in a variety of ways and Market Participants can develop new "games" that the CAISO cannot predict *a priori*. Therefore, it is impossible for the CAISO at this time to develop a comprehensive list of all activities that constitute Detrimental Practices or Market Manipulation. Rather, the CAISO must retain sufficient flexibility and be able to respond promptly when confronted with evidence that a certain type of behavior potentially jeopardizes system reliability or the integrity and efficiency of CAISO markets. The proposed procedures satisfy these criteria. Although the CAISO will not be able to impose penalties on Market Participants after-the-fact for engaging in Detrimental Practices or Market Manipulation, the Commission will have such authority (just as it has such authority today under the MMIP).

Several stakeholders have expressed concerns about the procedures for proscribing Detrimental Practices and Market Manipulation on the grounds that such procedures grant too much discretion to the CAISO. There is no merit to such claims. The proposed procedures provide significant transparency, as well as checks and balances on CAISO discretion. In that regard, the Preliminary Market Notice and Final Market Notice processes will be transparent to Market Participants because Preliminary Market Notices and Final Market Notices will be provided to all Market Participants in advance of the prohibitions described there being implemented. Similarly, any Formal Warning will be provided to the Market Participant(s) engaging in the questionable behavior in advance of the prohibitions described there being implemented. Further, the CAISO will

describe the specific behavior being prohibited and will provide an example of such behavior. Thus, it should be crystal clear to Market Participants exactly what behavior is being prohibited. Market Participants will not be able to claim that the CAISO is prohibiting some vague, ill-defined behavior.

In addition, the CAISO's proposal provides adequate opportunity for the Commission to act prior to the CAISO proscribing certain behavior and imposing penalties. Issuance of a Preliminary Market Notice/Formal Warning will facilitate input from Market Participants regarding the nature of the specific behavior being investigated by the CAISO, and should help the CAISO in reaching a final decision. Advance notification to Market Participants will allow them to petition the Commission if they believe that the CAISO is considering prohibiting a type of behavior that they believe does not constitute Detrimental Practices or Market Manipulation. Further, because both the Preliminary and Final Market Notices will be filed with the Commission, the Commission will have the ability to intercede promptly if it disagrees with the CAISO's conclusion that specific behavior should be prohibited. Moreover, Market Participants can challenge any penalties imposed by the CAISO pursuant to the ADR provisions of the ISO Tariff and can appeal any adverse decision to the Commission. EP 3.10. Thus, the Commission ultimately will determine whether it is appropriate to ban any specified Detrimental Practices or Market Manipulation behavior and/or whether any penalty imposed by the CAISO is appropriate. Under these circumstances, there is no opportunity for the CAISO to abuse any discretion it may have.

The CAISO notes that its "market notice process" for prohibiting Detrimental Practices and Market Manipulation is comparable to other processes pursuant to which public utilities can direct parties to undertake certain actions and impose penalties on parties that fail to act in accordance with the directives of the public utility. For example, the open access transmission tariff ("OATT") of the Midwest ISO (as well as the transmission tariffs of other public utilities) provides for a penalty for failure to curtail service as directed by the Midwest ISO.⁴¹ In particular, curtailment tariff provisions set forth the general criteria pursuant to which the public utility can order a party to curtail load.⁴² The public

⁴¹ See Midwest ISO OATT, FERC Electric Tariff, Second Revised Volume No. 1, Original Sheet Nos. 60 and 72. See also discussion in Section IV.A.1.a, *supra*, regarding circumstances in which other transmission providers can order parties to take certain actions and impose penalties for non-compliance.

⁴² For instance, Section 4.4.4 of the ISO Tariff permits the CAISO to order a Utility Distribution Company to curtail load "if necessary to avoid an anticipated System Emergency or to regain operational control over the ISO Controlled Grid during an actual System Emergency." Moreover, the Midwest ISO's tariff provides that a curtailment must be implemented in order to maintain reliable operation of the Midwest ISO's transmission system and the systems directly and indirectly connected with the Midwest ISO's transmission system, and that the Midwest ISO reserves the right to curtail service when the Midwest ISO, in its sole discretion, deems that an emergency or other unforeseen condition impairs or degrades the reliability of the transmission system or the systems directly and indirectly interconnected with the Midwest ISO's transmission

utility has the authority to apply the general criteria and issue the specific order to curtail load without any Commission involvement in the process. Similarly, in connection with the O & I proposal, the CAISO has identified the “general” criteria it will apply to determine whether a specific type of behavior constitutes Detrimental Practices or Market Manipulation (see EP 4.7); the CAISO additionally would apply such general criteria and determine whether “specific” behavior should be prohibited. The Commission would not be involved in the latter process, just like the Commission does not determine whether a public utility can issue a particular curtailment order.

Moreover, the Commission has authorized natural gas pipelines to issue operational flow orders (“OFOs”), in response to the existence of operating conditions that may affect services provided by the pipeline, directing shippers to take or refrain from specific actions. Natural gas pipelines can impose penalties on shippers that do not follow pipeline issued OFOs.⁴³ As the Commission has explained:

OFOs generally restrict service or require shippers to take particular actions. For instance, an OFO can reduce or eliminate tolerances for imbalances or contract overruns; institute severe penalties; or restrict intra-day nominations, the use of secondary receipt and delivery points, or firm storage withdrawals. Penalties are designed to deter shippers from creating imbalances, or from overrunning contract entitlements, and include penalties for physical imbalances (differences between commodity input and output), scheduling imbalances (differences between actual and scheduled quantities), and non-compliance with OFO and other tariff provisions.⁴⁴

In response to new conditions that arise, natural gas pipelines are authorized to issue OFOs on an as-needed basis. For example, pipelines may issue OFOs upon a determination that action(s) is necessary for the following reasons: to alleviate conditions which threaten the integrity of the transporter’s system; to maintain pipeline operations at the pressures required to provide reliable firm services; to have adequate supplies in the system to deliver on demand (including injection of gas into the mainline, providing line pack and injecting gas into storage at the right place and right time); to maintain and

system. See Midwest ISO OATT, FERC Electric Tariff, Second Revised Volume No. 1, Original Sheet Nos. 58-60 and 70.

⁴³ See *Regulation of Short-Term Natural Gas Transportation Services, and Regulation of Interstate Natural Gas Transportation Services*, Order No. 637, 66 Fed. Reg. 10,156 (Feb. 25, 2000), FERC Stats. & Regs., Regs. Preambles ¶¶ 31,091, at 31,307 (2000) (“Order No. 637”). See also, e.g., Dominion Transmission, Inc., FERC Gas Tariff, Third Revised Volume No. 1, at Original Sheet No. 1065 to Original Sheet No. 1091 (tariff provisions concerning OFOs).

⁴⁴ Order No. 637 at 31,307.

protect the integrity and performance capability of the transporter's storage fields; to maintain firm service to all shippers; and to maintain the system in balance for the foregoing purposes.⁴⁵ Thus, pipeline Tariffs identify the general criteria that a pipeline can consider in determining whether to issue an OFO. The pipeline issues OFOs via a market notice directing shippers to take or refrain from taking specific actions. The pipeline does not require Commission approval to issue a specific OFO.

The general criteria specified in pipeline OFO Tariff provisions are comparable in substance and specificity to the general criteria in EP 4.7 that the CAISO will apply to determine whether specific behavior constitutes Detrimental Practices and Market Manipulation and should be prohibited. Just as a natural gas pipeline will issue a market notice directing shippers to take specific actions or refrain from specific actions, so too will the CAISO issue a market notice – indeed, two market notices – prohibiting Detrimental Practices and Market Manipulation. In both instances, the Commission does not need to approve the specific action taken by the regulated company. Thus, the CAISO's proposed procedures for prohibiting Detrimental Practices and Market Manipulation are similar to the procedures which the Commission has approved for the issuance of OFOs by natural gas pipelines. Indeed, the CAISO's proposed procedures place even stricter limits on the exercise of discretion because the CAISO will follow a two-notice process and will provide the Commission with copies of such notices. Thus, the Commission will have an opportunity to intervene in instances where it disagrees with the CAISO's exercise of discretion, but no such opportunity for intervention exists in the OFO process. Under these circumstances, there should not be any concern about the CAISO exercising discretion.⁴⁶

⁴⁵ See Columbia Gas Transmission Corporation, FERC Gas Tariff, Second Revised Volume No. 1, at Second Revised Sheet No. 380.

⁴⁶ The CAISO notes that there are other provisions in the ISO Tariff that permit the CAISO to make "adjustments" to the treatment of entities, subject to the requirement that the "adjustments" be published under the ISO Home Page, but *not* subject to any requirement that such "adjustments" be filed with the Commissions and commented on by market participants. For example, Sections 10.5.2 of the ISO Tariff (concerning ISO Metered Entities) and 10.6.9 of the ISO Tariff (concerning Scheduling Coordinator Metered Entities) both provide that the CAISO has the authority to grant exemptions from certain CAISO metering standards provided that the CAISO annually publishes details of the criteria the CAISO will use when considering an application for an exemption and details of specific exemptions which are available. These provisions allow the CAISO to exempt metered entities from meeting all of the usual requirements for such entities, and allow the CAISO grant the exemption without a public comment period being necessary. Additionally, the Eligible Intermittent Resources Protocol ("EIRP") provides that, subject to a rate cap, the CAISO has full discretion to set the rate applicable to Participating Intermittent Resources and to determine the required duration of their commitment, so long as the CAISO publishes this information under the ISO Home Page. EIRP 2.4.1 provides that, "[b]eginning on the date first certified, a Participating Intermittent Resource must pay the Forecast Fee for all metered Energy generated by the Participating Intermittent Resource over the duration of the commitment indicated in the letter of intent described in EIRP 2.2.1(c)." EIRP 2.2.1(c), in

C. The Investigation and Enforcement Process

Under the Enforcement Protocol, the CAISO will have the authority to investigate any activity, event, or occurrence that the CAISO believes might constitute a violation of any Rule of Conduct set forth in the EP. With respect to the investigation process generally, the CAISO will follow certain procedures that will apply to possible violations of all of the Rules of Conduct.

As a general matter, potential Rule of Conduct violations may be identified based on a variety of activities, including routine monitoring of market data by the CAISO, referrals of anomalous market behavior, or questions from the Oversight and Enforcement Agencies, other regulatory agencies, and Market Participants. The CAISO reviews all logged events of non-compliance with the obligations described in the ISO Tariff, e-mails directed to "Compliance Notifications," and records any other direct referrals by telephone or e-mail.

After a potential Rule of Conduct violation has been identified, and after the CAISO has determined that no specific automated penalty procedure is applicable, the CAISO will conduct a reasonable investigation seeking available facts, data, and other information relevant to the suspected violation. EP 3.2. The CAISO will provide appropriate notice to the affected Market Participant and provide an opportunity for the Market Participant to present data, information, and/or written comment relevant to the event or behavior being investigated. EP 3.3, 3.4. The CAISO will notify the Market Participant of the results of the investigation. EP 3.5. Where the investigation results in a penalty or sanction, the CAISO will state its findings and conclusions in writing, and will make such writing available to the affected Market Participant(s). EP 3.6.

Where the results of the investigation demonstrate that a Rule of Conduct has been violated, the CAISO will take appropriate penalty or sanction action as outlined in the EP. The CAISO may also refer any matter under investigation to an Oversight and Enforcement Agency. Where the CAISO makes such a referral, it will notify the affected Market Participant of the referral and will make

turn, states that the CAISO will specify the form of the letter of intent and publish it under the ISO Home Page. In specifying the form of the letter of intent, the CAISO will specify the duration of the commitment, which is an essential term of the relationship with the Participating Intermittent Resource. As to the rate charged to a Participating Intermittent Resource for the Forecast Fee (defined in EIRP 1.2.2), EIRP 2.4.1 explains that the CAISO may set the initial rate and make such changes to the rate "as may be necessary from time to time to recover costs incurred by the ISO for the forecasting conducted on behalf of Participating Intermittent Resources," so long as the rate is posted under the ISO Home Page and does not exceed the rate cap specified in the ISO Tariff, Appendix F, Schedule 4. In sum, the CAISO has discretion to set the rate (subject to the rate cap) and the duration of commitment, and must publish this information under the ISO Home Page, but the CAISO is not required to obtain public comment concerning its decision. As with these provisions, there should be no requirement that the CAISO's filing of market notices be made subject to a public comment period.

available to the affected Market Participant the data and other information provided to the Oversight and Enforcement Agency. The foregoing is subject to the limitations set forth in Section 20.3 of the ISO Tariff. EP 3.7.

The CAISO notes that the Enforcement Protocol specifies that the activities and remedies authorized under the protocol are in addition to any other actions or relief that may be available to the CAISO elsewhere in the ISO Tariff or under law, regulation, or order. Moreover, nothing in the Enforcement Protocol limits the right of the CAISO to take action or seek relief otherwise available to it, and such action or relief may be pursued in lieu of or in addition to the action or relief specified in the protocol. EP 1.8.

A number of these procedures that the CAISO proposes in the EP relating to the investigation and enforcement of the Rules of Conduct are similar to the procedures adopted by ISO-NE for investigations of possible rules violations. See ISO-NE MRP 13.6. Moreover, the level of detail provided in the CAISO's procedures is similar to the level of detail contained in the ISO-NE procedures.

D. Penalty Provisions

1. Penalty Levels

Once the CAISO has determined that a Market Participant has violated a Rule of Conduct, the CAISO must determine the appropriate amount of any penalty to be imposed. Additionally, the CAISO may seek to have some other type of sanction(s) imposed against the Market Participant. EP 5.7. Similarly, the Commission may impose either a penalty or some other appropriate remedy when it acts *sua sponte* to enforce the provisions of the Enforcement Protocol.

The amounts (including maximum amounts) of the penalties, and the methodologies for determining such amounts, are consistent with the following directives enunciated by the Commission in the SMD NOPR:

[s]ince the tariff rules are intended to ensure the fair and efficient operation of the markets, the penalties should be designed to deter conduct that is inconsistent with fair and efficient operation of the markets. Specifically, the penalties should deter conduct that results in an economic benefit derived from a violation of the rules. The penalties should, at a minimum, require payment of the economic benefit derived by the violator from violating the rules. Where the violation could result in conduct that could be harmful to the reliability of the grid, it would be appropriate for the penalty to be significantly higher to serve as a deterrent for the conduct. The Independent Transmission Provider must specify the conditions that would apply for each level of penalty.

SMD NOPR at P 455. The penalties set forth in the EP are designed to ensure that a Market Participant that engages in prohibited behavior will not receive an economic benefit from so doing, and to deter Market Participants from engaging in the behavior. These penalties – which are stiffer than the options available today to the CAISO and the Commission under the MMIP– should serve as a more effective deterrent.

2. Penalty Determination Factors

As described above and in Sections 2.2 through 2.10 of the Enforcement Protocol, each Rule of Conduct entails nominal maximum levels for penalties. Section 5.1 of the Enforcement Protocol specifies that the CAISO will determine the penalty amount for a violation of Rules of Conduct by first calculating the maximum amount of the penalty as set forth in Sections 2.2 through 2.10, and as may be enhanced by Section 5.3 of the Enforcement Protocol. The CAISO will then determine the specific penalty amount to be assessed, up to the maximum amount, by considering various factors. Among the factors the CAISO may consider are the following: the degree to which the violation may have affected System Reliability or market integrity; the degree to which the Market Participant benefited from the violation; the frequency and duration of the violation; any cumulative effect of multiple penalties applying to a single event; and the extent to which the Market Participant failed to act on opportunities or information allowing the Market Participant to make efforts to rectify or ameliorate the violation. EP 5.1(a), -(c), -(g), -(h), -(n), and -(o).

The Commission previously has approved tariff provisions that contain factors similar to many of the factors proposed by the CAISO in Section 5.1 of the Enforcement Protocol. For example, ISO-NE MRP 13.6.2.2(a) and NMISA MR 7.6.2.2(a) contain provisions similar to factors (d), (k), and (p). ISO-NE MRP 13.5.1 and 13.6.2.2(b), and NMISA MR 7.5.1 and 7.6.2.2(b), contain provisions similar to factor (n). PX Schedule 10, Section 5.4.2 contains provisions similar to factor (f). PX Section 10, Section 5.4.3 contains provisions similar to factor (g). PX Schedule 10, Section 5.4.5 contains provisions similar to factor (i). ISO-NE MRP 13.4.2.4(a) and NMISA MR 7.4.2.3(a) are similar to factor (r). Finally, ISO-NE MRP 13.4.2.4(b) and NMISA MR 7.4.2.3(b) are similar to factor (s).

In addition, the SMD NOPR identifies the following standards that could be applied for adjusting the levels of penalties: the impact on the operation of the grid; the financial impact on the violator; and any good faith efforts to maintain compliance. SMD NOPR at P 456. Factors (c), (d), (k), (r), and (s) in Section 5.1 of the Enforcement Protocol are consistent with these standards. The CAISO stresses that there are many more factors specified under the O & I proposal than there are specified in the SMD NOPR. Thus, the CAISO is providing

greater protections to Market Participants and an increased likelihood that penalties imposed will be fair and take into account all relevant factors

In addition, as described in Section 5.2 of the Enforcement Protocol, the following circumstances may excuse a violation of a Rule of Conduct under the Enforcement Protocol: (1) circumstances in which Uncontrollable Force was a factor; (2) circumstances in which the Market Participant is able to demonstrate that it was Section 2.3.1.2.1 of the ISO Tariff; (3) circumstances in which the Market Participant is able to demonstrate that it was acting in good faith and consistent with Good Utility Practice to preserve System Reliability in a System Emergency or other system disturbance, unless contrary to an CAISO operating order; and (4) circumstances in which the act or omission giving rise to the apparent violation was specifically required by a Commission order or CAISO operating instruction. Section 5.2 is similar to provisions in ISO-NE MRP 13.4.6 and NMISA MR 7.4.5.

As described in Section 5.3 of the Enforcement Protocol, the CAISO may triple the nominal maximum amount of any fixed penalty stated for a violation of Sections 2.2 to 2.10 of the Enforcement Protocol, in the following circumstances: (1) if the violation occurs during a System Emergency; or (2) if the CAISO determines that the violation is part of a continuing pattern of the same violation for which one or more monetary penalties have previously been imposed upon the Market Participant. (However, penalties under Section 2.2(c) will not be subject to such enhancement.) The CAISO notes that the Commission authorized both ISO-NE and the NMISA to impose administrative penalties up to triple the base amount of the penalty under circumstances similar to those proposed by the CAISO. See ISO-NE MRP 13.5.3 and NMISA MR 7.5.3. The CAISO submits that in instances where a violation could result in conduct that could be harmful to the reliability of the grid, it is appropriate for the penalty to be significantly higher to serve as a deterrent for the conduct. Indeed, in the SMD NOPR, the Commission proposes higher penalties in such circumstances. SMD NOPR at P 455.

3. Applying Penalty Amounts

Under Section 5.4 of the Enforcement Protocol, penalties imposed as a result of engaging in prohibited behavior will be assessed through Preliminary and Final Settlement Statements issued to the responsible Scheduling Coordinator by the CAISO, and the CAISO will provide a description of the penalty to the Scheduling Coordinator before invoicing the amount of that penalty through the Settlement process with the exception of penalties assessed through automated algorithms. The description will include the identity of the Market Participant that committed the violation, a description of the violation, the amount of the penalty, and a description of any application of mitigating or enhancing factors. Section 5.4 of the Enforcement Protocol also states that the CAISO also

will publish this information under the ISO Home Page after Final Settlement Statements are issued.

Although the CAISO intends to use final Settlement data for any publication of penalties or Rule of Conduct violations, there remains a possibility that the CAISO's dispute resolution process will modify penalties or violations that are reported based on final Settlement data. Where final Settlement statements are modified based on resolution of a dispute in a way that mitigates the violation or penalty, then the CAISO will publish a correction.

4. Dispute Resolution and Appeal

A Market Participant that disputes a penalty will have an initial opportunity to request CAISO review of the penalty via its Scheduling Coordinator, through the routine Preliminary Settlement Statement validation and dispute process as set forth in Section 11.7.2 of the ISO Tariff. If the CAISO denies the dispute, a Market Participant can pursue a claim by initiating ADR review through its Scheduling Coordinator. This would be done in accordance with the ADR Procedures set forth in the ISO Tariff. See EP 3.10, 5.4. Finally, the Market Participant may ultimately appeal to the Commission any award resulting from the ADR procedures. See Section 13.4 of the ISO Tariff. The CAISO also notes that none of the proposed Tariff provisions limit a Market Participant's rights to file complaints directly with the Commission under Section 206 of the Federal Power Act. Thus, any Market Participant incurring a penalty would have more than adequate opportunity for review of such penalty to ensure that the penalty has not been arbitrarily, capriciously, and/or discriminatorily imposed.

5. Use of Penalty Proceeds

The CAISO proposes that any penalty amounts it collects under the Enforcement Protocol be distributed to Scheduling Coordinators, after first subtracting reasonable costs incurred by the CAISO for payments to vendors for equipment or services that are used to investigate violations of Rules of Conduct and administer penalties described in the EP. The CAISO will hold the collected penalty amounts in a trust account until the end of each calendar year. At the end of each year, and after subtracting the reasonable costs incurred as described above, the CAISO will allocate the remainder, including accrued interest, to Scheduling Coordinators in proportion to their Metered Demand (including exports) in the calendar year. Any amounts paid in respect of penalties that are not allocated amongst Scheduling Coordinators in proportion to their metered Demand (including exports) will be credited to the Surplus Account. These proposals will be implemented pursuant to a new Section 3.1.2 of the Settlement and Billing Protocol ("SABP") and revisions to Sections 3.1.1 and 6.5.2 of the SABP.

This approach provides equitable compensation to the Market Participants that may be harmed as a result of any violations of Rules of Conduct, namely those Market Participants in the ISO Control Area that consume and pay the costs of energy and ancillary services. Violations of Rules of Conduct adversely impact market efficiency, thereby increasing the costs to the end-customers of the energy and ancillary services products purchased in the CAISO's markets. Distributing penalty amounts in proportion to Scheduling Coordinators' Metered Demand provides an equitable method to compensate these Market Participants because Metered Demand represents (1) Load, which consumes both Energy and Ancillary Services, and (2) exports from the ISO Control Area which consume Ancillary Services.

This approach does not provide the CAISO with any incentive to impose penalties in order to reduce its Grid Management Charge ("GMC"). As explained above, the CAISO proposes to recover via this mechanism only those payments to outside vendors for equipment or services that the CAISO acquires or utilizes in connection with the investigation of violations of the Rules of Conduct described in the Enforcement Protocol and the administration of penalties. These costs would be incremental to the costs that currently comprise the GMC. The CAISO would not attempt to recover costs related to the Uninstructed Deviation Penalties proposed as part of MD02 or costs related to the current No-Pay and Committed Period penalties. The CAISO's proposal would merely hold GMC constant, all other factors being equal, and equitably recover the costs of enforcing Rules of Conduct from the Market Participants that violate them.

Because the CAISO will recover investigation and penalty administration costs from a pool of all fines it collects, it will not have any incentive – or any mechanism – to recover excessive costs from a particular Market Participant. In addition, this methodology avoids the administrative burden of tracking the costs of individual investigations, preparing invoices, and potentially having to justify and negotiate costs billed to specific Market Participants.

The CAISO's proposal is comparable to measures the Commission has previously approved for other independent system operators. For example, ISO-NE market rules provide that payments of penalties received will be reflected as a credit to charges under the ISO-NE tariff for market participants other than the penalized participant, allocated in proportion to total charges under the tariff in the month the payment is received. ISO-NE Market Rule 13.6.3. The market participant is required to pay the amount of the penalty or post a bond for the amount of the penalty to ISO-NE if the participant is seeking review of the penalty under the ADR process within 30 days of the date of ISO-NE's invoice. *Id.*

ISO-NE also has a provision in its market rules which provides that, if a monetary penalty is imposed, ISO-NE may charge the penalized market participant "the reasonable costs of the ISO's investigation" of the market

participant's behavior. Moreover, such costs will be payable after the deadline for requesting ADR has passed and any requested ADR proceedings are complete. ISO-NE Market Rule 13.5.4. Further, the ISO-NE market rules provide that the costs of the ADR process will be assessed to the market participant if the penalty is affirmed, to ISO-NE if the penalty is removed, and apportioned by the ADR decision maker among the parties if the sanction is reduced. Costs assessed to ISO-NE are automatically included in ISO-NE's budget. ISO-NE Market Rule 13.7.6.6.

The NMISA has a provision in its market rules similar to that found in ISO-NE Market Rule 13.6. See NMISA Market Rule 7.6.3. The NMISA market rules provide that any monetary penalties collected by the NMISA "will be used to reduce the ISA expenses charged to Market Participants." NMISA Market Rule 7.5.4. Similarly, the NYISO market rules provide that, except for one type of penalty charge, penalty amounts will be credited against costs collectable under Rate Schedule 1 of the NYISO Services Tariff. See NYISO Market Mitigation Plan, Section 4.3.6.

The CAISO's proposed treatment of penalty revenues is reasonable and contains adequate protections to preclude the CAISO from imposing penalties for the purpose of covering CAISO costs. Consistent with the authority the Commission has granted other independent transmission providers and market operators, the Commission should approve the CAISO's proposed Tariff provisions regarding the treatment of penalty revenues.

V. TARIFF AND PROTOCOL CHANGES TO ADDRESS ADDITIONAL TYPES OF PROHIBITED MARKET BEHAVIOR

The CAISO is proposing several modifications to the main body of the Tariff, to address additional types of prohibited market behavior. The new language, which is discussed in greater detail below, will be included in the main body of the Tariff and not in the new Enforcement Protocol because many of the provisions pertain to bidding and scheduling matters are addressed in the Tariff.

A. Scheduling on Zero-Rated Transmission Paths

One type of scheduling "game" identified in the Enron memos occurs where a Scheduling Coordinator submits schedules and/or adjustment bids across a tie point that had been de-rated to zero capacity in hopes of getting paid for providing a counter-flow schedule that would need to be cut by the CAISO in real time. This "game," which was referred to as "Wheel Out" by the Enron traders, was "played" by Scheduling Coordinators other than just Enron. The extent and impact of the "Wheel Out" game in California is discussed in greater detail in the October 4 Report which is contained herein as Attachment D. In the

Show Cause Order, the Commission explained that "Wheel Out" constitutes a prohibited gaming practice. See Show Cause Order at P 44.

The CAISO's Day-Ahead and Hour-Ahead Congestion Management program ("CONG") currently does not allow the CAISO to reject or cancel schedules across a tie point that has been de-rated to zero transmission capacity. Instead, when a tie point is de-rated to zero capacity, the CAISO sets the available capacity for the tie point in the CONG software to approximately zero.⁴⁷ When the CONG software is run, the software adjusts schedules as necessary to achieve the result of a net zero scheduled flow across the tie point. For example, if schedules are submitted that create a net flow in one direction, the CONG software will seek to offset this flow by accepting adjustment bids for counter-flows in the opposite direction and/or reduce initial scheduled flows based on adjustment bids. As discussed in the Enron memos, this creates a potential gaming opportunity for Market Participants when a tie point is known to be out of service. Specifically, because Scheduling Coordinators can schedule on zero-rated paths, Scheduling Coordinators, knowing that such schedules will be canceled by the CAISO in real time, can profit from such schedules by submitting schedules to provide counter-flows across a tie point or adjustment Bids that the CONG software will use to "relieve" the Congestion (i.e., reduce the net flow across the path to zero). In the case where the tie point was de-rated to zero capacity, there will be congestion in the Hour-Ahead congestion markets. Thus, any Scheduling Coordinators providing counter-flow schedules to relieve this congestion will be paid counter-flow revenues.⁴⁸

Thus, while the "Congestion" – which never really existed because no Energy could have flowed across the path to begin with – is "relieved" by the counter-flow, the physically impossible Schedule across the zero-rated path remains. To adhere to WECC requirements, it is necessary for the CAISO operations staff to eliminate this physically impossible Schedule before real time. Real money changes hands and real staff time must be expended to eliminate a Schedule that could never have been delivered in the first place.

To remedy the problems caused by scheduling on zero-rated transmission paths, the CAISO proposes to prohibit Scheduling Coordinators from submitting Schedules on known zero-rated paths, reject Day-Ahead Schedules submitted

⁴⁷ The CAISO's scheduling system currently does not have a minimum level of operating transfer capability (i.e., zero) at or below which it rejects Schedules. In practice, the available capacity for lines that are out is set at .03 MW in order to facilitate computation by the CONG software in a more timely manner.

⁴⁸ In real time, when a tie point is de-rated to zero, the CAISO effectively removes this tie-point from the transmission system by canceling all schedules on the tie-point during the final real time inter-tie checkout prior to each operating hour. However, any Congestion charges and payments associated with the Day-Ahead and Hour-Ahead congestion management process are not canceled or reversed from the CAISO settlement system.

on such paths, and require Scheduling Coordinators, if time permits, to zero out any Schedules on transmission path(s) in the Hour-Ahead Market if the path rating(s) are reduced to zero after Final Day-Ahead Schedules are issued. Further, as necessary to comply with Applicable Reliability Criteria, the CAISO proposes to reduce any non-zero Final Hour-Ahead Schedules across zero-rated transmission paths to zero after the close of the Hour-Ahead Market. No Usage Charges will be assessed, nor will any Usage Charges for counter-flow be paid, for Schedules across a path with an Operating Transfer Capability of zero. The CAISO proposes the addition of Section 2.2.9 to the ISO Tariff, as well as the addition of the defined term "Operating Transfer Capability" to Appendix A of the ISO Tariff, to effect these changes. Moreover, as part of its MD02 comprehensive market redesign, the CAISO intends to modify the CONG software to reject Schedules on tie-lines that are out of service at the time the Day-Ahead and Hour-Ahead Congestion Management markets are run. Engaging in the "Wheel-Out" practice may also be considered a violation of the Rules of Conduct concerning Detrimental Practices and Market Manipulation, and will be reported to the appropriate Oversight and Enforcement Agencies.

The CAISO's proposal herein – which will eliminate inappropriate gaming opportunities – is consistent with WECC requirements and good utility practice prohibit the scheduling of an amount of power across a transmission path that exceeds the operating transfer capability of that path.⁴⁹ WECC practice further prohibits scheduling power across de-energized facilities or scheduling across another entity's facilities without the entity's consent.⁵⁰

B. The Hour-Ahead Ancillary Services Buy-Back Price

The current ISO Tariff and Scheduling Protocols clearly indicate that sales of Ancillary Service schedules in the Day Ahead market represent "binding commitments" for physical capacity and that "the ISO will require SCs to honor their Day-Ahead Ancillary Services schedules."⁵¹ However, in the event an Scheduling Coordinator does not honor these binding commitments and instead submits an Hour Ahead Ancillary Service schedule lower than the final Day Ahead schedule awarded by the CAISO, the Tariff currently provides that

⁴⁹ The WECC Minimum Operating Reliability Criteria ("MORC") direct that "No elements within the interconnection shall be scheduled above continuous operating limits." *WECC Minimum Operating Reliability Criteria*, Section 3.B.1.

⁵⁰ The WECC procedures explain that "Skip scheduling is not an accepted practice and will not be allowed. Skip scheduling consists of either or both of the following: Scheduling across de-energized facilities [or] [s]cheduling across another entity's facilities without its knowledge or consent." *WECC Scheduling Procedures for all Entities Involved in Interchange Scheduling, Minimum Requirements for Scheduling*, at ¶ 6.

⁵¹ See Section 2.5.21 of the ISO Tariff, Section 5.3 of the Schedules and Bids Protocol ("SBP"), and Sections 9.1 and 9.3 of the Scheduling Protocol ("SP").

participants bear the cost of replacing this capacity in the Hour-Ahead Market.⁵² Unfortunately, this settlement provision has been abused through a variety of trading practices which, in effect, treat commitments made in the CAISO's Day-Ahead Ancillary Services market simply as financial positions that may be used to speculate on differences in Day-Ahead and Hour-Ahead Ancillary Services, rather than as binding commitments to provide physical reserve capacity.

In this filing, the CAISO proposes to modify Section 2.5.21 of the ISO Tariff, Section 5.3 of the SBP, and Sections 9.1 and 9.3 of the SP to set the price for Ancillary Services sold in the Day-Ahead Market and "bought back" by the participant in the Hour-Ahead Market to the greater of the Day-Ahead Market Clearing Price or Hour-Ahead Market Clearing Price for the relevant Ancillary Service. The primary purpose of this modification is to eliminate the practice dubbed as "Get Shorty" by Enron, and referred to as "Paper Trading" in the Commission's Show Cause Order.⁵³ Under this strategy, participants anticipating that Hour-Ahead Ancillary Service prices may be lower in than Day Ahead Market prices sell Ancillary Service capacity they do not have in the Day-Ahead Market, knowing that they can "zero out" these commitments in the Hour-Ahead Market and thereby receive a net credit from the CAISO equal to the difference in prices in these two markets. The Commission's Show Cause Order found that this practice represents a violation of the MMIP since participant engaged in this practice "unfairly took advantage of the market rules by using false representations and/or receiving payments for services that they did not provide."⁵⁴

The modifications being made eliminate the ability of participants to profit through such "Paper Trading," while protecting suppliers in instances where the resources committed to provide Ancillary Services in the Day-Ahead Market become unavailable prior to the Hour-Ahead Market. In such cases, if the Day-Ahead price is higher than the Hour-Ahead price, then the supplier merely pays back what it was initially paid. If the Hour-Ahead price is higher than the Day-Ahead price, the supplier pays the price to replace the service that it no longer can provide. The supplier cannot profit from its misfortune, nor is the supplier unduly penalized for it.

⁵² In practice, the Tariff does not actually allow participants to "buy back" Ancillary Services, but simply specifies settlement terms for cases in which participants do not "honor" their Day Ahead Schedules by unilaterally reducing (or completely "zeroing out") these commitments in Hour Ahead Schedules submitted to the CAISO (i.e., by submitting an Hour Ahead Ancillary Service Schedule to the CAISO that is zero, or otherwise less than the resources Final Day Ahead Schedule for that Ancillary Service.

⁵³ See Show Cause Order at PP 48-51. See also October 4 Report at 20-23, and discussion of Enron games in Section II, *supra*.

⁵⁴ Show Cause Order at P 51 (footnote omitted).

In the absence of this relatively simply settlement modification, the ability of the CAISO and other legal and regulatory entities to detect "Paper Trading" would, as a practical matter, continue to be extremely limited and administratively burdensome. The difficulty detecting "Paper Trading" stems, in part, from the fact that virtually all Day-Ahead Ancillary Services commitments that are canceled prior to the Hour-Ahead Market are imports to the CAISO system by marketers (rather than utilities or generators directly operating physical resources).⁵⁵ For imports of Ancillary Services, suppliers only identify the Control Area rather than the actual physical resources backing these commitments. Detection of "Paper Trading" is further hindered – and sometimes even made impossible – by the fact that the actual availability of Day-Ahead Ancillary Services commitments that are reduced or cancelled in the Hour-Ahead Market cannot be subsequently be tested or verified after-the fact. Thus, as a practical matter, the settlement modification being made represents the only reliable means of deterring the practice of "Paper Trading."

In addition to eliminating the financial incentive for "Paper Trading" of non-existent resources, this tariff revision also eliminates the ability of participants with physical resources that could provide Ancillary Services to sellers to profit through "arbitrage" during periods when prices in the Day-Ahead Ancillary Services markets may be systematically higher than Hour-Ahead prices. The Commission's Show Cause Order indicates that such behavior is "consistent with legitimate arbitrage" if the participant actually has the capacity being sold in the Day-Ahead Market.⁵⁶ However, as described below, the CAISO believes this practice represents an abuse of the current settlement provisions for Day-Ahead Ancillary Services commitments which negatively impacts system reliability, and believes the Commission's conclusion that this is "consistent with legitimate arbitrage" is based on the erroneous premise that the CAISO's Day-Ahead and Hour-Ahead Ancillary Services markets are simply "financial markets" for a single "fungible commodity," rather than separate markets for two distinct physical products.

As noted above, the ISO Tariff and Scheduling Protocols clearly indicate that sales of Ancillary Services Schedules in the Day-Ahead Market represent "binding commitments" for physical capacity and that "the ISO will require SCs to honor their Day-Ahead Ancillary Services schedules." The rationale for this language is twofold. First, Ancillary Services capacity is a physical commitment (or product) that is essential to meet the demand for system reliability, rather than simply a "financial position" for a "commodity." Secondly, due to various

⁵⁵ For example, all Ancillary Services that were "bought back" over the 2000-2001 period covered in the CAISO's most recent report on the Enron strategies were imports, the bulk of these "buy backs" involve participants who are primarily marketers (Enron, Sempra, Coral, and Avista) rather than utilities or generators directly operating physical resources. See July Report, Tables 5 and 6, page 18.

⁵⁶ See Show Cause Order at P 64.

constraints and characteristics of resources that comprise the supply of Ancillary Services, Ancillary Services commitments procured by the CAISO on a Day-Ahead basis are not directly “fungible” with commitments procured by the CAISO on a Hour-Ahead basis. For instance, due to the lead times and scheduling requirements necessary ensure that many resources can be available to provide reserve capacity in real time, the CAISO must purchase the bulk of its Ancillary Services requirements on a Day-Ahead basis in order to ensure that sufficient supply of such unloaded capacity is procured. Thus, capacity procured on the Day-Ahead and the Hour-Ahead basis are two distinct physical products, offering different degrees of system reliability. Although the CAISO conducts an Hour-Ahead Market for Ancillary Services, the CAISO purchases the bulk of its Ancillary Services requirements in a Day-Ahead Market to ensure system reliability.

While the CAISO seeks to lower its purchase costs by deferring some portion of its Ancillary Services purchases from the Day Ahead to the Hour-Ahead Market when Hour-Ahead prices are lower, the CAISO must limit the portion of Ancillary Services capacity purchased in the Hour-Ahead Market due to uncertainty about the available supply of reserve capacity on an Hour-Ahead basis, even if the prices in the Hour-Ahead Market may be systemically lower than Day-Ahead prices. When participants seek from profit from such prices differences by canceling commitments made in the Day-Ahead Market, the direct impact of this “arbitrage” is to require the CAISO procure a higher portion of its reliability requirements in the Hour-Ahead Market. While this may represent a source of profit for marketers who engage in this practice, the net result of this practice is to reduce the CAISO’s ability to manage system reliability and costs through its Ancillary Services procurement decisions.

C. Cut Counter-flow Schedules

A general type of scheduling practice described in the Enron memos is where Scheduling Coordinators submit Schedules in the Day-Ahead and/or Hour-Ahead congestion markets, providing counter-flows on a congested path. These schedules receive Congestion charges that are ultimately paid by Scheduling Coordinators with Schedules in the congested direction as counter-flow revenue in the Day-Ahead and/or Hour-Ahead congestion markets. Under existing CAISO scheduling and Settlement practices, Scheduling Coordinators may subsequently cut the counter-flow Schedules immediately prior to real time, but such Scheduling Coordinators will still receive the counter-flow revenues for the schedules submitted in the Day-Ahead and/or Hour-Ahead congestion markets. In other words, a Scheduling Coordinator may receive Congestion payments for counter-flows scheduled in the Day-Ahead and/or Hour-Ahead Congestion Management markets, even though these counter-flow Schedules are reduced or cut in real time. This scheduling practice is made possible by a market design flaw and is perpetuated by the inability of System Resources to

set Market Clearing Prices. Although differential prices are calculated today in the forward congestion management markets, a single Imbalance Energy price applies in real time. Under MD02, this design flaw is corrected, and System Resources are proposed to be eligible to set prices. However, until MD02 is fully implemented, a measure such as that proposed here is necessary.

Because the CAISO pays for Congestion relief provided by scheduled counter-flows, this creates a potential gaming opportunity for Scheduling Coordinators to sell Congestion relief in the forward markets and then to cut the counter-flow Schedule after the close of the Hour-Ahead Market. Although in many cases counter-flow Schedules are due to circumstances that are unforeseeable and beyond the control of a Scheduling Coordinator (i.e., they are not the product of gaming), a financial inequity occurs every time a counter-flow Schedule is cut or reduced because Congestion payments are made for counter-flows that are not delivered in real time. It is not appropriate to pay Scheduling Coordinators for services that are not actually rendered. Moreover, in the Show Cause Order, the Commission agreed that Cutting Non-firm, also known as Non-firm Export, is a prohibited gaming practice. See Show Cause Order at P 42. Accordingly, the CAISO is proposing Tariff revisions to address this issue.

Specifically, the CAISO proposes to amend Section 7.3.1.5.2 of the ISO Tariff to provide that, when a Schedule in the counter direction of Congestion is not delivered, to the extent that any Scheduling Coordinator would receive a Usage Charge payment for Energy that was scheduled in a counter direction over an inter-tie in the Day-Ahead or Hour-Ahead Market but was not delivered in real time, that Usage Charge payment will be eliminated, pro rata, based on the difference between the scheduled counter-flow in the Hour-Ahead Market, and the final real-time Schedule in the counter direction.⁵⁷ This amendment is

⁵⁷ The amendment does not eliminate the payment of Usage Charges on internal interfaces (e.g. Paths 15 and 26) due to the fact that any Imbalance Energy charges resulting from cancellation of export or import Schedules are already priced in a manner that essentially subjects Scheduling Coordinators to a net Imbalance Energy charge that reflects any actual real-time Congestion existing over these internal interfaces. For example, if an export Schedule on an external intertie from NP15 is cut, along with a corresponding import schedule into SP15, this would create a positive real-time imbalance within NP15 and a negative real-time imbalance in SP15. The positive imbalance in NP15 would be paid the decremental real-time price in NP15, while the negative imbalance in SP15 would be charged at the incremental price in SP15. Thus, during periods of north-to-south Congestion, when these initial Schedules would have created a counter-flow on the zonal interfaces within the CAISO system (Paths 15 and 26) in the forward Congestion Management process, the Scheduling Coordinator would be subject to a net real time imbalance charge equal to the difference between the decremental price in NP15 and a higher incremental price in SP15, reflecting the relative price in these two Zones due to Congestion. Thus, while the Scheduling Coordinator may continue to receive a Congestion payment for the counter-flow created by the Scheduling Coordinator's forward Schedules, the Scheduling Coordinator would be charged a net Imbalance Energy charge that reflects any actual real-time Congestion that exists over these internal interfaces.

designed to reduce or eliminate the potential reliability problems, gaming opportunities, and settlement inequities that may result when scheduled counter-flows are reduced or cut in real time. The proposed Tariff amendment addresses these concerns while avoiding the potential disputes and administrative burdens associated with any alternative rule that might rely on case-by-case determinations of "fault" or "gaming" based on the circumstances underlying each scheduled counter-flow Schedule that is cut in real time. Instead, the amendment eliminates any incentive to cut counter-flow Schedules intentionally. In this regard, the CAISO's proposal is consistent with the settlement consequence under Tariff Section 7.3.1.5.2 for undelivered counter-flows on internal paths.

The proposed Tariff change is more analogous to the elimination of payment for services not provided, rather than a penalty. However, if such behavior is systematic and part of a gaming strategy, then eliminating the Usage Charges for service not provided might not be a sufficient deterrent. Under such circumstances, the CAISO may elect to open an investigation into gaming as described above in Section IV.B.

D. Noncompliance with Operating Orders

In order to ensure that system reliability is maintained, the CAISO must be certain that Market Participants will comply with the operating orders the CAISO issues. The CAISO believes that the ISO Tariff, in particular Section 2.3.1.2, already requires Market Participants to comply with CAISO operating orders. In order to re-affirm that CAISO operating orders must be followed, the CAISO proposes to modify Section 2.3.1.2.1 to state that all System Resources are required to comply with the CAISO's operating orders. In addition, the Enforcement Protocol will set forth specific penalties that may apply to non-compliance with CAISO operating orders. The CAISO also proposes to modify Section 2.3.1.2.1 to provide that Final Hour-Ahead Schedules for Energy for Generating Units, System Resources, System Units, and Curtailable Demand are deemed to be operating orders and, as such, these Schedules are binding obligations and must be fulfilled unless otherwise directed by the CAISO. The proposed Tariff changes also provide that any Hour-Ahead Ancillary Services Schedule or Supplementary Energy Bid is a binding obligation, and a resource so scheduled or bid cannot be made unavailable or otherwise fail to respond to CAISO operating orders, except for conditions beyond the control of the resource owner. Finally, the CAISO proposes to revise Section 2.3.1.2.1 to provide that any Day-Ahead commitment of a resource, either self-scheduled or committed in

Similarly, if an export Schedule on an external intertie from NP15 is cut without a corresponding cut in an import Schedule into SP15, this would create a positive real-time imbalance within the Zone in which the export Schedule was cut (NP15), so that the Scheduling Coordinator would deliver Energy to the higher priced congested Zone (SP15), but would receive the lower decremental price paid for Energy in NP15.

a Day-Ahead Market, is a binding obligation, and a resource so scheduled cannot be de-committed or otherwise made unavailable except for conditions beyond the control of the resource owner or as approved by the CAISO.⁵⁸ The CAISO proposes to impose penalties, under the Enforcement Protocol, on Market Participants that violate Section 2.3.1.2.1. See EP 2.2.

E. Circular Schedules

Another type of scheduling practice that is addressed in the Enron memos is commonly referred to as "Circular Schedules" or "Circular Scheduling." The "Death Star" trading strategy made famous in the Enron memos is one particular form of a Circular Schedule.⁵⁹ In general, Circular Schedules are sets of schedules on two or more Tie-Points between different Control Areas or Zones that create a closed loop flow of Energy that does not have a separate generation source and load in the ISO Control Area or another Control Area.⁶⁰ The entire purpose of the Circular Schedule is to collect Congestion revenues from the creation of counter-flows.

Unfortunately, because of the circular nature of the generation source and load of a Circular Schedule, such Schedules may make it more difficult for the CAISO grid operators to manage the actual power flows on the system by adjusting import and export Schedules in real time. As such, they potentially can

⁵⁸ The CAISO submitted similar changes to Section 2.3.1.2.1 of the ISO Tariff in its June 17, 2002 filing in the MD02 proceeding. See Transmittal Letter for June 17, 2002 MD02 Filing, Docket Nos. ER02-1656-003, *et al.*, at 26-29, and Appendix A to June 17, 2002 MD02 Filing at 205-06. However, the Commission has deferred taking action on most components of the June 17, 2002 filing, including the proposed changes to Section 2.3.1.2.1. See *California Independent System Operator Corporation*, 100 FERC ¶ 61,060, at 61,257-58 (2002). These Tariff provisions are crucial to the CAISO's reliable operation of the transmission grid, and the Commission should approve such provisions in its order on the instant filing rather than continuing to defer consideration of such provisions.

⁵⁹ The "Death Star" strategy involved scheduling Energy in the opposite direction of Congestion in the Day-Ahead without actually injecting Energy into or taking Energy off of the grid in real time, yet receiving a separate Congestion payment.

⁶⁰ These schedules appear as an import and export through the ISO Control Area, but actually include additional schedules outside of the ISO Control Area (or back through the ISO Control Area through another Scheduling Coordinator) which form a closed loop of scheduled Energy with no specific source or sink. In that regard, one schedule would be a "wheel through" whereby a Scheduling Coordinator schedules power into the CAISO at one point and then out of the CAISO at another point. If there were Congestion in the other direction, this schedule would have the effect of relieving such Congestion, for which the CAISO would pay the Scheduling Coordinator. The second schedule is between the same two locations but is in the opposite direction and is scheduled outside of the ISO Control Area (or back through the ISO Control Area through another Scheduling Coordinator with existing transmission rights, which allow Energy to be scheduled in the same direction of Congestion without paying Congestion charges). The second schedule cancels the flows of the first schedule. However, the CAISO still makes the payment for relieving congestion even though the flows of the first schedule that relieve congestion are offset by the second schedule.

adversely affect system reliability. In the Show Cause Order, the Commission explained that Circular Scheduling constitutes a prohibited gaming practice. See Show Cause Order at P 43.

The CAISO proposes a number of changes to the Tariff and Protocols specifically to address the problems caused by circular schedules. First, the CAISO proposes a new defined term, Circular Schedule, to be included in the Master Definitions Supplement to the Tariff.⁶¹ Second, the CAISO proposes new Tariff Section 7.3.1.5.3 to provide that Scheduling Coordinators will not receive a Usage Charge payment for scheduled flows in a counter direction if such scheduled flow is the result of a Circular Schedule. Third, the CAISO proposes new Section 2.1.7 of the SBP to prohibit Scheduling Coordinators from submitting Circular Schedules, and to explain that the CAISO may periodically provide examples of Circular Schedules under the ISO Home Page.

As described in Section 2.7(c)(iii) of the Enforcement Protocol, engaging in a Circular Schedule subjects a Market Participant to the rescission of the Usage Charge in accordance with Section 7.3.1.5.3, and an additional maximum penalty equal to the value of the Usage Charge so rescinded. Engaging in a Circular Schedule may also be considered a violation of the Rules of Conduct concerning Detrimental Practices and Market Manipulation, and will be reported to the appropriate Oversight and Enforcement Agencies.

VI. COORDINATION WITH OVERSIGHT AND ENFORCEMENT AGENCIES AND RELATED CHANGES TO TARIFF CONFIDENTIALITY PROVISIONS

A. Coordination with Oversight and Enforcement Agencies

The CAISO seeks to coordinate with the Oversight and Enforcement Agencies in order to make them aware of violations of Rules of Conduct that also might constitute violations of other laws. For example, pursuant to Section 5.7 of the Enforcement Protocol, the CAISO, in its discretion, may refer the actions of a Market Participant to the Oversight and Enforcement Agencies,⁶² and recommend that those agencies impose additional sanctions upon the Market Participant on a going-forward basis. Coordination with the Oversight and

⁶¹ *Inter alia*, the definition provides that a closed loop of Energy Schedules that includes a transmission segment on the Pacific DC Intertie shall not be a Circular Schedule because such a Schedule directly changes power flows on the network and can mitigate Congestion between SP15 and NP15.

⁶² In order to describe these agencies in a term contained in the EP, the CAISO proposes the term "Oversight and Enforcement Agency," to mean any of the following: the Commission, the United States Department of Justice or any of its subsidiaries, the California Department of Justice or any of its subsidiaries, the CPUC, or the EOB.

Enforcement Agencies should serve as an additional deterrent to improper behavior and provide additional assurance that possible violations of Rules of Conduct, including those having to do with Detrimental Practices and Market Manipulation, are identified, investigated, corrected, and eliminated. The CAISO recognizes that the behavior of Market Participants may be subject to investigation and possible responsive action by the Oversight and Enforcement Agencies, even where the CAISO's Rules of Conduct do not address that behavior. The ability of the Oversight and Enforcement Agencies to deter such behavior can only be increased through the sharing of information by the CAISO. Further, as indicated above, other independent system operators have Commission-approved market monitoring plans enabling them to consult with interested government agencies regarding the need for further investigations or actions necessary to achieve the purposes of their respective market monitoring plans. On the other hand, the CAISO acknowledges that its sharing of information with the Oversight and Enforcement Agencies should be subject to appropriate provisions to ensure that the confidential information of a Market Participant that is the subject of a referral by the CAISO is safeguarded to the greatest possible extent.

The CAISO plans to increase coordination with Oversight and Enforcement Agencies by providing them access to timely market data on an ongoing basis. To provide timely access to CAISO data, the CAISO proposes to create a secure data repository or "regulatory data server." This data server will contain raw market and operational data delayed only a day or so to allow the CAISO generally to check the integrity of the raw data, and will be updated daily. The raw data will be made available to agencies having statutory oversight and enforcement authority.⁶³ Thus, these agencies will have access to the same raw data that the CAISO's DMA relies on for its market and other analyses. The availability of this data will for the first time provide the agencies the mechanism to monitor the performance of the energy market and observe trends on a near real time basis, rather than wait for monthly data productions.

The CAISO also proposes to provide confidential information to the Oversight and Enforcement Agencies in the course of investigations conducted under the O & I process described in Section IV of this transmittal letter. The CAISO will provide to the agencies monthly reports of CAISO investigations (conducted in accordance with the procedures described above in Section IV of

⁶³ Access to the regulatory server data will also be provided, subject to adequate confidentiality safeguards being established, to Commission Staff in Folsom. Depending on the requirements identified, the "regulatory server" may simply involve a procedure for pushing data (including bids, metered quantities, market quantities and prices, and system conditions) to the agencies via a file transfer protocol, with provision for periodic corrections as required. Alternatively, a secure web-based data repository that would support menu-driven downloads of data may be developed, depending on the cost of such a design and cost recovery arrangements.

this transmittal letter), including the current status, planned activities, and penalties that might be under consideration. These reports will cover all events that the CAISO determines require additional investigation based on an initial review of the facts. Because these reports will be based on incomplete investigations, the CAISO believes that these periodic reports on CAISO investigations should be treated as confidential information by the agencies. In addition, the CAISO will inform the Oversight and Enforcement Agencies of the final disposition of each reported investigation.

B. Necessary Revisions to Tariff Confidentiality Provisions

In order to allow the CAISO to provide confidential data to Oversight and Enforcement Agencies as discussed above, the CAISO proposes to add Section 20.3.5 to the ISO Tariff. These provisions have been drafted after giving careful consideration to comments that Market Participants provided on the conditions under which confidential information is shared. Under new Section 20.3.5, the CAISO may disclose information otherwise required to be maintained in confidence under the Tariff to an Oversight and Enforcement Agency. Proposed Section 20.3.5(a) provides that the CAISO may make disclosures of information to an Oversight and Enforcement Agency on a routine or periodic basis, with or without advance notice to Market Participants, if all of the following requirements have been met: (1) the CAISO has identified each category of information that it intends to disclose to an Oversight and Enforcement Agency in a market notice issued at least thirty days in advance of the disclosure; (2) each category of information that the CAISO proposes to disclose is of a type wherein each Market Participant has access to that portion of the information pertaining to it contemporaneous with the disclosure, through each Market Participant's systems or records; (3) the proposed disclosure relates to the CAISO markets as a whole and is comprised of information on all Market Participants for which such information is available to the CAISO; and (4) each Oversight and Enforcement Agency to which the CAISO makes such disclosure is bound legally to treat the information as confidential under terms no less protective than the requirements stated in Section 20.3.5(c).

Proposed Section 20.3.5(b) provides that the CAISO may disclose any information required to be maintained in confidence under the Tariff to an Oversight and Enforcement Agency, without meeting the requirements of Section 20.3.5(a), if certain specified requirements have all been met. The CAISO must have a reasonable belief that a violation has occurred and that the information is relevant to the investigation. Further, the agency to which the information is provided must have authority over the potential violation, and must be legally bound to treat the information as confidential. Finally, the ISO must provide five business days' advance notice to the Market Participant of the disclosure, unless such notice would jeopardize the investigation.

Section 20.3.5(c) provides that each of the Oversight and Enforcement Agencies to which information is disclosed under Section 20.3.5 must be bound, at a minimum, to a legal obligation that set forth in writing the terms applicable to the treatment of confidential and/or commercially sensitive information, and that obligates the agency not to disclose to any third party information provided under the section without providing written notice to the CAISO and the affected Market Participant at least five business days in advance of the intended date of release. Section 20.3.5(c) further provides that the Market Participant may, at its sole discretion and own cost, direct any challenge to or defense against the proposed disclosure and the CAISO must cooperate as provided in Section 20.3.4(b). Finally Section 20.3.5(d) provides that nothing in Section 20.3.5 will limit the ability of an Oversight and Enforcement Agency to seek information in accordance with the provisions of Section 20.3.4(b), nor the ability of the CAISO to disclose information in accordance with that section.

The CAISO requests that the Commission approve these provisions for the defined Oversight and Enforcement Agencies in recognition of the role and enforcement responsibilities that such agencies have at the federal and state level. For example, the Oversight and Enforcement Agencies have been investigating market transactions for various types of unlawful behavior that fall within such agencies' jurisdiction, including, but not limited to, fraud, antitrust violations, and unfair business practices.⁶⁴ The CAISO expects that timely access to market data provided through the regulatory server will increase the CAISO's ability to share information and responsibility with the Oversight and Enforcement Agencies. The creation of the regulatory server will also make the data available the Oversight and Enforcement Agencies much closer to real time, which will enhance their monitoring capabilities.

Proposed Section 20.3.5 provides greater protections to Market Participants than do the existing provisions of the ISO Tariff. In that regard, under Section 20.3.4(b), if the CAISO is required to provide confidential information in the course of an ongoing judicial or administrative proceeding, the CAISO may publicly disclose such information upon notification to the affected Market Participant. The CAISO is not required to wait a specified period of time after notifying such Market Participant before it can release the requested confidential information. However, under Section 20.3.5(c), at least five business days prior written notice to the CAISO and the affected Market Participant is required before an Oversight and Enforcement Agency may release confidential information to the public. This provides Market Participants with (1) an additional protection not found in the existing Tariff and (2) adequate opportunity to challenge the public disclosure of confidential information. Further, under Section 20.3.5(a), one of the requirements that must be met before information

⁶⁴ The EOB, by statute, has oversight responsibility over the operations and activities of the CAISO.

will be provided to each Oversight and Enforcement Agency is that the agency must be bound legally to treat the information as confidential under terms no less protective than the requirements stated in Section 20.3.5(c) pursuant to a written agreement that sets forth appropriate protections for the treatment of confidential information.

The CAISO's proposed information dissemination proposal is generally modeled after the disclosure provisions of the New England Power Pool ("NEPOOL") Information Policy which have been approved by the Commission.⁶⁵ Thus, the Commission has already found similar disclosure provisions to be just and reasonable. Similarly, the Midwest ISO's market monitoring plan permits the Midwest ISO's market monitoring unit to "bring any matter to the attention of interested government agencies as the IMM may deem necessary to achieve the purposes, objectives and effective implementation of the Market Monitoring Plan." *Midwest Independent Transmission System Operator, Inc.*, 99 FERC ¶ 61,237 at 61,977 (2002). Likewise, PJM's market monitoring plan permits PJM's market monitoring unit to consult with authorized government agencies regarding the need for specific investigations and enables PJM to provide confidential information to such agencies subject to the protection of such confidential information and the confidentiality of any ongoing investigation. *The New Power Company v. PJM Interconnection, Inc.*, 98 FERC ¶ 61,208 (2002). These market monitoring plans recognize the need for market monitoring units to have an effective means of coordinating with other oversight and enforcement agencies in order to monitor market behavior effectively. The CAISO is requesting similar authority. Such authority is especially appropriate for the CAISO given the extensive gaming and market manipulation that has occurred in the CAISO's markets over the past couple of years. Finally, the CAISO notes that the NYISO has a mechanism in place whereby it provides confidential information to the New York Public Service Commission ("NYPSC") – subject to specified non-disclosure protections – in order to enable the NYPSC to perform its statutory responsibilities more effectively.

VII. CHANGES TO THE EXISTING MMIP

The changes the CAISO proposes to the MMIP fall into four basic categories. First, the CAISO proposes a number of "housekeeping" revisions to the MMIP in order to correct certain outdated and erroneous references in the MMIP. These changes include the following:

⁶⁵ See *New England Power Pool*, 95 FERC ¶ 61,105 (2001); *New England Power Pool*, 95 FERC ¶ 61,248 (2001).

-- The CAISO has eliminated references in the MMIP to the PX, and instead has substituted, where appropriate, references to "other power markets or exchanges."

-- The CAISO has changed all of the MMIP's references to the Market Surveillance Unit ("MSU") into references to the DMA.⁶⁶

-- The CAISO has changed all references to "ISO Participant" into references to "Market Participant."

Second, the CAISO proposes several revisions to the MMIP in order to ensure consistency with the Enforcement Protocol. These revisions include the following:

-- The CAISO has eliminated the use of the defined term "Activity Rule" in the MMIP. See MMIP 1.2.2. The term "Rule of Conduct," as used in the EP, is substituted where appropriate.

-- The CAISO has added cross-references to the Enforcement Protocol. See EP 1.2.3.1.

-- The CAISO has added the Market Surveillance Committee ("MSC") to the group of entities to which the MMIP applies. See MMIP 1.3.1.3.

-- The MMIP now explains that the MMIP provides a general framework for the operation of the DMA and the MSC and is not intended to limit the activities or remedies available to these entities. See MMIP 1.1.

-- The process for publication of information has been modified. See MMIP 8.

-- Minor changes have been made to Appendix A to the MMIP.

Third, the CAISO proposes several minor modifications to the structure and responsibilities of the DMA, including the following:

-- The DMA shall be under the general management of the ISO CEO or his or her designee. See MMIP 3.

-- The DMA may make recommendations for Rules of Conduct changes and other actions through the ISO CEO and Governing Board. See MMIP 4.

⁶⁶ The MSU is the former name of the DMA.

Fourth and finally, the CAISO proposes several modifications involving the authority and responsibilities of the MSC, which include the following:

- The role of the MSC in regulatory and legal proceedings has been clarified. See MMIP 5.
- The process for implementation of recommendations in MMIP has been modified, so that this process applies specifically to the MSC. See MMIP 7.

VIII. EFFECTIVE DATE

For the changes described in this Amendment No. 55, the CAISO requests an effective date of sixty days after the submission of the present filing, or September 20, 2003, in accordance with the provisions of 18 C.F.R. § 35.3 (2003).

IX. COMMUNICATIONS

Communications regarding this filing should be addressed to the following individuals, whose names should be placed on the official service list established by the Secretary with respect to this submittal:

Charles F. Robinson
Anthony J. Ivancovich
Gene Waas
California Independent
System
Operator Corporation
151 Blue Ravine Road
Folsom, CA 95630
(916) 608-7135

David B. Rubin
Bradley R. Miliauskas
Michael Kunselman
Swidler Berlin Shereff
Friedman, LLP
3000 K Street, N.W., Suite 300
Washington, D.C. 20007
(202) 424-7516

X. SERVICE

The CAISO has served this filing on the California Public Utilities Commission, the California Energy Commission, the California Electricity Oversight Board, and all parties with effective Scheduling Coordinator Service Agreements under the ISO Tariff. In addition, the CAISO has posted a copy of the filing under its Home Page.

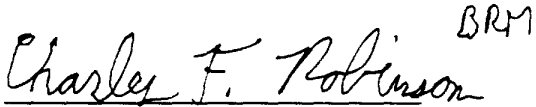
XI. SUPPORTING DOCUMENTS

The following documents, in addition to this transmittal letter, support this filing:

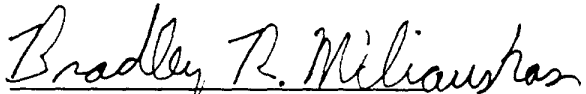
- Attachment A: Table of Contents for this transmittal letter
- Attachment B: Enforcement Protocol
- Attachment C: Revised Tariff sheets reflecting proposed changes
- Attachment D: Revised Tariff sheets in black-line format
- Attachment E: Background and Stakeholder Process Timeline
- Attachment F: A form of notice of this filing suitable for publication in the Federal Register (also provided in electronic format)

If there are any questions concerning this filing, please contact the undersigned.

Respectfully submitted,

 ^{BRM}

Charles F. Robinson
Anthony J. Ivancovich
Gene Waas
California Independent System
Operator Corporation
151 Blue Ravine Road
Folsom, CA 95630



David B. Rubin
Bradley R. Miliauskas
Michael Kunselman
Swidler Berlin Shereff Friedman, LLP
3000 K Street, N.W., Suite 300
Washington, D.C. 20007

Counsel for the California Independent System Operator Corporation

ATTACHMENT A

**Table of Contents
for Amendment No. 55
Transmittal Letter**

	<u>Page</u>
I. INTRODUCTION	2
II. NEED FOR THE O & I PROGRAM.....	5
A. The California Electricity Crisis and Initial Commission Response	5
B. Documentation of Gaming and Market Manipulation	6
C. Inadequacy of Commission and CAISO Authority.....	14
D. Relationship Between O & I and Market Redesign	18
E. Conclusion	21
III. OVERSIGHT AND INVESTIGATION PROGRAM OVERVIEW.....	22
A. Program Objectives.....	22
B. Elements of O & I Program	24
C. Stakeholder Process	27
D. Actions Requested of the Commission	28
IV. THE ENFORCEMENT PROTOCOL.....	30
A. The Basic Rules of Conduct.....	30
1. Summary of Each Rule.....	31
a. Compliance with Operating Orders.....	31
b. Submission of Feasible Energy and Ancillary Service Bids and Schedules	33
c. Physical Withholding.....	34

**Table of Contents
for Amendment No. 55
Transmittal Letter
(Continued)**

	<u>Page</u>
d. Economic Withholding	35
e. Compliance with Availability Reporting Requirements	36
f. Factual Accuracy Requirement.....	37
g. Compliance with Obligations to Provide Information Required by the ISO Tariff	39
2. The Rules of Conduct are Consistent with the Proposed Standard Market Design and Other Commission Initiatives.....	40
3. The Rules Are Consistent with Commission Staff Recommendations	43
4. The Rules are Consistent with Commission-Approved “Best Practices”	44
B. Detrimental Practices and Market Manipulation.....	44
1. Summary of the Rules.....	44
2. Safeguards.....	45
C. The Investigation and Enforcement Process.....	53
D. Penalty Provisions.....	54
1. Penalty Levels	54
2. Penalty Determination Factors	55
3. Applying Penalty Amounts.....	56
4. Dispute Resolution and Appeal	57
5. Use of Penalty Proceeds	57

**Table of Contents
for Amendment No. 55
Transmittal Letter
(Continued)**

	<u>Page</u>
V. TARIFF AND PROTOCOL CHANGES TO ADDRESS ADDITIONAL TYPES OF PROHIBITED MARKET BEHAVIOR	59
A. Scheduling on Zero-Rated Transmission Paths	59
B. The Hour-Ahead Ancillary Services Buy-Back Price	61
C. Cut Counter-flow Schedules.....	64
D. Noncompliance with Operating Orders	66
E. Circular Schedules	67
VI. COORDINATION WITH OVERSIGHT AND ENFORCEMENT AGENCIES AND RELATED CHANGES TO TARIFF CONFIDENTIALITY PROVISIONS.....	68
A. Coordination with Oversight and Enforcement Agencies	68
B. Necessary Revisions to Tariff Confidentiality Provisions.....	69
VII. CHANGES TO THE EXISTING MMIP.....	72
VIII. EFFECTIVE DATE	74
IX. COMMUNICATIONS	74
X. SERVICE	74
XI. SUPPORTING DOCUMENTS	75

ATTACHMENT B

ISO Enforcement Protocol

ISO ENFORCEMENT PROTOCOL

Table of Contents

EP 1	OBJECTIVES, DEFINITIONS, AND SCOPE	860
EP 1.1	Purpose	860
EP 1.2	Objectives	860
EP 1.3	Master Definitions Supplement	860
EP 1.4	Special Terms for This Protocol	861
EP 1.5	Rules of Interpretation	861
EP 1.6	Scope	862
EP 1.7	Liability of ISO	862
EP 1.8	Application of Other Remedies	862
EP 1.9	FERC Authority	862
EP 2	RULES OF CONDUCT	862
EP 2.1	Purpose	862
EP 2.2	Comply with Operating Orders	863
EP 2.3	Submit Feasible Energy and Ancillary Service Bids and Schedules	864
EP 2.4	No Physical Withholding	864
EP 2.5	No Economic Withholding	864
EP 2.6	Comply With Availability Reporting Requirements	865
EP 2.7	Provide Factually Accurate Information	865
EP 2.8	Provide Information Required by ISO Tariff	866
EP 2.9	No Detrimental Practices	866
EP 2.10	No Market Manipulation	867
EP 3	PROCESS FOR INVESTIGATION AND ENFORCEMENT GENERALLY	867
EP 3.1	Purpose; Scope	867
EP 3.2	Investigation	868
EP 3.3	Notice	868
EP 3.4	Opportunity to Present Evidence	868
EP 3.5	Results of Investigation	868
EP 3.6	Statement of Findings and Conclusions	868
EP 3.7	Referral to Oversight and Enforcement Agencies	868

EP 3.8	Officer Representative	869
EP 3.9	Record of Investigation	869
EP 3.10	Review of Notice	869
EP 4	PROCESS FOR PROHIBITING DETRIMENTAL PRACTICES AND MARKET MANIPULATION	869
EP 4.1	Scope	869
EP 4.2	General Process	869
EP 4.3	Preliminary Market Notice	
EP 4.4	Formal Warning	870
EP 4.5	Cease and Desist Directive	870
EP 4.6	Final Market Notice	871
EP 4.7	Criteria for Making Determination	871
EP 4.8	Penalties; Other Actions	872
EP 5	ADMINISTRATION OF PENALTIES	872
EP 5.1	Assesment; Factors to be Considered	872
EP 5.2	Excuse	873
EP 5.3	Enhancement	874
EP 5.4	Settlement	874
EP 5.5	Disposition of Proceeds	874
EP 5.6	Time Limitation	875
EP 5.7	Other Sanctions	875
EP 6	NO LIMITATIONS ON OTHER RIGHTS OF ISO	875
EP 7	AMENDMENTS	875

ISO ENFORCEMENT PROTOCOL ("EP")

EP 1 OBJECTIVES, DEFINITIONS, AND SCOPE

EP 1.1 Purpose

This Protocol sets forth the rules pursuant to which the ISO will vigilantly monitor markets operated by the ISO and vigorously enforce clearly specified Rules of Conduct in order to (a) ensure to the extent possible reliable operation of the transmission grid, (b) promote dependable, effectively functioning, efficient, fair and competitive markets, (c) operate markets that produce just and reasonable prices for consumers, and (d) deter behavior by Market Participants that is inconsistent with these goals.

EP 1.2 Objectives

The objectives of this Protocol are to provide:

- (a) Clear Rules of Conduct specifying inappropriate behavior by Market Participants;
- (b) A deterrent to Market Participants from engaging in Detrimental Practices, Market Manipulation, and other activities that are inappropriate and inconsistent with the Rules of Conduct;
- (c) A process for specifying by market notice or Formal Warning additional activities that violate certain Rules of Conduct;
- (d) Appropriate penalties for Rule of Conduct violations;
- (e) An appropriate process for the ISO to monitor and investigate activities that might violate the Rules of Conduct;
- (f) An appropriate process for referrals to Oversight and Enforcement Agencies; and
- (g) An appropriate process for levying applicable penalties for violations, including reasonable accommodation for circumstances or events beyond a Market Participant's control.

EP 1.3 Master Definitions Supplement

Unless the context otherwise requires, any word or expression defined in the Master Definitions Supplement to the ISO Tariff shall have the same meaning where used in this Protocol. References to a Section or Appendix are to a section of or an appendix to the ISO Tariff. References to EP are to this Protocol or to the stated section or paragraph of, or appendix to, this Protocol.

EP 1.4 Special Terms for This Protocol

In this Protocol, the following words and expressions shall have the meanings set opposite them:

- (a) **"Detrimental Practices"** has the meaning set forth in EP 2.9(a).
- (b) **"FERC"** means the Federal Energy Regulatory Commission.
- (c) **"Final Market Notice"** has the meaning set forth in EP 4.6.
- (d) **"Formal Warning"** has the meaning set forth in EP 4.4.
- (e) **"Market Manipulation"** has the meaning set forth in EP 2.10(a).
- (f) **"Net Excess Load"** has the meaning set forth in EP 2.7(c).
- (g) **"New Behavior"** has the meaning set forth in EP 4.2.
- (h) **"Oversight and Enforcement Agency"** means any of the following: FERC, the United States Department of Justice or any of its subsidiaries, the California Department of Justice or any of its subsidiaries, the California Public Utilities Commission, or the California Electricity Oversight Board.
- (i) **"Participant Benefits"** has the meaning set forth in Appendix A to this Protocol.
- (j) **"Preliminary Market Notice"** has the meaning set forth in EP 4.3.
- (k) **"Rules of Conduct"** has the meaning set forth in EP 2.

EP 1.5 Rules of Interpretation

Unless the context otherwise requires, if the provisions of this Protocol and the ISO Tariff conflict, the ISO Tariff will prevail to the extent of the inconsistency. Provisions of the ISO Tariff have been summarized or repeated in this Protocol only to aid understanding.

A reference in this Protocol to a given agreement, ISO Protocol, or instrument shall be a reference to that agreement or instrument as modified, amended, supplemented, or restated through the date as of which such reference is made.

The captions and headings in this EP are inserted solely to facilitate reference and shall have no bearing upon the interpretation of any of the terms and conditions of this Protocol.

This Protocol shall be effective as of the date specified by FERC.

EP 1.6 Scope

The EP governs:

- (a) All Market Participants; and
- (b) The ISO.

EP 1.7 Liability of ISO

Any liability of the ISO arising out of or in relation to this Protocol shall be subject to Section 14 of the ISO Tariff as if references to the ISO Tariff were references to this Protocol.

EP 1.8 Application of Other Remedies

The activities and remedies authorized under this Protocol are in addition to any other actions or relief that may be available to the ISO elsewhere in the ISO Tariff or under law, regulation or order. Nothing in this Protocol limits or should be construed to limit the right of the ISO to take action or seek relief otherwise available to it, and such action or relief may be pursued in lieu of or in addition to the action or relief specified in this Protocol.

EP 1.9 FERC Authority

In addition to the ISO, FERC shall have the authority to assess the penalties specified herein, and otherwise to enforce the rules set forth in this Protocol, independently or by referral or complaint of another entity, and additionally shall have the authority to impose penalties equal to the market impact of a violation under this Protocol. In undertaking such action, FERC shall not be bound by the notice procedures and other processes set forth in EP 3 and EP 4. Specifically, FERC shall have authority to remedy a violation under this Protocol from the date of the violation. Nothing in this Protocol shall be deemed to be a limitation or condition on the authority of FERC or other entities under current law or regulation.

EP 2 RULES OF CONDUCT

EP 2.1 Purpose

These Rules of Conduct are designed to serve as guiding principles as to the standard of behavior that is expected of Market Participants and to provide a summary of types of activities for which a Market Participant might be subject to enforcement action. The ISO will enforce these Rules of Conduct through the provisions specified in EP 2.2 through EP 2.10. Events that may constitute violations shall be treated according to the standards and evaluation factors set forth in EP 3 and EP 4.

EP 2.2 Comply with Operating Orders

- (a) **General Rule.** Market Participants must comply with operating orders issued by the ISO.
- (b) **Standard Penalty.** Unless otherwise provided below, a violation of this rule is subject to a maximum penalty of \$10,000 per event **and** allocation of any WECC RMS penalty incurred by the ISO due to such event (pursuant to Section 2.5.26.5 of the ISO Tariff) **and** an amount equal to the Market Clearing Price multiplied by any quantity of energy called for in the operating order that was not provided.

Examples of events that may constitute a violation of the general rule and that are subject to the standard penalty include (but are not limited to) the following:

- Failure of a Market Participant to comply with any operating order issued by the ISO pursuant to Section 2.3.1.2.1 of the ISO Tariff, unless excused for reasons of public health or safety, or other reasons set forth in this Protocol (but see EP 2.2(d)).
 - Failure of a Generating Unit, System Unit, or System Resource owned or controlled by a Participating Generator without a bid for available Generation to comply with an order to start-up, increment, or decrement output pursuant to Section 5.6.1 of the ISO Tariff.
 - Failure by a Must-Offer Generator to operate a Generating Unit on-line and at minimum load so that it is capable of providing all of its available capacity in compliance with the must-offer obligation, as set forth in Sections 5.11 *et seq.* of the ISO Tariff, unless such a unit has been granted a waiver or exception pursuant to Section 5.11.6 of the ISO Tariff.
- (c) **Special Penalties.**
- (i) Failure of a UDC to implement an order issued by the ISO to curtail Load in order to manage a System Emergency, pursuant to Section 4.5.3 and Section 2.3.1.2.1 of the ISO Tariff, is subject to a maximum penalty of \$110,000 per event **and** an amount equal to \$1,000 per megawatt-hour of firm load not curtailed).
- (ii) Any failure to comply with an operating order that contributes to or prolongs an outage as described in Section 2.3.2.9.3 of the ISO Tariff is subject to a maximum penalty of \$110,000 per event **and** allocation of any WECC RMS penalties incurred by the ISO due to such event (pursuant to Section 2.5.26.5 of the ISO Tariff).

- (d) **Exception.** Violations of this rule that are subject to the Uninstructed Deviation Penalty under Section 11.2.4.1.2 of the ISO Tariff are subject to penalty under this rule only to the extent that the ISO has issued a separate and distinct non-automated Dispatch Instruction to the Market Participant.

EP 2.3 Submit Feasible Energy and Ancillary Service Bids and Schedules

- (a) **General Rule.** Market Participants must bid and schedule Energy and Ancillary Services from resources that are available and capable of performing at the levels specified in the bid and/or schedule.
- (b) **Standard Penalty.** Subject to the exceptions below, a violation of this rule is subject to a maximum penalty of \$10,000 per event.
- (c) **Exceptions.** Violations of this rule for which an Uninstructed Deviation Penalty under Section 11.2.4.1.2 of the ISO Tariff has been assessed or for which payments under Section 2.5.26 of the ISO Tariff have been eliminated are not subject to penalty under this section.

EP 2.4 No Physical Withholding

- (a) **General Rule.** Market Participants may not engage in physical withholding of the output of a Generating Unit, in whole or in part. "Physical withholding" for purposes of this rule means a failure to offer to sell or to schedule into the ISO Market the output of or services of a Generating Unit capable of serving an ISO market, in a manner consistent with the ISO Tariff.
- (b) **Standard Penalty.** Subject to the exception below, a violation of this rule is subject to a maximum penalty of \$25,000 per event **and** an amount equal to twice the Participant Benefits received by the offending party as a result of such behavior.
- (c) **Exception.** Behavior otherwise falling within this rule that is the particular focus of another provision in the ISO Tariff specifically designed to address such behavior (e.g., Appendix A to the MMIP) is not subject to penalty under this section.

EP 2.5 No Economic Withholding

- (a) **General Rule.** Market Participants may not engage in economic withholding of the output of a Generating Unit. "Economic withholding" for purposes of this rule means:
- submitting a bid for a Generating Unit that is not consistent with the bid caps or thresholds specified in the ISO Tariff or any applicable agreement; **or**

- submitting a bid for a Generating Unit that is unjustifiably high (relative to known operational characteristics and/or the known operating cost of the resource) and the Generating Unit is not or will not be dispatched or scheduled, or the bid (which is unjustifiably high) will set a Market Clearing Price.
- (b) **Standard Penalty.** Subject to the exception below, a violation of this rule is subject to a maximum penalty of \$25,000 per event and an amount equal to twice the Participant Benefits received by the offending party as a result of such behavior.
- (c) **Exception.** Behavior otherwise falling within this rule that is the particular focus of another provision in the ISO Tariff specifically designed to address such behavior (e.g., the Automated Mitigation Procedure set forth in Appendix A to the MMIP) is not subject to penalty under this section.

EP 2.6 Comply With Availability Reporting Requirements

- (a) **General Rule.** Market Participants must comply with all reporting requirements governing the availability and maintenance of a Generating Unit or transmission facility, including proper Outage scheduling requirements. The responsible entity (Scheduling Coordinator or Participating Transmission Owner) must immediately notify the ISO when capacity changes or resource limitations occur that affect the availability of the unit or facility or the ability to comply with Dispatch Instructions.
- (b) **Standard Penalty.** Subject to the exception below, a violation of this rule is subject to a maximum penalty of \$10,000 per event.
- (c) **Exception.** Violations of this rule for which an Uninstructed Deviation Penalty under Section 11.2.4.1.2 of the ISO Tariff has been assessed are not subject to penalty under this section.

EP 2.7 Provide Factually Accurate Information

- (a) **General Rule.** All applications, Schedules, reports, and other communications by a Market Participant or agent of a Market Participant to the ISO, including maintenance and outage data, bid data, transaction information, and load and resource information, must be submitted by a responsible company official who is knowledgeable of the facts submitted. All such information submitted must be true, complete, and consistent with the operational plans of the company to the best knowledge of the person submitting the information.
- (b) **Standard Penalty.** Unless otherwise provided below, a violation of this rule is subject to a maximum penalty of \$10,000 per event.

(c) **Special Penalties.**

- (i) Submitting Load Schedules that are substantially in excess of metered Load served by a Scheduling Coordinator is subject to a maximum penalty equal to the Net Excess Load multiplied by the applicable Market Clearing Price. For purposes of this section, Net Excess Load means the amount by which scheduled Load exceeds actual load plus a reasonable tolerance band established by the ISO from time to time and posted under the ISO Home Page.
- (ii) Failing to provide complete and accurate Settlement Quality Meter Data, as provided in Section 10 of the ISO Tariff and Section 4.1 of the Meter Service Agreement, that results in an error that is discovered after issuance of Final Settlement Statements is subject to penalties described in Appendix A to the EP.
- (iii) Engaging in a Circular Schedule is subject to the rescission of the Usage Charge in accordance with Section 7.3.1.5.3 of the ISO Tariff and an additional maximum penalty equal to the value of the Usage Charge so rescinded.

EP 2.8 Provide Information Required by ISO Tariff

- (a) **General Rule.** All information that is required to be submitted to the ISO under the ISO Tariff, its protocols, or jurisdictional contracts must be submitted in a complete, accurate, and timely manner. Market Participants must comply with requests for information or data by the ISO that are consistent with the ISO Tariff, including timelines specified in the ISO Tariff for submitting Schedules and other information.
- (b) **Standard Penalty.** Except as otherwise provided below, a violation of this rule is subject to a maximum penalty of \$500 for each day that the required information is late.
- (c) **Special Penalties.** Failure to provide timely information in response to written requests by the ISO for information reasonably necessary to conduct an investigation, or in response to an audit authorized by the ISO Tariff, subject to a maximum special penalty of \$1,000 per day that the requested information is late (first violation); \$2,500 per day (second violation by the same Market Participant within a rolling three-year period); \$5,000 per day (subsequent violations by the same Market Participant within a rolling three-year period).

EP 2.9 No Detrimental Practices

- (a) **General Rule.** Market Participants shall not engage in Detrimental Practices as defined in this rule. "Detrimental Practices" for purposes of this rule shall mean behavior that meets both of the following requirements:

- Such behavior takes unfair advantage of the rules and procedures set forth in or pursuant to the ISO Tariff to the detriment of System Reliability, other Market Participants, or the efficiency of the ISO Market; **and**
 - Such behavior or behavior substantially similar to it has been proscribed in a Final Market Notice in accordance with the procedures outlined in EP 4.6.
- (b) **Standard Penalty.** A violation of this rule is subject to a maximum penalty of \$25,000 per event **and** an amount equal to twice the Participant Benefits received by the offending party as a result of such behavior.
- (c) **Limitation.** No penalty may be assessed by the ISO under this rule until such behavior or behavior substantially similar to it has been proscribed in a Final Market Notice in accordance with the procedures outlined in EP 4.6.

EP 2.10 No Market Manipulation

- (a) **General Rule.** Market Participants shall not engage in Market Manipulation, which is behavior that meets both of the following requirements:
- Such behavior is fraudulent, deceptive, or manipulative and is intended to create artificial or distorted market prices or outcomes, including prices or outcomes that do not reflect or are not consistent with supply and demand conditions; **and**
 - Such behavior or behavior substantially similar to it has been proscribed in a Final Market Notice in accordance with the procedures outlined in EP 4.6.
- (b) **Standard Penalty.** A violation of this rule is subject to a maximum penalty of \$25,000 per event **and** an amount equal to twice the Participant Benefits received by the offending party as a result of such behavior.
- (c) **Limitation.** No penalty may be assessed by the ISO under this rule until such behavior or behavior substantially similar to it has been proscribed in a Final Market Notice in accordance with the procedures outlined in EP 4.6.

EP 3 PROCESS FOR INVESTIGATION AND ENFORCEMENT GENERALLY

EP 3.1 Purpose; Scope

The provisions of this EP 3 set forth the procedures by which the ISO will formally investigate potential violations of the Rules of Conduct set forth in EP 2, and by

which it will conclude its investigations. Except as hereinafter provided, the provisions of this section apply to all of the Rules of Conduct set forth above (EP 2.2 through EP 2.10), and apply to action undertaken by the ISO only. The ISO may adopt alternate or additional procedures for undertaking preliminary or initial review of potential violations of Rules of Conduct. However, the ISO shall comply with the provisions of this section before seeking to assess penalties against a Market Participant for a violation or potential violation of the Rules of Conduct set forth in EP 2. Notwithstanding the foregoing, the provisions of this EP 3 will not apply to violations for which the ISO has developed automated algorithms to detect such violations and to assess monetary consequences, provided that such violations are subject to review under the ISO's current Settlement and dispute resolution processes.

EP 3.2 Investigation

The ISO will conduct a reasonable investigation seeking available facts, data, and other information relevant to the suspected violation.

EP 3.3 Notice

The ISO will provide notice of the investigation to the Market Participant(s) that are the subject(s) of the investigation in sufficient detail to allow for a meaningful response.

EP 3.4 Opportunity to Present Evidence

The ISO will provide an opportunity to the Market Participant(s) that are the subject(s) of the investigation to present data, information, and/or written comment relevant to the event or behavior being investigated. The ISO will consider all such information or data presented.

EP 3.5 Results of Investigation

The ISO will notify the Market Participant(s) that are the subject(s) of the investigation of the results of the investigation.

EP 3.6 Statement of Findings and Conclusions

Where the investigation results in a penalty or sanction, the ISO will state its findings and conclusions in writing, and will make such writing available to the Market Participant(s) that are the subject(s) of the investigation.

EP 3.7 Referral to Oversight and Enforcement Agencies

The ISO may refer any matter under investigation to an Oversight and Enforcement Agency. Where the ISO makes such a referral, it will notify the Market Participant(s) that are the subject(s) of the investigation of the referral and will make available to such Market Participants the data and other information provided to the Oversight and Enforcement Agency. The foregoing is subject to the limitations set forth in Section 20.3 of the ISO Tariff.

EP 3.8 Officer Representative

Where an investigation results in a penalty or other sanction by the ISO, or a referral requesting action of another authority, the ISO shall direct its notice of such result to a responsible representative of the Market Participant that is the subject of the investigation at the officer level.

EP 3.9 Record of Investigation

Where an investigation results in a sanction or referral, the ISO will maintain a record of the investigation until its decision has been finally reviewed, if review is sought, or until the period for seeking review has expired.

EP 3.10 Review of Determination

A Market Participant that is the subject of an investigation may obtain review of a determination resulting in the assessment of a penalty by the ISO, using the dispute resolution procedures outlined in Section 13 of the ISO Tariff.

EP 4 PROCESS FOR PROHIBITING DETRIMENTAL PRACTICES AND MARKET MANIPULATION

EP 4.1 Scope

The provisions of this EP 4 set forth the procedures by which the ISO will provide additional notice to Market Participants of behavior potentially subject to penalties or other action under EP 2.9 and EP 2.10. The provisions of this section apply only to EP 2.9 and EP 2.10, and further apply only to action undertaken by the ISO. The ISO shall comply with the provisions of this section, in addition to the provisions of EP 3 above, before assessing penalties or taking other action against a Market Participant for a violation or potential violation of EP 2.9 and EP 2.10.

EP 4.2 General Process

The process by which the ISO will identify specific behavior that is subject to the provisions of EP 2.9 and EP 2.10, prior to assessing penalties or taking other adverse action against a Market Participant for a violation of those provisions, generally will consist of the following steps:

- (a) On determining that a New Behavior may warrant action under EP 2.9 and/or EP 2.10, the ISO will issue a Preliminary Market Notice to all Market Participants and file such notice with FERC, on the terms specified in EP 4.3, unless such a general market notice potentially will cause harm to the ISO Market, in which case the ISO will issue a Formal Warning to the affected Market Participant(s) and file such warning with FERC, on the terms specified in EP 4.4. For purposes of this section, New Behavior means conduct that is neither the subject of a prior market notice under this section, nor substantially similar to conduct addressed in a prior market notice under this section.

- (b) The Preliminary Market Notice or Formal Warning may direct Market Participant(s) to cease and desist from engaging in the behavior at issue, on terms specified in EP 4.5, pending conclusion of an investigation.
- (c) Following the issuance of a Preliminary Market Notice or Formal Warning, the ISO will undertake an investigation to determine whether the behavior at issue warrants proscription under EP 2.9 or EP 2.10. In conducting its investigation, the ISO will comply with the provisions of EP 3 above, and will consider the factors set forth in EP 4.7.
- (d) At the conclusion of the investigation, the ISO will issue a Final Market Notice to all Market Participants and to FERC, on the terms specified in EP 4.6.

EP 4.3 Preliminary Market Notice

A Preliminary Market Notice issued under this section shall specify the New Behavior under investigation, provide an example of the behavior, and identify the Rules of Conduct potentially violated by the behavior (EP 2.9 and/or EP 2.10). A Preliminary Market Notice also may contain a directive to Market Participants to cease and desist from engaging in the suspected behavior, on the terms specified in EP 4.5. A Preliminary Market Notice shall be posted under the ISO Home Page and further shall be e-mailed to all Market Participants included on the ISO's e-mail distribution list. The notice shall be effective as of the time that it is posted under the ISO Home Page. Additionally, the Preliminary Market Notice shall be filed with FERC within forty-eight (48) hours after issuance (or, if the FERC office is not open for business at that time, by 10:00 EST on the next business day thereafter).

EP 4.4 Formal Warning

A Formal Warning issued under this section shall specify the New Behavior under investigation, provide an example of the behavior, and identify the Rules of Conduct potentially violated by the behavior (EP 2.9 and/or EP 2.10). A Formal Warning also may contain a directive to Market Participants to cease and desist from engaging in the suspected behavior, on the terms specified in EP 4.5. A Formal Warning shall be transmitted to the affected Market Participant(s) by e-mail at the address listed in the ISO's e-mail distribution list, and also by overnight mail. The warning shall become effective for a Market Participant as of the time the e-mail is transmitted to that Market Participant. Additionally, the Formal Warning shall be filed with FERC within forty-eight (48) hours after issuance (or, if the FERC office is not open for business at that time, by 10:00 EST on the next business day thereafter). A Formal Warning may be filed with FERC under seal.

EP 4.5 Cease and Desist Directive

A Preliminary Market Notice or Formal Warning may contain a directive to Market Participant(s) to cease and desist from engaging in the suspected behavior, pending conclusion of an investigation. In the event that a Market Participant does not comply with the directive, and the suspected behavior subsequently is prohibited, the ISO may refer such noncompliance to FERC or other authority for

corrective action. The ISO shall not be authorized directly to assess penalties for such noncompliance except as provided in EP 4.6.

EP 4.6 Final Market Notice

All suspected violations of EP 2.9 and/or EP 2.10, for which a Preliminary Market Notice or Formal Warning has been issued, will be concluded with the issuance of a Final Market Notice. The Final Market Notice shall specify the suspected behavior that was investigated, provide an example of the behavior, and identify the Rules of Conduct potentially violated by the behavior (EP 2.9 and/or EP 2.10). The Final Market Notice further shall contain a concise statement of the ISO's findings and conclusions, including a statement concerning whether the suspected behavior thereafter will be deemed to be a violation of EP 2.9 and/or EP 2.10. Where the behavior is found to violate a Rule of Conduct, the Final Market Notice will state the possible consequences of such violation, including applicable penalties. A Final Market Notice may not be issued until at least forty-eight (48) hours after issuance of a Preliminary Market Notice or Formal Warning. The Final Market Notice shall be posted under the ISO Home Page and further shall be e-mailed to all Market Participants included on the ISO's e-mail distribution list. The notice shall be effective as of the time that it is posted under the ISO Home Page. A Final Market Notice prohibiting the suspected conduct shall be deemed to cover the behavior described therein, and conduct substantially similar to such behavior. The Final Market Notice shall be filed with FERC within twenty-four (24) hours after issuance (or, if the FERC office is not open for business at that time, by 10:00 EST on the next business day thereafter).

EP 4.7 Criteria for Making Determination

The ISO shall consider the following factors, among others, in determining whether a behavior should be deemed a violation of EP 2.9 and/or EP 2.10:

- (a) Whether the specific behavior meets the definition of Detrimental Practices and/or Market Manipulation stated in EP 2.9 and/or EP 2.10.
- (b) The impact of the specific type of behavior on market efficiency.
- (c) Whether the specific type of behavior adversely impacts market prices in ways that are inconsistent with market supply and demand conditions.
- (d) Whether the specific type of behavior tends to make prices in comparable markets converge, as in the case of most forms of arbitrage, or tends to make prices diverge from levels consistent with supply and demand in different markets.
- (e) Whether the specific type of behavior is sustainable, and the extent to which other Market Participants can replicate the behavior.
- (f) Whether other Market Participants are able to protect themselves from the specific type of behavior.

- (g) Whether the specific type of behavior negatively impacts System Reliability, considering the transparency of the specific type of behavior to the system operator, the impact of the specific type of behavior on prediction of real-time system performance, and the impact of the specific type of behavior on transmission availability.
- (h) Whether the specific type of behavior conflicts with legal or regulatory requirements.

EP 4.8 Penalties; Other Actions

The ISO shall not be authorized to assess penalties under EP 2.9 and/or EP 2.10 for New Behavior until twenty-four (24) hours after filing a Final Market Notice meeting the requirements of EP 4.6 with FERC. Thereafter, the ISO may assess penalties for violations occurring from the time of the issuance of the Final Market Notice, going forward. Nothing in this section, however, shall preclude the ISO from referring earlier behavior to FERC or other authority for action.

EP 5 ADMINISTRATION OF PENALTIES

EP 5.1 Assessment; Factors to be Considered

The ISO will determine the penalty amount for a violation of Rules of Conduct by first calculating the maximum amount of the penalty as set forth in EP 2.2 through 2.10, as may be enhanced by EP 5.3. The ISO will then determine the specific penalty amount to be assessed, up to the maximum amount, by considering the following factors:

- (a) The degree to which the violation may have affected System Reliability or market integrity;
- (b) Whether the violation occurred during a System Emergency, warning, or alert;
- (c) The degree to which the Market Participant benefited from the violation;
- (d) The degree to which the violation affected overall market prices for Energy, Ancillary Services, and/or Congestion, or otherwise affected the integrity of the markets for Energy, Ancillary Services, and/or Congestion;
- (e) Whether other entities were harmed and the extent of this harm;
- (f) Whether the violation was inadvertent and unintentional, or willful, or grossly negligent;
- (g) The frequency of the violation;
- (h) The duration of the violation;
- (i) Whether the Market Participant was acting alone or in concert with others;

- (j) The Market Participant's attempts to self-identify and promptly correct the violation or provide restitution;
- (k) The Market Participant's history of prior misconduct;
- (l) The appropriateness of the penalty to the magnitude of the Market Participant's business;
- (m) The deterrent effect the penalty is likely to have on similar conduct by other Market Participants;
- (n) Any cumulative effect of multiple penalties applying to a single event;
- (o) The extent to which the Market Participant failed to act on opportunities or information allowing the Market Participant to make efforts to rectify or ameliorate the violation;
- (p) For penalties imposed based on inaccurate meter data, the ISO will consider whether or not the errors have a root cause, scope, duration, and magnitude consistent with Good Utility Practice, and for ISO polled meter data, the ISO will consider its own contribution, if any, to the magnitude of the inaccuracy of the meter data based on the activities the ISO performs under the Metering Protocol;
- (q) Resource performance and availability are subject to, among other factors, climatic variations and emissions, license, and other limitations. A Market Participant that has made a good faith effort to describe in a bid or schedule the technical abilities of equipment in expected operating conditions as a result of variations in actual operating conditions or capabilities may have an applicable penalty mitigated, so long as all obligations to report relevant de-rates or outages that affect the ability of the Market Participant to meet its scheduled or bid performance characteristics are fulfilled;
- (r) A penalty imposed on a Market Participant for failure to deliver accurate information may be mitigated if the Market Participant has made a good faith effort to supply accurate, responsive information. Inadvertent errors or omissions may be considered as mitigating factors; and
- (s) In assessing a failure to schedule load accurately in accordance with EP 2.7(c)(i), the ISO will specifically consider reasonable sources of load forecast error.

EP 5.2 Excuse

The following circumstances may excuse a violation of a Rule of Conduct under the terms of this Protocol:

- (a) **Uncontrollable Force.** The ISO will consider Uncontrollable Force, as provided in Section 15 of the ISO Tariff, in determining whether a Rule of Conduct violation should be penalized.

- (b) **Safety, Licensing, or Other Requirements.** Failure by a Market Participant to perform its obligations may not be subject to penalty if the Market Participant is able to demonstrate that it was acting in accordance with Section 2.3.1.2.1 of the ISO Tariff.
- (c) **Emergencies.** Failure by a Market Participant to perform its obligations may not be subject to penalty if the Market Participant is able to demonstrate that it was acting in good faith and consistent with Good Utility Practice to preserve System Reliability in a System Emergency, unless contrary to an ISO operating order.
- (d) **Conflicting Directives.** To the extent that any action or omission by a Market Participant is specifically required by a FERC Order or ISO operating order, the Market Participant may not be subject to penalty for that act or omission.

EP 5.3 Enhancement

The ISO may triple the maximum amount of any fixed penalty stated for a violation of EP 2.2 to EP 2.10 in the following circumstances:

- (a) If the violation occurred during a System Emergency; or
- (b) If the ISO determines that the violation is part of a continuing pattern of the same violation for which one or more monetary penalties have previously been imposed upon the Market Participant.

Penalties under EP 2.2(c) shall not be subject to such enhancement.

EP 5.4 Settlement

Penalties assessed under this Protocol will be administered through Preliminary and Final Settlement Statements issued to the responsible Scheduling Coordinator by the ISO. Except for penalties assessed through automated algorithms, the ISO will provide a description of the penalty to the responsible Scheduling Coordinator before invoicing the amount of that penalty through the Settlement process. The description will include the identity of the Market Participant that committed the violation, a description of the violation, the amount of the penalty and a description of any application of mitigating factors. The ISO also may publish this information under the ISO Home Page after Final Settlement Statements are issued.

The Scheduling Coordinator shall pay the amount of the penalty to the ISO pursuant to the ISO's Settlement process, as set forth in Section 11 of the ISO Tariff. In all cases, a Market Participant may dispute the ISO's imposition of a penalty through its Scheduling Coordinator as set forth in the ISO Tariff.

EP 5.5 Disposition of Proceeds

Penalty proceeds received by the ISO shall be allocated as described in SABP 3.1.2.

EP 5.6 Time Limitation

No penalties may be assessed by the ISO under this Protocol more than three years after discovery by the ISO of the underlying violation.

EP 5.7 Other Sanctions

In addition to imposing penalties under this Protocol, the ISO may also refer the actions of a Market Participant to the Oversight and Enforcement Agencies, and recommend that those agencies impose additional sanctions upon the Market Participant on a going forward basis. The ISO may recommend sanctions including but not limited to conditioning of the Market Participant's market-based rate authority by placing specific limitation and/or affirmative requirements on the Market Participant's future market behavior. The ISO shall recommend sanctions specifically designed to deter the behavior of the individual Market Participant(s) and/or mitigate the detrimental impacts of their behavior on System Reliability, market efficiency, and other Market Participants, while avoiding the necessity of placing additional restrictions on all Market Participants.

EP 6 NO LIMITATIONS ON OTHER RIGHTS OF THE ISO

Nothing contained in this Protocol shall limit the ability of the ISO to collect information from Market Participants or to institute new provisions pursuant to Section 19 of the ISO Tariff.

EP 7 AMENDMENTS

If the ISO determines that an amendment to this Protocol is needed, the ISO will follow the ISO Protocol amendment process set forth in Section 16 of the ISO Tariff.

APPENDIX A

1. Method for Calculating Inaccurate Meter Data Penalty (EP 2.7(c)(ii))

There is no penalty for inaccuracies in meter data used for Preliminary Settlement Statements. However, an error discovered after issuance of Final Settlement Statements is a Rule of Conduct violation. Penalties are sized depending on whether the Scheduling Coordinator or the ISO identified the error. An increased penalty will apply for errors that are discovered by the ISO.

Table A1 below shows how the size of the charge depends on whether or not the Scheduling Coordinator finds the error, whether or not the Scheduling Coordinator owes the market, and whether or not the ISO reruns settlement of the market. If the ISO reruns the market, then settlement to all Scheduling Coordinators is recalculated, and the impact of such reruns on charges assessed will be considered. A charge equal to 30% of the estimated value of the Energy error will apply if the Scheduling Coordinator discovers the error, or 75% of the estimated value of the Energy error if the ISO discovers the error. The ISO will not issue a penalty unless it is greater than \$1,000 for at least one Trading Day during the period the incomplete or inaccurate meter data event existed.

Table A1 – Calculation of Inaccurate Meter Data Penalty

Case	Does SC Owe Market?	Does ISO Re-Run Settlement of the Market?
Case 1: SC Identifies Inaccurate Meter Data	Yes	No: Charge = (MW x Hourly Ex Post Price ¹) x 1.30 Yes: Charge = (MW x Hourly Ex Post Price ¹) x 0.30
Case 1: SC Identifies Inaccurate Meter Data	No	No: Charge = Market Settlement x 1.00 ² Yes: Charge = (MW x Hourly Ex Post Price ¹) x 0.30
Case 2: ISO Identifies Inaccurate Meter Data	Yes	No: Charge = (MW x Hourly Ex Post Price ¹) x 1.75 Yes: Charge = (MW x Hourly Ex Post Price ¹) x 0.75
Case 2: ISO Identifies Inaccurate Meter Data	No	No: Charge = Market Settlement x 1.00 ² Yes: Charge = (MW x Hourly Ex Post Price ¹) x 0.75

Notes to Table A1:

1 The ISO will use the greater of the Hourly Ex Post Price or \$10. The Hourly Ex Post Price used will be the value posted under the ISO Home Page for each Trading Hour of the applicable Trading Day.

2 If the market owes the Scheduling Coordinator but the amount is too small to justify re-running the market, the ISO will not take steps to adjust the implicit charge.

The ISO will only issue a penalty that is greater than \$1,000 for at least one Trading Day during the period the incomplete or inaccurate meter data event existed.

If the error is to the detriment of the responsible Scheduling Coordinator (e.g., under-reported generation or over-reported load), and the ISO does not rerun the market, then no correction will be made, representing an implicit penalty of 100% of the value of the Energy. If the market is rerun after the error is corrected, then the Scheduling Coordinator will be given credit for the additional Energy through the normal Settlement process. If the Scheduling Coordinator is paid for an error due to a market rerun, then the ISO will impose a charge to assure that market reruns do not diminish the incentive to correct such errors. This charge would be 30% of the Energy value of the error if the Scheduling Coordinator discovers the error, or 75% estimated value of the error if the ISO discovers the error.

If the error is to the detriment of the market, then a charge equal to 30% or 75% of the estimated value of the error, as appropriate, will be added to the charge for the Energy. If there is no market rerun, then the cost of Energy supplied by the ISO (and inappropriately charged to the market as Unaccounted for Energy) must be recovered as well, and the charge will be equal to 130% or 175% of the estimated value of the error, as appropriate.

2 **Method for Calculating Participant Benefits (EP 2.4, 2.5, 2.9, and 2.10)**

The ISO will calculate the base (or minimum) penalty for physical withholding, economic withholding, Detrimental Practices, or Market Manipulation based on one of the two alternative general equations described below, depending on the circumstances of the violation:

a) **Option 1**

In circumstances other than those in which Option 2 is employed as described below, the following equation will be used to quantify Participant Benefits:

Quantity x (Price – Marginal Cost)

Where:

Quantity represents the volume of Energy, capacity, or other transaction type by the Market Participant that is involved in or affected by the Rule of Conduct violation.

Price represents the price received by the Market Participant for these transactions.

Marginal Cost represents the approximate short-term marginal costs, if any, incurred to provide the Energy for the transaction involved in the

Rule of Conduct violation. For Energy transactions associated with thermal Generating Units, marginal costs shall be based on incremental heat rates previously filed with the ISO, monthly spot market gas prices, and a rate of \$6/MWh for other variable costs.

For non-thermal Generating Units, imports or transactions based on resource portfolios (rather than specific thermal Generating Units), marginal costs shall be based on a proxy gas-fired Generating Unit with a heat rate 9,000 MBtu/MWh and monthly spot market gas prices.

Marginal costs shall be calculated only for the hours in which the Rule of Conduct violation occurred, and shall not include start-up or other costs incurred during other hours.

For transactions for capacity, Congestion relief, or other non-Energy transactions, no direct or indirect opportunity costs shall be included in the calculation.

b) Option 2

In cases where the conduct of a Market Participant is likely to have had a significant impact on market prices, the following equation may be used to quantify Participant Benefits:

$$\text{Quantity} \times (\text{Price} - \text{Estimated Price without Conduct})$$

Where:

Quantity represents the volume of Energy, capacity, or other transaction type by the Market Participant that is involved in or affected by the Rules of Conduct violation.

Price represents the price received by the Market Participant for these transactions.

Estimated Price without Conduct represents the estimated price that would have been received by the Market Participant for these transactions if the conduct had not occurred. These prices may be estimated by the ISO based on re-calculation of the approximate prices that would result if the conduct had not occurred.

ATTACHMENT C

changes to the Suggested Adjusted Schedules, all of the Suggested Adjusted Schedules shall become the Final Schedules. The Final Schedules shall serve as the basis for Settlement between the ISO and each Scheduling Coordinator.

2.2.9 Prohibition on Scheduling Across Out-of-Service Transmission Paths. Scheduling Coordinators shall not submit any Schedule using a transmission path for any Settlement Period for which the Operating Transfer Capability for that path is zero MW. The ISO shall reject Schedules submitted for transmission paths on which the Operating Transfer Capability is zero MW. If the Operating Transfer Capability of a transmission path is reduced to zero after Final Day-Ahead Schedules have been submitted, then, if time permits, the ISO shall direct the responsible Scheduling Coordinators to reduce all Schedules on such zero-rated transmission paths to zero in the Hour-Ahead Market. As necessary to comply with Applicable Reliability Criteria, the ISO shall reduce any non-zero Final Hour-Ahead Schedules across zero-rated transmission paths to zero after the close of the Hour-Ahead Market. No Usage Charges will be assessed, nor will any Usage Charges for counter-flow be paid, for Schedules across a path with an Operating Transfer Capability of zero.

2.2.10 Information to be Provided by the ISO to all Scheduling Coordinators.

By 6:00 p.m. two days prior to a Trading Day, the ISO shall publish on WEnet information, including the following to all Scheduling Coordinators for each Settlement Period of the Trading Day:

2.2.10.1 Scheduled Line Outages. Scheduled transmission line Outages;

2.2.10.2 [Not Used]

2.2.10.3 Forecast Loop-Flow. Forecast Loop Flow over ISO Inter-zonal Interfaces and Scheduling Points;

2.2.10.4 Advisory Demand Forecasts. Advisory Demand Forecasts by location;

2.2.10.5 Updated Transmission Loss Factors. Updated Generation Meter Multipliers reflecting Transmission Losses to be supplied by each Generating Unit and by each import into the ISO Control Area;

2.2.10.6 Ancillary Services. Expected Ancillary Services requirement by reference to Zones for each of the reserve Ancillary Services.

2.2.10.7 [Not Used]

2.2.10.8 [Not Used]

2.3.1.2 Market Participant Responsibilities.

2.3.1.2.1 Comply with Operating Orders Issued. With respect to this Section 2.3.1.2, all Market Participants within the ISO Control Area and all System Resources shall comply fully and promptly with the ISO's operating orders, unless such operation would impair public health or safety. In this regard, Final Hour-Ahead Schedules for Energy for Generating Units, System Resources, System Units, and Curtailable Demand are deemed to be operating orders. As such, these Schedules are binding obligations and must be fulfilled unless otherwise directed by the ISO. Any Hour-Ahead Ancillary Services Schedule or Supplementary Energy Bid is a binding obligation, and a resource so scheduled or bid cannot be made unavailable or otherwise fail to respond to ISO operating orders except for conditions beyond the control of the resource owner. Any Day-Ahead commitment of a resource, either self-scheduled or committed in the Day-Ahead Market, is a binding obligation, and such resource cannot be de-committed or otherwise be made unavailable except for conditions beyond the control of the resource owner or as approved by the ISO. The ISO will honor the terms of Existing Contracts, except during a System Emergency and circumstances in which the ISO considers that a System Emergency is imminent or threatened. In a System Emergency and circumstances in which the ISO considers that a System Emergency is imminent or threatened, Existing Rights Holders must follow ISO operating orders even if those operating orders conflict with the terms of Existing Contracts. For this purpose ISO operating orders to shed Load shall not be considered as an impairment to public health or safety.

2.3.1.2.2 Implementation of Instructions. All Market Participants shall respond to ISO instructions with no more delay than specified in the response times set out in the ISO Protocols.

2.3.1.3 Operating Reliability Criteria.

2.3.1.3.1 The ISO shall exercise Operational Control over the ISO Controlled Grid to meet planning and Operating Reserve criteria no less stringent than those established by WSCC and NERC as those standards may be modified from time to time, and Local Reliability Criteria that are in existence on the ISO Operations Date and have been submitted to the ISO by each Participating TO pursuant to

Section 2.2.1(v) of the TCA. All Market Participants and the ISO shall comply with the ISO reliability criteria, standards, and procedures.

2.3.1.3.2 The ISO may establish planning and Operating Reserve criteria more stringent than those established by WSCC and NERC or revise the Local Reliability Criteria subject to and in accordance with the provisions of the TCA.

2.3.2 Management of System Emergencies.

2.3.2.1 Declaration of System Emergencies. The ISO shall, when it considers that conditions giving rise to a System Emergency exist, declare the existence of such System

services. Accordingly the Scheduling Coordinators shall adjust their schedules to accommodate the minimum outputs required by the Generating Units included on the Schedules.

Notwithstanding the foregoing, a Scheduling Coordinator who has sold or self-provided Regulation, Spinning Reserve, Non-Spinning Reserve or Replacement Reserve capacity to the ISO in the Day-Ahead Market shall be required to replace that capacity in whole or in part from the ISO if the scheduled self-provision is decreased between the Day-Ahead and Hour-Ahead Markets, or if the Ancillary Service associated with a Generating Unit, Curtailable Demand, or System Resource successfully bid in a Day-Ahead Ancillary Service Market is reduced in the Hour-Ahead Market, for any reason (other than the negligence or willful misconduct of the ISO, or a Scheduling Coordinator's involuntary decrease in such sold capacity or scheduled self-provision on the instruction of the ISO). The price for such replaced Ancillary Service shall be the greater of the Market Clearing Price in the Hour-Ahead Market or the Market Clearing Price in the Day-Ahead Market for the Ancillary Service for the Settlement Period concerned for the Zone in which the Generating Units or other resources are located. The ISO will purchase the Ancillary Service concerned from another Scheduling Coordinator in the Hour-Ahead Market in accordance with the provisions of the ISO Tariff.

2.5.22 Rules For Real Time Dispatch of Imbalance Energy Resources.

2.5.22.1 Overview. During real time, the ISO shall dispatch Generating Units, Loads and System Resources to procure Imbalance Energy. In addition, the ISO may also need to purchase additional Ancillary Services if the services arranged in advance are used to provide Imbalance Energy, and such depletion needs to be recovered to meet reliability contingency requirements.

Charge for each hour they have counter-scheduled on the Congested Inter-Zonal Interfaces.

The amount payable shall be the product of the Usage Charge referred to in Section 7.3.1.2 for that particular hour, multiplied by the Scheduling Coordinator's scheduled flows.

7.3.1.5.2 If a Scheduling Coordinator fails to provide the scheduled flows in a counter direction, it must reimburse the ISO for the ISO's costs of buying or selling Imbalance Energy in each of the Zones affected by the non-provided scheduled flows in a counter direction, at the ISO's Zonal Imbalance Energy prices. That is, for any Scheduling Coordinator that does not produce, in real time, the amount of Energy scheduled in the Day-Ahead Market or Hour-Ahead Market will be deemed to have purchased/sold the amount of Energy under/over produced in the real time imbalance market at the real time price. In addition, to the extent that any Scheduling Coordinator would receive a Usage Charge payment for Energy that was scheduled in a counter direction over an inter-tie in the Day-Ahead or Hour-Ahead Market but was not delivered in real time, that Usage Charge payment will be eliminated, pro rata, based on the difference between the scheduled counter-flow in the Hour-Ahead Market, and the final real-time Schedule in the counter direction.

For purposes of any adjustments to Usage Charges under this provision, scheduled flows in the counter direction and any related Usage Charges shall be determined relative to the direction of the final Hour-Ahead flow on the inter-tie. If Congestion reverses direction in the Hour-Ahead relative to Day-Ahead, the Day-Ahead Usage Charge deemed to have been paid to the Scheduling Coordinator in the counter direction is \$0/MWh (not the negative of the Day-Ahead Usage Charge).

7.3.1.5.3 Scheduling Coordinators shall not receive a Usage Charge payment for scheduled flows in a counter direction if such scheduled flow is the result of a Circular Schedule.

7.3.1.6 ISO Disbursement of Net Usage Charge Revenues. The ISO will determine the net Usage Charges on an interface-by-interface basis by subtracting the Usage Charge fees paid to

Scheduling Coordinators from the Usage Charge fees paid by Scheduling Coordinators. The net Usage Charge revenues collected by the ISO for each Inter-Zonal Interface shall be, subject to the provisions of Section 7.3.1.7 of the ISO Tariff, paid to: (i) FTR Holders, in accordance with Section 9.6; and (ii) to the extent not paid to FTR Holders, to Participating TOs who own the Inter-Zonal Interfaces and Project Sponsors as provided in Section 3.2.7.3. Participating TOs will credit in turn the Usage Charge revenue to their Transmission Revenue Balancing Accounts, or, for those Participating TOs that do not have such accounts, to their Transmission Revenue Requirements.

7.3.1.7 ISO Debit of Net Usage Charge Revenues. If, after the issuance of Final Day-Ahead Schedules by the ISO, (a) Participating TOs instruct the ISO to reduce interface limits based on operating conditions or (b) an unscheduled transmission outage occurs and as a result of either of those events, Congestion is increased and Available Transfer

law. The ISO shall cooperate with the affected Market Participant to obtain proprietary or confidential treatment of confidential information by the person to whom such information is disclosed prior to any such disclosure.

- (c) In order to maintain reliable operation of the ISO Control Area, the ISO may share individual Generating Unit Outage information with the operations engineering and/or the outage coordination division(s) of other Control Area operators, Participating TOs, MSS Operators engaged in the operation and maintenance of the electric supply system whose system is significantly affected by the Generating Unit and who have executed the Western Electricity Coordinating Council Confidentiality Agreement for Electric System Data.

20.3.5 Disclosure to Oversight and Enforcement Agencies

Notwithstanding anything in this Section 20.3 to the contrary, the ISO may disclose information otherwise required to be maintained in confidence under the ISO Tariff to an Oversight and Enforcement Agency, on the terms and conditions hereinafter described.

- (a) The ISO may disclose to an Oversight and Enforcement Agency individual bids, schedules, outage plans, and other information routinely collected by the ISO for purposes of monitoring the ISO markets and analyzing market performance, subject to the limitations stated below. The ISO may make such disclosures to an Oversight and Enforcement Agency on a routine or periodic basis, with or without advance notice to Market Participants, if all of the following requirements have been met:
- (1) The ISO has identified each category of information that it intends to disclose to an Oversight and Enforcement Agency under this Section 20.3.5 in a market notice issued at least thirty (30) days in advance of the disclosure;
 - (2) Each category of information that the ISO proposes to disclose is of a type wherein each Market Participant has access to that portion of the information

- pertaining to it (e.g., an Energy Bid) contemporaneous with the disclosure, through each Market Participant's systems or records;
- (3) The proposed disclosure relates to the ISO markets as a whole and is comprised of information on all Market Participants for which such information is available to the ISO; rather than comprised of a subset of available information focusing on a particular Market Participant or Market Participants; and
 - (4) Each of the Oversight and Enforcement Agencies to which the ISO makes such disclosure is bound legally, by virtue of applicable law, regulation, protective order, contract, or other means, to treat the information as confidential under terms no less protective than the requirements stated in subsection (c) below.
- (b) The ISO may disclose any information required to be maintained in confidence under the ISO Tariff to any of the Oversight and Enforcement Agencies, without meeting the requirements stated in subsection (a) above, if all of the following requirements have been met:
- (1) The ISO has a reasonable belief that the Market Participant or Market Participants to which the disclosure pertains may have violated an applicable market rule, tariff provision, protocol, regulation, or law;
 - (2) Each of the Oversight and Enforcement Agencies to which the information is to be disclosed has oversight or enforcement authority over the potential violation;
 - (3) The ISO has a reasonable belief that the information to be disclosed would be relevant to an investigation of the potential violation;
 - (4) The ISO provides notice to the Market Participant or Market Participants that is or are the subject of the disclosure five (5) business days in advance of the proposed disclosure, unless affording such notice could jeopardize a pending or anticipated investigation by the ISO or by the Oversight and Enforcement

Agency to whom the disclosure is to be made, in which case, no notice will be required; and

- (5) Each of the Oversight and Enforcement Agencies to which the ISO makes such disclosure is bound legally, by virtue of applicable law, regulation, protective order, contract or other means, to treat the information as confidential under terms no less protective than the requirements stated in subsection (c) below.
- (c) Each of the Oversight and Enforcement Agencies to which information is disclosed under this section must be bound, at a minimum, to a legal obligation that sets forth in writing the terms applicable to the treatment of confidential and/or commercially sensitive information, and that obligates the agency not to disclose to any third party information provided under this section without providing written notice to the ISO and the Market Participant that is the subject of the disclosure at least five (5) business days in advance of the intended date of release. The Market Participant may, at its sole discretion and own cost, direct any challenge to or defense against the proposed disclosure and the ISO shall cooperate as provided in Section 20.3.4(b).
- d) Nothing in this section shall limit the ability of an Oversight and Enforcement Agency to seek information in accordance with the provisions of Section 20.3.4(b), nor limit the ability of the ISO to disclose information in accordance with that section.

20.4 Staffing and Training To Meet Obligations.

The ISO shall engage sufficient staff to perform its obligations under this ISO Tariff in a satisfactory manner consistent with Good Utility Practice. The ISO shall make its own arrangements for the engagement of all staff and labor necessary to perform its obligations hereunder and for their payment. The ISO shall employ (or cause to be employed) only persons who are appropriately qualified, skilled and experienced in their respective trades or occupations. ISO employees and contractors shall abide by the ISO Code of Conduct for employees contained in the ISO bylaws and approved by FERC.

20.5 Accounts and Reports.

The ISO shall notify Market Participants of any significant change in the accounting treatment or methodology of any costs or any change in the accounting procedures, which is expected to result in a significant cost increase to any Market Participant. Such notice shall be given at the earliest possible time, but no later than, sixty (60) days before implementation of such change.

BEEP Interval Ex Post Prices

The prices charged to or paid by Scheduling Coordinators for Imbalance Energy in each Zone in each BEEP Interval.

BEEP Software

The balancing energy and ex post pricing software which is used by the ISO to determine which Ancillary Service and Supplemental Energy resources to Dispatch and to calculate the Ex Post Prices.

Black Start

The procedure by which a Generating Unit self-starts without an external source of electricity thereby restoring power to the ISO Controlled Grid following system or local area blackouts.

Black Start Generator

A Participating Generator in its capacity as party to an Interim Black Start Agreement with the ISO for the provision of Black Start services, but shall exclude Participating Generators in their capacity as providers of Black Start services under their Reliability Must-Run Contracts

Bulk Supply Point

A UDC metering point.

Business Day

A day on which banks are open to conduct general banking business in California.

C.F.R.

Code of Federal Regulations.

Circular Schedule

A Schedule or set of Schedules that creates a closed loop of Energy Schedules between the ISO Controlled Grid and one or more other Control Areas that do not have a source and sink in separate Control Areas, which includes Energy scheduled in a counter direction over a Congested Inter-Zonal Interface through two or more Scheduling Points. A closed loop of Energy Schedules that includes a transmission segment on the Pacific DC Intertie shall not be a Circular Schedule because such a Schedule directly changes power flows on the network and can mitigate Congestion between SP15 and NP15.

Completed Application Date

For purposes of Section 5.7, the date on which a New Facility Operator submits an Interconnection Application to the ISO that satisfies the requirements of the ISO Tariff and the TO Tariff of the Interconnecting PTO.

Completed Interconnection Application

An Interconnection Application that meets the information requirements as specified by the ISO and posted on the ISO Home Page.

Conditional Energy Bids

A Bid for Energy to serve Demand at or below a specified price.

Congestion

A condition that occurs when there is insufficient Available Transfer Capacity to implement all Preferred Schedules simultaneously or, in real time, to serve all Generation and Demand. "Congested" shall be construed accordingly.

Congestion Management

The alleviation of Congestion in accordance with Applicable ISO Protocols and Good Utility Practice.

<u>Operating Reserve</u>	The combination of Spinning and Non-Spinning Reserve required to meet WSCC and NERC requirements for reliable operation of the ISO Control Area.
<u>Operating Transfer Capability</u>	The maximum capability of a transmission path to transmit real power, expressed in MW, at a given point in time.
<u>Operational Control</u>	The rights of the ISO under the Transmission Control Agreement and the ISO Tariff to direct Participating TOs how to operate their transmission lines and facilities and other electric plant affecting the reliability of those lines and facilities for the purpose of affording comparable non-discriminatory transmission access and meeting Applicable Reliability Criteria.
<u>Operator</u>	The operator of facilities that comprise the ISO Controlled Grid or a Participating Generator.
<u>OPF (Optimal Power Flow)</u>	A computer optimization program which uses a set of control variables (which may include active power and/or reactive power controls) to determine a steady-state operating condition for the transmission grid for which a set of system operating constraints (which may include active power and/or reactive power constraints) are satisfied and an objective function (e.g. total cost or shift of schedules) is minimized.
<u>Order No. 888</u>	The final rule issued by FERC entitled "Promoting Wholesale Competition through Open Access Non- discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities," 61 Fed. Reg. 21,540 (May 10, 1996), FERC Stats. & Regs., Regulations Preambles [1991-1996] ¶¶ 31,036 (1996), Order on Rehearing, Order No. 888-A, 78 FERC ¶¶ 61,220 (1997), as it may be amended from time to time.

- Order No. 889** The final rule issued by FERC entitled "Open Access Same-Time Information System (formerly Real Time Information Networks) and Standards of Conduct," 61 Fed. Reg. 21,737 (May 10, 1996), FERC Stats. & Regs., Regulations Preambles [1991-1996] ¶¶ 31,035 (1996), Order on Rehearing, Order No. 889-A, 78 FERC ¶¶ 61,221 (1997), as it may be amended from time to time.
- Original Participating TO** A Participating TO that was a Participating TO as of January 1, 2000.
- Outage** Disconnection or separation, planned or forced, of one or more elements of an electric system.
- Overgeneration** A condition that occurs when total Generation exceeds total Demand in the ISO Control Area.
- Oversight and Enforcement Agency** Any of the following: FERC, the United States Department of Justice or any of its subdivisions, the California Department of Justice or any of its subdivisions, the California Public Utilities Commission, or the California Electricity Oversight Board.
- Participating Buyer** A Direct Access End-User or a wholesale buyer of Energy or Ancillary Services through Scheduling Coordinators.
- Participating Intermittent Resource** One or more Eligible Intermittent Resources that meets the requirements of the technical standards for Participating Intermittent Resources adopted by the ISO and published on the ISO Home Page.

Participating Load

An entity providing Curtailable Demand, which has undertaken in writing to comply with all applicable provisions of the ISO Tariff, as they may be amended from time to time.

**Participating Seller or
Participating Generator**

A Generator or other seller of Energy or Ancillary Services through a Scheduling Coordinator over the ISO Controlled Grid from a Generating Unit with a rated capacity of 1 MW or greater, or from a Generating Unit providing Ancillary Services and/or Imbalance Energy through an aggregation arrangement approved by the ISO, which has undertaken to be bound by the terms of the ISO Tariff, in the case of a Generator through a Participating Generator Agreement.

ISO MARKET MONITORING AND INFORMATION PROTOCOL

Table of Contents

MMIP 1	OBJECTIVES, DEFINITIONS, AND SCOPE	494
MMIP 1.1	Objectives	494
MMIP 1.1.1	Means and Actions	494
MMIP 1.1.2	Reporting Requirements	494
MMIP 1.2	Definitions	494
MMIP 1.2.1	Master Definitions Supplement	494
MMIP 1.2.2	Special Terms for This Protocol	495
MMIP 1.2.3	Rules of Interpretation	495
MMIP 1.3	Scope	495
MMIP 1.3.1	Scope of Application to Parties	495
MMIP 1.3.2	Liability of ISO	495
MMIP 2	PRACTICES SUBJECT TO SCRUTINY	495A
MMIP 2.1	Practices Subject to Scrutiny – General	495A
MMIP 2.1.1	Anomalous Market Behavior	496
MMIP 2.1.2	Abuse of Reliability Must-Run Unit Status	496
MMIP 2.1.3	Gaming	496
MMIP 2.1.4	ISO and Other Market Design Flaws	497
MMIP 2.1.5	Market Structure Flaws	497
MMIP 2.2	Scrutiny of Participant Changes Potentially Affecting Market Structure	497
MMIP 2.2.1	Exercises of Horizontal Market Power	497
MMIP 2.3	Response Action by ISO	498
MMIP 2.3.1	Corrective Actions	498
MMIP 2.3.2	Further Actions	498
MMIP 2.3.3	Response to Gaming Behavior	499
MMIP 2.3.4	Adverse Effects of Transition Mechanisms	499

MMIP 3	ISO DEPARTMENT OF MARKET ANALYSIS	500
MMIP 3.1	Establishment	500
MMIP 3.2	Composition	500
MMIP 3.3	Accountability and Responsibilities	500
MMIP 3.3.1	Department of Market Analysis	500
MMIP 3.3.2	CEO and MSC	500
MMIP 3.3.3	Chief Executive Officer (CEO)	500
MMIP 3.3.4	Regulatory and Antitrust Enforcement Agencies	501
MMIP 3.3.5	Complaints	501
MMIP 4	SPECIFIC FUNCTIONS OF ISO DEPARTMENT OF MARKET ANALYSIS	501
MMIP 4.1	Information Gathering and Market Monitoring Indices for Evaluation	501
MMIP 4.1.1	Information System	501
MMIP 4.1.2	Data Categories	501
MMIP 4.1.3	Catalog of Market Monitoring Indices	502
MMIP 4.2	Evaluation of Information	502
MMIP 4.2.1	Ongoing Evaluation	502
MMIP 4.2.2	Submission of Evaluation Results	502
MMIP 4.3	Review of Rules of Conduct	502
MMIP 4.4	Reports and Recommendations	502
MMIP 4.4.1	ISO CEO and Governing Board	502
MMIP 4.4.2	Regulatory Agencies	503
MMIP 4.4.3	ISO Market Surveillance Committee	503
MMIP 4.5	Market Participants	503
MMIP 4.5.1	Collection of Data	503
MMIP 4.5.2	Dissemination of Data	504
MMIP 4.6	External Consulting Assistance and Expert Advice	504
MMIP 4.7	Liability for Damages	505

MMIP 5	MARKET SURVEILLANCE COMMITTEE	505
MMIP 5.1	Establishment	505
MMIP 5.2	Composition	505
MMIP 5.2.1	Qualifications	505
MMIP 5.2.2	Criteria for Independence	505
MMIP 5.3	Appointments to the MSC	506
MMIP 5.4	Compensation and Reimbursements	506
MMIP 5.5	Liability for Damages	506
MMIP 6	SPECIFIC FUNCTIONS OF MARKET SURVEILLANCE COMMITTEE (MSC)	506
MMIP 6.1	Information Gathering and Evaluation Criteria	506
MMIP 6.2	Evaluation of Information	506
MMIP 6.3	Reports and Recommendations	507
MMIP 6.3.1	Required Reports	507
MMIP 6.3.2	Additional Reports	507
MMIP 6.4	Publication of Reports and Recommendations	507
MMIP 7	IMPLEMENTATION OF RECOMMENDATIONS	507
MMIP 7.1	Plan and Rules of Conduct Changes	507
MMIP 7.2	Tariff Changes	507
MMIP 7.3	Sanctions and Penalties	507
MMIP 8	PUBLICATION OF INFORMATION	508
MMIP 8.1	Market Monitoring Data and Indices	508
MMIP 8.2	Reports to Regulators	508
MMIP 9	AMENDMENTS	508

**ISO Market Monitoring and
Information Protocol (MMIP)**

MMIP 1 OBJECTIVES, DEFINITIONS, AND SCOPE

MMIP 1.1 Objectives

This Protocol (MMIP) sets forth the workplan and, where applicable, the rules under which the ISO Department of Market Analysis and ISO Market Surveillance Committee will monitor the ISO Markets to identify abuses of market power, to ensure to the extent possible the efficient working of the ISO Markets immediately upon commencement of their operation, and to provide for their protection from abuses of market power in both the short term and the long term, and from other abuses that have the potential to undermine their effective functioning or overall efficiency in accordance with Section 16.3 of the ISO Tariff. Such monitoring activities will be carried out by, among other ISO departments, the ISO Department of Market Analysis and the ISO Market Surveillance Committee to be established and to operate under the terms of this Protocol, as set forth below. These protocols provide a general framework for the operation of the Department of Market Analysis and the Market Surveillance Committee and are not intended to limit the activities or remedies available to these entities or to the ISO as a whole elsewhere in the ISO Tariff or otherwise under law.

MMIP 1.1.1 Means and Actions

This Protocol sets forth general means of data collection, analysis, decision-making, and formulation of corrective actions, that will be instituted or undertaken by the ISO Department of Market Analysis and ISO Market Surveillance Committee. It describes implementation mechanisms to be created by the ISO to serve these purposes.

MMIP 1.1.2 Reporting Requirements

This Protocol sets forth the information dissemination, publication and reporting activities and other means of providing information that the ISO generally undertakes to meet its reporting requirements to regulatory agencies, Market Participants and others. The goal of the reporting provisions of this Protocol is to adequately inform regulatory agencies, law enforcement agencies, policymakers, Market Participants and others of the state of the ISO Markets, especially their competitiveness and efficiency. This function is designed to facilitate efficient corrective actions to be taken by the appropriate body or bodies when required.

MMIP 1.2 Definitions

MMIP 1.2.1 Master Definitions Supplement

Any word or expression defined in the Master Definitions Supplement to the ISO Tariff shall have the same meaning where used in this Protocol. References to a Section or Appendix are to a Section or an Appendix of the ISO Tariff. References to MMIP are to this Protocol or to the stated section, paragraph or appendix of this Protocol.

MMIP 1.2.2 Special Terms for This Protocol

In this Protocol, the following words and expressions shall have the meanings set opposite them:

"Department of Market Analysis (DMA)" means the unit established under MMIP 3.1.

"Rules of Conduct" has the same meaning as provided for in the Enforcement Protocol.

"Market Surveillance Committee (MSC)" means the committee established under MMIP 5.1.

"ISO Home Page" means the ISO internet home page at <http://www.caiso.com> or such other internet address as the ISO shall publish from time to time.

MMIP 1.2.3 Rules of Interpretation

MMIP 1.2.3.1 Unless the context otherwise requires, if the provisions of this Protocol conflict with the ISO Tariff and/or the Enforcement Protocol, the ISO Tariff and the Enforcement Protocol will prevail to the extent of the inconsistency. The provisions of the ISO Tariff have been summarized or repeated in this Protocol only to aid understanding.

MMIP 1.2.3.2 A reference in this Protocol to a given agreement, ISO Protocol or instrument shall be a reference to that agreement or instrument as modified, amended, supplemented or restated through the date as of which such reference is made.

MMIP 1.2.3.3 The captions and headings in this MMIP are inserted solely to facilitate reference and shall have no bearing upon the interpretation of any of the terms and conditions of this Protocol.

MMIP 1.2.3.4 This Protocol shall be effective as of January 1, 1998. Any amendment to this Protocol shall be effective as of the date of such amendment, or as of the date such amendment is approved by FERC.

MMIP 1.3 Scope

MMIP 1.3.1 Scope of Application to Parties

The MMIP applies to:

MMIP 1.3.1.1 All ISO Market Participants;

MMIP 1.3.1.2 The ISO;

MMIP 1.3.1.3 The Market Surveillance Committee.

MMIP 1.3.2 Liability of ISO

Any liability of the ISO arising out of or in relation to this Protocol shall be subject to Section 14 of the ISO Tariff as if references to the ISO Tariff were references to this Protocol.

MMIP 2 PRACTICES SUBJECT TO SCRUTINY

MMIP 2.1 Practices Subject to Scrutiny - General

The Department of Market Analysis shall monitor the activities of
Market Participants

that affect the operation of the ISO Markets and that provide indications of the phenomena set forth below in this Section 2.1. Where appropriate, it will take such further action as it considers necessary under Section 2.3.

MMIP 2.1.1 Anomalous Market Behavior

Anomalous market behavior, which is defined as behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or as behavior leading to unusual or unexplained market outcomes. Evidence of such behavior may be derived from a number of circumstances, including:

- MMIP 2.1.1.1** withholding of Generation capacity under circumstances in which it would normally be offered in a competitive market;
- MMIP 2.1.1.2** unexplained or unusual redeclarations of availability by Generators;
- MMIP 2.1.1.3** unusual trades or transactions;
- MMIP 2.1.1.4** pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions, e.g., prices and bids that appear consistently excessive for or otherwise inconsistent with such conditions; and
- MMIP 2.1.1.5** unusual activity or circumstances relating to imports from or exports to other markets or exchanges.

The Department of Market Analysis shall evaluate, on an ongoing basis, whether the continued or persistent presence of such circumstances indicates the presence of behavior that is designed to or has the potential to distort the operation and efficient functioning of a competitive market, e.g., the strategic withholding and redeclaring of capacity, and whether it indicates the presence and exercise of market power or of other unacceptable practices.

MMIP 2.1.2 Abuse of Reliability Must-Run Unit Status

Where Generating Units are determined by the ISO to be Reliability Must-Run Units, circumstances that indicate that such Generating Units are being operated in a manner that will adversely affect the competitive nature and efficient workings of the ISO Markets.

MMIP 2.1.3 Gaming

"Gaming", or taking unfair advantage of the rules and procedures set forth in the ISO Tariffs, Protocols or Rules of Conduct, or of transmission constraints in periods in which exist substantial Congestion, to the detriment of the efficiency of, and of consumers in, the ISO Markets. "Gaming" may also include taking undue advantage of other conditions that may affect the availability of transmission and generation capacity, such as loop flow, facility outages, level of hydropower output or seasonal limits on energy imports from out-of-state, or actions or behaviors that may otherwise render the system and the ISO Markets vulnerable to price manipulation to the detriment of their efficiency.

MMIP 2.1.4 ISO and Other Market Design Flaws

Design flaws and inefficiencies in the ISO Tariff, ISO Protocols and operational rules and procedures of the ISO, including the potential for problems between the ISO and other independent power markets or exchanges insofar as they affect the ISO Markets which may be evident from anomalous market behavior monitored under MMIP 2.1.1 above, from evidence of gaming monitored under MMIP 2.1.3 above, or from other activities.

MMIP 2.1.5 Market Structure Flaws

With respect to flaws in the overall structure of the California energy markets that may reveal undue concentrations of market power in Generation or other structural flaws, the Department of Market Analysis shall provide such information or evidence of such flaws and such analysis as it may conduct to the ISO CEO and/or to the ISO Governing Board, subject to due protections of confidential or commercially sensitive information. After due internal consultation, if instructed by any of such ISO institutions or persons, the Department of Market Analysis shall also provide such information or evidence to the Market Surveillance Committee, the appropriate regulatory and antitrust enforcement agency or agencies, subject to due protections of confidential or commercially sensitive information. The Department of Market Analysis shall, at the direction of the ISO CEO and/or the ISO Governing Board, or their designee, provide such other evidence, views, analyses or testimony as may be appropriate or required and as it is reasonably capable of providing to assist the investigations of such agencies.

MMIP 2.2 Scrutiny of Participant Changes Potentially Affecting Market Structure

The Department of Market Analysis may undertake the following measures to monitor the special circumstances that may affect the operation of the ISO Markets due to corporate reorganizations including bankruptcies or changes in affiliate relationships and may recommend corrective actions as provided in Section 2.3.

MMIP 2.2.1 Exercises of Horizontal Market Power

The Department of Market Analysis may analyze the impact of changes in market structure on the ability of Market Participants to exercise short-term horizontal market power.

MMIP 2.3 Response Action by ISO

MMIP 2.3.1 Corrective Actions

Where the monitoring activities or any consequent investigations carried out by the Department of Market Analysis pursuant to MMIP 2 and MMIP 4 reveal a significant possibility of the presence of or potential for exercises of market power that would adversely affect the operation of the ISO Markets, or other markets interconnected or interdependent on the ISO Markets, the Department of Market Analysis shall take the appropriate measures under this section and under MMIP 4, 6, and 7 to institute the corrective action most effective and appropriate for the situation or, in the case of markets interconnected to or interdependent on the ISO Markets, the Department of Market Analysis may recommend corrective actions to the appropriate regulatory agencies.

MMIP 2.3.2 Further Actions

Where the monitoring activities of or any consequent investigations carried out by the Department of Market Analysis pursuant to MMIP 2.1 and 2.2 reveal that activities or behavior of Market Participants in the ISO Markets have the effect of, or potential for, undermining the efficiency, workability or reliability of the ISO Markets to give or to serve such Market Participants an unfair competitive advantage over other Market Participants, the Department of Market Analysis shall fully investigate and analyze the effect of such activities or behavior and make recommendations to the ISO CEO and the ISO Governing Board for further action by the ISO or, where necessary, by other entities. The ISO may publicize such activities or behavior and its recommendations thereof, in whatever medium it believes most appropriate. The Department of Market Analysis may, where appropriate, make specific recommendations to the ISO CEO and to the ISO Governing Board for amendment to rules and protocols under its control, or for changes to the structure of the ISO Markets, and the Department of Market Analysis may recommend actions, including fines or suspensions, against specific entities in order to deter such activities or behavior.

MMIP 2.3.3 Response to Gaming Behavior

If evidence of "gaming" or taking undue advantage exists, as described in MMIP 2.1.4, the Department of Market Analysis shall review the "gaming" behavior and/or the relationship between system conditions and market behavior and pricing in order to assess the potential for and impact of such gaming behavior, with a view to taking appropriate action, if necessary, either with respect to structural changes, or to changes to the ISO Tariff, Protocols or Rules of Conduct, or to proscribe specific behavior by Market Participants, as provided for in the Enforcement Protocol. In carrying out such activities the Department of Market Analysis shall in appropriate circumstances seek the advice of the MSC on the merits of such actions.

MMIP 2.3.4 Adverse Effects of Transition Mechanisms

Should the monitoring and analysis conducted under MMIP 2.2.3 reveal significant adverse effects of transition mechanisms on competition in or the efficient operation of the ISO Markets, the Department of Market Analysis shall examine and fully assess the efficacy of all possible measures that may be taken by the ISO, in order to prevent or to mitigate such adverse effects. The Department of Market Analysis shall make such recommendations to the CEO of the ISO and to the ISO Governing Board as it considers appropriate for action by the ISO and/or for referral to regulatory or law enforcement agencies. Such proposed measures may include, but shall not be limited to the following:

- MMIP 2.3.4.1** the use of direct bid caps as a mechanism to prevent or mitigate artificially high Market Clearing Prices caused by abuses of market power;
- MMIP 2.3.4.2** the use of contracts for differences for eliminating the incentive for Generators to bid ISO prices to artificially high levels enabled by the presence of market power;
- MMIP 2.3.4.3** calling upon Reliability Must-Run Units to operate; and to modify Reliability Must-Run Contracts;
- MMIP 2.3.4.4** bid floors to prevent or mitigate the possible exercise of below-cost bidding or predatory pricing.

In the event that the ISO Governing Board adopts, and where necessary obtains regulatory approval for, any

measure proposed pursuant to MMIP 2.3.4, the Department of Market Analysis shall monitor the implementation and effect of such measure on the state of the ISO Markets and shall periodically report on them to the CEO and the ISO Governing Board.

MMIP 3 ISO DEPARTMENT OF MARKET ANALYSIS

MMIP 3.1 Establishment

There shall be established on or before ISO Operations Date within the ISO a Department of Market Analysis that shall be responsible for the ongoing development, implementation, and execution of the ISO Market monitoring and information scheme described in this MMIP and the adherence to its objectives, as set forth in MMIP 1.1.

MMIP 3.2 Composition

The Department of Market Analysis shall be adequately staffed by the ISO with full-time ISO staff with the experience and qualifications necessary to fulfill the functions referred to in this MMIP. Such qualifications may include professional training pertinent to and experience in the operation of markets analogous to ISO Markets, in the electric power industry, and in the field of competition and antitrust law, economics and policy. The Department of Market Analysis shall be under the general management of the ISO CEO, provided that the CEO may designate another ISO officer (currently the General Counsel) for day-to-day oversight of the Department.

MMIP 3.3 Accountability and Responsibilities

MMIP 3.3.1 Department of Market Analysis

The Department of Market Analysis shall report to and be accountable to the ISO CEO and his or her designee on all matters pertaining to policy and other matters that may affect the effectiveness and integrity of the monitoring function referred to in this Protocol, including matters pertaining to market monitoring, information development and dissemination and pertaining to generic or entity-specific investigations, corrective actions or enforcement.

MMIP 3.3.2 CEO and MSC

The ISO CEO and the MSC shall each have the independent authority to refer any of the matters referred to in MMIP 3.3.1 to the ISO Governing Board for approval of recommended actions.

MMIP 3.3.3 Chief Executive Officer (CEO)

MMIP 3.3.3.1 The Department of Market Analysis shall report to and be accountable to the ISO CEO and his or her designee on all matters relating to administration of the Department and the internal resources and organization of the ISO in accordance with MMIP 3.3.3.2.

MMIP 3.3.3.2 The ISO, through its CEO and Governing Board, shall determine that the Department of Market Analysis has adequate resources and full access to data and the full cooperation of all parts of the ISO organization in developing the database necessary for the effective functioning of the Department of Market Analysis and the fulfillment of its monitoring function.

MMIP 3.3.4 Regulatory and Antitrust Enforcement Agencies

Where considered necessary and appropriate, or where so ordered by the regulatory or antitrust agency with jurisdiction over the matter in question, or by a court of competent jurisdiction, the ISO shall refer a matter to the regulatory or antitrust enforcement agency concerned, e.g., in cases of serious abuse requiring expeditious investigation or action by the agency. In all such cases of direct referral, the ISO CEO shall promptly inform the ISO Governing Board and the MSC of the fact of and the content of the referral.

MMIP 3.3.5 Complaints

Any Market Participant, or any other interested entity, may at any time submit information to or make a complaint to the Department of Market Analysis concerning any matter that it believes may be relevant to the Department of Market Analysis's monitoring responsibilities. Such submissions or complaints may be made on a confidential basis in which case the Department of Market Analysis shall preserve the confidentiality thereof. The Department of Market Analysis, at its discretion, may request further information from such entity and carry out any investigation that it considers appropriate as to the concern raised. The Department of Market Analysis shall periodically make reports to the ISO CEO and ISO Governing Board on complaints received.

MMIP 4 SPECIFIC FUNCTIONS OF ISO DEPARTMENT OF MARKET ANALYSIS

MMIP 4.1 Information Gathering and Market Monitoring Indices for Evaluation

MMIP 4.1.1 Information System

The Department of Market Analysis shall be responsible for developing an information system and criteria for evaluation that will permit it to effectively monitor the ISO Markets to identify and investigate abuses of that market, whether caused by exercises of market power or by other actions or inactions.

MMIP 4.1.2 Data Categories

To develop the information system set forth in MMIP 4.1.1, the Department of Market Analysis shall initially develop, and shall refine on the basis of experience, a detailed catalog of all the categories of data it will have the means of acquiring, and the procedures it will use (including procedures for protecting confidential data) to handle such data.

MMIP 4.1.3 Catalog of Market Monitoring Indices

The Department of Market Analysis shall initially develop, and shall refine on the basis of experience, a catalog of the ISO Market monitoring indices that it will use to evaluate the data so collected.

MMIP 4.2 Evaluation of Information

MMIP 4.2.1 Ongoing Evaluation

The Department of Market Analysis shall evaluate and reevaluate on an ongoing basis the data categories and market monitoring indices that it has developed under MMIP 4.1.2 and 4.1.3, and the information it collects and receives from various other sources, including and in particular the ISO's operation of the ISO Markets. Such ongoing evaluations shall provide the basis for its reporting and publication responsibilities as set forth in this Protocol, for recommendations on proposed changes to the ISO Tariff and ISO Protocols and other potential rules affecting the ISO Markets, and for the development of criteria or standards for the initiation of proposed corrective or enforcement actions. In evaluating such information, the Department of Market Analysis may consult the MSC or such external bodies as may be appropriate.

MMIP 4.2.2 Submission of Evaluation Results

The final results of the Department of Market Analysis's ongoing evaluations under MMIP 4.2.1 shall routinely and promptly be submitted to the ISO CEO and to the MSC for comment.

MMIP 4.3 Review of Rules of Conduct

The Department of Market Analysis shall review Rules of Conduct for their effectiveness and consistency with its market monitoring activities and standards. The Department of Market Analysis may at that time, and from time to time thereafter based on its experience in monitoring the ISO Markets, propose to the ISO CEO and/or the ISO Governing Board that changes be made in such Rules of Conduct.

MMIP 4.4 Reports and Recommendations

MMIP 4.4.1 ISO CEO and Governing Board

On the basis of the evaluation conducted under MMIP 4.2 or the review conducted under MMIP 4.3, the Department of Market Analysis shall prepare periodic reports, as required by the ISO CEO, and specific ad hoc reports as appropriate, for the ISO CEO and ISO Governing Board on the state of competition in or the efficiency of the ISO Markets; and on its monitoring activities, the results of its evaluation and review activities, and its development and implementation of recommendations. Where appropriate, the ISO Department of Market Analysis may recommend to the ISO CEO and/or the ISO Governing Board actions to be taken, including the amendment of the ISO Tariff and ISO Protocols and corrective or enforcement action against specific entities. Such reports shall be made not less frequently than quarterly in the case of the ISO CEO and annually in

the case of the ISO Governing Board and shall contain such information and be in such form as specified by such entities. Such reports shall be made public and publicized as specified by such entities except to the extent that they contain confidential or commercially sensitive information or to the extent such entities determine that effective enforcement of the monitoring function dictates otherwise.

MMIP 4.4.2 Regulatory Agencies

As required in the ISO Tariff or by the ISO CEO and ISO Governing Board, or as required by the regulatory agency with jurisdiction over the matters in question, the Department of Market Analysis shall prepare reports to the FERC and other regulatory agencies, which shall be reviewed and approved by the ISO CEO or his or her designee and then submitted as required. When publicly available reports are made to one regulatory agency with competent jurisdiction, such as the FERC, the Department of Market Analysis may simultaneously make such reports available to other regulatory agencies with legitimate interests in their contents, such as the Electricity Oversight Board, the California Public Utilities Commission, the California Energy Commission and/or the California Attorney General.

MMIP 4.4.3 ISO Market Surveillance Committee

All reports and recommendations to be made to regulatory agencies under MMIP 4.4.2, unless urgency requires otherwise, shall first be submitted to the MSC for comments, which comments shall be reflected in any submittal to the ISO Governing Board seeking approval of any such reports or recommendations. All final reports made to external regulatory agencies shall be simultaneously submitted to the MSC.

MMIP 4.5 Market Participants

MMIP 4.5.1 Collection of Data

The Department of Market Analysis may request that Market Participants or other entities whose activities may affect the operation of the ISO markets submit any information or data determined by the Department of Market Analysis to be potentially relevant. This data will be subject to due safeguards to protect confidential and commercially sensitive data. Failures by Market Participants to provide such data shall be treated under the Enforcement Protocol. In the event of failures by other entities to provide such data, the ISO may take whatever action is available to it and appropriate for it to take, including reporting the failure to the pertinent regulatory agency, after providing such entity the opportunity to respond in writing as to the reason for the alleged failure.

and may include possible exclusion from the ISO Markets or termination of any relevant ISO agreements or certifications. Before any such action is taken, the ISO Participant shall be provided the opportunity to respond in writing as to the reason for the alleged failure.

MMIP 4.5.2 Dissemination of Data

Any Market Participant may request that the ISO provide data that the ISO has collected concerning that Market Participant; and, such data may, subject to constraints on the ISO's resources and at the ISO's sole discretion, be provided by the ISO subject to due safeguards to protect confidential and commercially sensitive data. Where such activity imposes a significant burden or expense on the ISO, the data may be provided on the condition that a reasonable contribution to the cost incurred by the ISO is made to the ISO by the requesting party.

MMIP 4.6 External Consulting Assistance and Expert Advice

In carrying out any of its responsibilities under this MMIP 4, including the development of an information system, market monitoring indices and evaluation criteria, and the catalogs associated therewith, and in its analysis and ongoing evaluation of these catalogs and of the Rules of Conduct under MMIP 4.3, the Department of Market Analysis may hire consulting assistance subject to the budgetary approval of the ISO CEO and may seek such expert external advice as it believes necessary.

MMIP 4.7 Liability for Damages

As provided in Section 14.1 and 14.2 of the ISO Tariff, the Department of Market Analysis, the MSC, the ISO CEO and other ISO staff, and the ISO Governing Board shall not be liable to any Market Participant under any circumstances whatsoever for any matter described in those sections, including but not limited to any financial loss or loss of economic advantage resulting from the performance or non-performance by such ISO entities of their functions under this Protocol.

MMIP 5 MARKET SURVEILLANCE COMMITTEE

MMIP 5.1 Establishment

There shall be established on or before ISO Operations Date a Market Surveillance Committee (MSC), whose role it shall be to provide independent external expertise on the ISO market monitoring process as described in this Protocol and, in particular, to provide independent expert advice and recommendations to the ISO CEO and Governing Board. Members of the Committee shall not be, and shall not be understood to be, employees or agents of the ISO.

MMIP 5.2 Composition

MMIP 5.2.1 Qualifications

The MSC shall comprise a body of three or more independent and recognized experts whose combined professional expertise and experience shall encompass the following:

MMIP 5.2.1.1 economics, with emphasis on antitrust, competition, and market power issues in the electricity industry;

MMIP 5.2.1.2 experience in operational aspects of generation and transmission in electricity markets;

MMIP 5.2.1.3 experience in antitrust or competition law in regulated industries; and

MMIP 5.2.1.4 financial expertise relevant to energy or other commodity trading.

MMIP 5.2.2 Criteria for Independence

Each member of the MSC must meet the following criteria for independence:

MMIP 5.2.2.1 no material affiliation, through employment, consulting or otherwise, with any Market Participant or affiliate thereof consistent with the pertinent FERC Standards of Conduct; and

MMIP 5.2.2.2 no material financial interest in any Market Participant or affiliate thereof consistent with the pertinent FERC Standards of Conduct.

MMIP 5.2.2.3 during their time on the Committee, members may not provide paid expert witness testimony or other commercial services to the ISO or to any other party in connection with any legal or regulatory proceeding relating to the ISO or any trade or other transaction involving the ISO markets (except that the Committee may consult with and make

recommendations concerning the functioning of the markets to ISO Management or the ISO Governing Board in connection with legal or regulatory proceedings).

MMIP 5.3 Appointments to the MSC

For each position on the MSC, the ISO CEO shall conduct a thorough search and requisite due diligence to develop a nomination to the ISO Governing Board, which nomination shall be consistent with meeting the combined professional expertise and experience of the MSC set forth in MMIP 5.2.1 and with the criteria for independence set forth in MMIP 5.2.2. The ISO Governing Board shall expeditiously consider such nominations. If the nomination is approved, the ISO CEO shall appoint the candidate so nominated to the MSC. If the nomination is rejected, the ISO CEO shall expeditiously proceed to develop another nomination in accordance with this MMIP.

MMIP 5.4 Compensation and Reimbursements

Members of the MSC shall be compensated on such basis as the ISO Governing Board shall from time to time determine.

Members of the MSC shall receive prompt reimbursement for all expenses reasonably incurred in the execution of their responsibilities under this MMIP 5.

MMIP 5.5 Liability for Damages

As provided in Section 14.1 and 14.2 of the ISO Tariff, the Department of Market Analysis, the MSC, the ISO CEO and other ISO staff, and the ISO Governing Board shall not be liable to any Market Participant under any circumstances whatsoever for any matter described in those sections, including but not limited to any financial loss or loss of economic advantage resulting from the performance or non-performance by such ISO entities of their functions under this Protocol.

MMIP 6 SPECIFIC FUNCTIONS OF MARKET SURVEILLANCE COMMITTEE (MSC)

MMIP 6.1 Information Gathering and Evaluation Criteria

The MSC shall review the initial catalogs of information and data and of evaluation criteria developed by the Department of Market Analysis pursuant to MMIP 4 and shall propose such changes, additions or deletions to such catalogs or items therein as it sees fit. In so doing, the MSC shall have full discretion to specify database items or evaluation criteria for inclusion in the pertinent catalog.

MMIP 6.2 Evaluation of Information

The MSC may, upon request of the Department of Market Analysis, the ISO Management or the ISO Governing Board, or on its own volition, evaluate such information or data, including as may be collected by the Department of Market Analysis on the basis of the evaluation criteria developed by the Department of Market Analysis or on such further articulated evaluation criteria developed by the MSC.

MMIP 6.3 Reports and Recommendations

MMIP 6.3.1 Required Reports

All evaluations carried out by the MSC pursuant to MMIP 6.2, and any recommendations emanating from such evaluations, shall be embodied by the MSC in written reports to the ISO CEO and ISO Governing Board and shall be made publicly available subject to due restrictions on dissemination of confidential or commercially sensitive information. The MSC may submit any MSC report to FERC, subject to due restrictions on dissemination of confidential or commercially sensitive information.

MMIP 6.3.2 Additional Reports

The MSC may make such additional reports and recommendations as it sees fit relating to the monitoring program referred to in this Protocol, the analysis of information, the evaluation criteria or any corrective or enforcement actions proposed by the Department of Market Analysis or proposed of its own volition.

MMIP 6.4 Publication of Reports and Recommendations

Upon request of the MSC, the ISO shall publish reports and recommendations of the MSC or incorporate them, if consistent, into the ISO's own reports or recommendations.

MMIP 7 IMPLEMENTATION OF RECOMMENDATIONS

MMIP 7.1 Plan and Rules of Conduct Changes

Following a recommendation of the MSC, the ISO Governing Board may make such changes as it believes are appropriate to any ISO Protocol or Agreement or to any Rules of Conduct applicable in accordance with MMIP 9.

MMIP 7.2 Tariff Changes

Upon recommendation of the MSC, the ISO Governing Board shall consider and may adopt proposed ISO Tariff changes in accordance with MMIP 9.

MMIP 7.3 Sanctions and Penalties

Upon recommendation of the MSC, the ISO may impose such sanctions or penalties as it believes necessary and as are permitted under the ISO Tariff and related protocols approved by FERC; or it may make any such referral to such regulatory or antitrust agency as it sees fit to recommend the imposition of sanctions and penalties.

MMIP 8 PUBLICATION OF INFORMATION

MMIP 8.1 Market Monitoring Data and Indices

The ISO Department of Market Analysis shall, pursuant to MMIP 4.1, develop a catalog of data and indices. Upon approval of the ISO CEO, such catalogs shall be duly published on the ISO Home Page and disseminated to all Market Participants.

MMIP 8.2 Reports to Regulators

The ISO shall develop annual reports of market performance for delivery to FERC, and such other reports as may be required by FERC, which shall be submitted for review to the MSC. The Department of Market Analysis shall prepare and submit such reports to the ISO CEO, ISO Governing Board and to the regulatory agency concerned.

MMIP 9 AMENDMENTS

If the ISO determines a need for an amendment to this Protocol, the ISO will follow the requirements as set forth in Section 16 of the ISO Tariff.

(e) The Mitigation Measures shall not be applied to Energy bids projected to be Dispatched as Imbalance Energy through the BEEP stack in the hours in which all Zonal BEEP Interval Ex Post Prices are projected to be below \$91.87/MWh. If the zonal BEEP Interval Ex Post Price is projected to be above \$91.87/MWh in any ISO zone, the Mitigation Measures shall be applied to all bids, except those from System Resources, in all ISO zones. The ISO will apply Mitigation Measures to all bids taken out of merit order to address Intra-Zonal Congestion.

(f) The Mitigation Measures shall not be applied to bids below \$25/MWh.

(g) The posting of the MCP may be delayed if necessary for the completion of automated mitigation procedures.

(h) Bids not mitigated under these Mitigation Measures shall remain subject to mitigation by other procedures specified in the ISO Tariff as may be appropriate.

4.3 Sanctions for Physical Withholding

The ISO may report a Market Participant the ISO determines to have engaged in physical withholding, including providing the ISO false information regarding the derating or outage of an Electric Facility, to the Federal Energy Regulatory Commission in accordance with Section 2.3.3.9.5 of the ISO Tariff. In addition, a Market Participant that fails to operate a Generating Unit in conformance with ISO dispatch instructions shall be subject to the penalties set forth in Section 11.2.4.1.2 of the ISO Tariff.

4.4 Duration of Mitigation Measures

Bids will be mitigated only in the specific hour that they violate the price and market impact thresholds.

5 FERC-ORDERED MEASURES

In addition to any mitigation measures specified above, the ISO shall administer, and apply when appropriate in accordance with their terms, such other mitigation measures as it may be directed to implement by order of the FERC.

6 DISPUTE RESOLUTION

- (3) Resource_ID2 (required only for individual interchange schedules and Inter-SC Trades);
- (4) Energy type – firm (FIRM), non-firm (NFIRM), wheeling (WHEEL), dynamic (DYN), Energy (ENGY), Spinning Reserve (CSPN), Non-Spinning Reserve (CNSPN) or Replacement Reserve (CRPLC); and
- (5) Hourly scheduled Energy or Ancillary Service, utilizing the same sign convention as set forth in (g) above.

SBP 2.1.7 No Scheduling Coordinator shall submit a Circular Schedule. The ISO may periodically provide examples of such Circular Schedules under the ISO Home Page.

SBP 2.2 Validation of Balanced Schedules

Each SC will be assigned a workspace within the ISO's scheduling system. Each workspace will have a work area for Day-Ahead and Hour-Ahead Schedules, Adjustment Bids and Supplemental Energy bids. The SC shall only be allowed to access and manipulate its Schedule and bid data within this workspace. Each area is organized into segments. A segment is used to hold the SC's Schedules relating to the same Trading Day. The Schedule validation process is divided into two stages. The ISO shall carry out the first stage validation immediately after it has received a Schedule. The ISO shall carry out the second stage validation ten (10) minutes before (pre-validation) and immediately after each deadline (as specified in the SP) for submission of Schedules. However, a SC can also initiate the stage two validation at any time prior to that deadline, as described in more detail in the SP. If the SC adds a new Schedule or modifies an existing Schedule, that Schedule must be re-validated. SCs must comply with the ISO Data Templates and Validation Rules document, which contains the validation criteria for Balanced Schedules.

SBP 2.2.1 Stage One Validation

During stage one validation, each incoming Schedule will be validated to verify proper content, format and syntax. The ISO will check that the SC had not exceeded its Security Amount and verify that the SC is certified in accordance with the ISO Tariff. The ISO will further verify that the SC has inputted valid Generating Unit and Demand location identification. Scheduled Reliability Must-Run Generation will be verified against the contract reference numbers in the ISO's Scheduling Coordinator database. A technical validation will be performed verifying that a scheduled Generating Unit's output is not beyond its declared capacity and/or operating limits. If there is an error found during stage one validation, the SC will be notified immediately through WEnet. The SC can then look at the notification messages to review the detailed list of errors, make changes, and resubmit the Schedule if it is still within the timing requirements of the SP. Additionally, if the ISO detects an invalid contract usage (of either Existing Contract rights or Firm Transmission Rights), the ISO will issue an error message in similar manner to the SC and allow the SC to view the message(s), to make changes, and to resubmit the contract usage template(s) if it is still

SBP 5.2.3 Validation Checks

The ISO's stage one validation checks are performed automatically whenever Ancillary Services Schedules and bids are submitted, as described in the SP. The ISO's stage two validation is performed automatically in accordance with the timing requirements described in the SP. A SC can also check whether its Ancillary Services Schedules and bids will pass the ISO's stage two validation by manually initiating validation of its Ancillary Services Schedules and bids, as described in the SP, at any time prior to the deadline for submission of Ancillary Services Schedules and bids. It is a SC's responsibility to perform such checks.

SBP 5.3 Buy Back of Ancillary Services

A Scheduling Coordinator who has sold or self-provided Regulation, Spinning Reserve, Non-Spinning Reserve or Replacement Reserve capacity to the ISO in the Day-Ahead Market shall be required to replace such capacity to the extent scheduled self-provision is decreased between the Day-Ahead and Hour-Ahead Markets, or to the extent the Ancillary Service associated with a Generating Unit, Curtailable Demand, or System Resource successfully bid in a Day-Ahead Ancillary Service Market is reduced in the Hour-Ahead Market, for any reason (other than the negligence or willful misconduct of the ISO, or a Scheduling Coordinator's involuntary decrease in such sold capacity or scheduled self-provision on the instruction of the ISO). The price for such replaced Ancillary Service shall be the greater of the Market Clearing Price in the Hour-Ahead Market or the Market Clearing Price in the Day-Ahead Market for the same Settlement Period for the Ancillary Service capacity concerned.

SBP 6 ENERGY BIDS

SCs must submit Energy Bids for resources providing Spinning, Non-Spinning, or Replacement Reserves. The upper portion of the Energy Bid that corresponds to the resource's available capacity up to the highest operating limit, shall be allocated to any awarded or self-provided Ancillary Services in the following order from higher to lower capacity: a) Regulation Up; b) Spinning Reserve; c) Non-Spinning Reserve; and d) Replacement Reserve. For resources providing Regulation Up, the upper regulating limit shall be used if it is lower than the highest operating limit. The remaining portion of the Energy Bid, if there is any, shall constitute Supplemental Energy. Supplemental Energy bids are available to the ISO for procurement and use for Imbalance Energy, additional Voltage Support and Congestion Management in the Real Time Market.

SBP 6.1 Content of Energy Bids

SBP 6.1.1 Generation Section of Energy Bid Data

Each SC offering Spinning, Non-Spinning, or Replacement Reserve, or Supplemental Energy to the ISO will submit the following information for each Generating Unit for each Settlement Period:

the negligence or willful misconduct of the ISO, or a Scheduling Coordinator's involuntary decrease in such sold capacity or scheduled self-provision on the instruction of the ISO). The price for such replaced Ancillary Service shall be at the greater of the Market Clearing Price in the Day-Ahead Market or the Market Clearing Price in the Hour-Ahead Market for the same Settlement Period for the Ancillary Service capacity concerned. Increases in each Scheduling Coordinator's self-provided Ancillary Services between the Day-Ahead and Hour-Ahead Markets shall be limited to the estimated incremental Ancillary Service requirement associated with the increase between the Day-Ahead and Hour-Ahead Markets in that Scheduling Coordinator's scheduled Zonal Load. Notwithstanding this limit on increases in Hour-Ahead self-provision, a Scheduling Coordinator may buy or sell Ancillary Services through Inter-Scheduling Coordinator Ancillary Service Trades in the Hour-Ahead Market;

- (f) due to the design of the ISO's scheduling software, the ISO will not take into account Usage Charges in the evaluation of Ancillary Services bids or in price determination and, in the event of Congestion in the Day-Ahead Market or Hour-Ahead Market, Ancillary Services will be procured and priced on a Zonal basis; and
- (g) due to the design of the ISO's scheduling system, any specific resource can bid to supply a specific Ancillary Service or can self-provide such Ancillary Service but cannot do both in the same Settlement Period.

SP 9.2 Sequential Evaluation of Bids

- (a) When SCs bid into the Regulation, Spinning Reserve, Non-Spinning Reserve and Replacement Reserve markets, the same resource capacity may be offered into more than one of these Ancillary Services markets at the same time. The ISO will evaluate bids in the reserve markets for Regulation, Spinning Reserve, Non-Spinning Reserve and Replacement Reserve sequentially and separately in the following order:
 - (i) Regulation
 - (ii) Spinning Reserve
 - (iii) Non-Spinning Reserve; and
 - (iv) Replacement Reserve.
- (b) SCs are allowed to specify different reserve prices and different Energy prices for each Ancillary Service they bid. SCs can bid the same resource capacity into any one or all of the Ancillary Service markets they desire. Any resource capacity accepted by the ISO in one of these reserve markets will be deducted from the resource capacity bid into the other reserve markets, except that resource

capacity accepted in the Regulation market that represents the downward range of movement accepted by the ISO will not be deducted from the resource capacity bid into other reserve markets.

SP 9.3 Scheduling Ancillary Services Resources

- (a) SCs are allowed to self-provide all or a portion of the following Ancillary Services to satisfy their obligations to the ISO:
 - (i) Regulation;
 - (ii) Spinning Reserve;
 - (iii) Non-Spinning Reserve; and
 - (iv) Replacement Reserve.
- (b) The ISO will reduce the quantity of Ancillary Services it competitively procures by the corresponding amount of the Ancillary Services that SCs self-provide.
- (c) The ISO shall prepare supplier schedules for Ancillary Services (both self-provided and purchased by the ISO) for the Day-Ahead Market and the Hour-Ahead Market.
- (d) The Ancillary Services schedules shall contain the information set out in the SBP for each Settlement Period of the following Trading Day in the case of the Day-Ahead schedules or for a specific Settlement Period in the case of Hour-Ahead schedules.
- (e) Once the ISO has given SCs notice of the Day-Ahead and Hour-Ahead schedules, these schedules represent binding commitments made in the reserve markets between the ISO and the SCs concerned. A Scheduling Coordinator who has sold or self-provided Regulation, Spinning Reserve, Non-Spinning Reserve or Replacement Reserve capacity to the ISO in the Day-Ahead Market shall be required to replace such capacity to the extent scheduled self-provision is decreased between the Day-Ahead and Hour-Ahead Markets, or to the extent the Ancillary Service associated with a Generating Unit, Curtailable Demand, or System Resource successfully bid in a Day-Ahead Ancillary Service Market is reduced in the Hour-Ahead Market, for any reason (other than the negligence or willful misconduct of the ISO, or a Scheduling Coordinator's involuntary decrease in such sold capacity or scheduled self-provision on the instruction of the ISO). The price for such replacement shall be at the greater of the Market Clearing Price in the Hour-Ahead Market or the Market Clearing Price in the Day-Ahead Market for the Ancillary Service for the Settlement Period concerned for the Zone in which the Generating Unit or other resources on behalf of which the Scheduling Coordinator buys back the capacity, are located. The ISO will purchase the Ancillary Service concerned from another Scheduling

- (b) amounts in respect of penalties which may be levied by the ISO in accordance with the ISO Tariff. These charges will be levied on the Market Participants liable for payment of the penalty; and, if applicable, distributed as payments to Scheduling Coordinators entitled to receive them.
- (c) amounts required to reach an accounting trial balance of zero in the course of the Settlement process in the event that the charges calculated as due from ISO Debtors are lower

than payments calculated as due to the ISO Creditors for the same Trading Day. These charges will be allocated amongst the Scheduling Coordinators who traded on that Trading Day pro rata to their metered Demand (including exports) in MWh of Energy for that Trading Day. In the event that the charges due from ISO Debtors are higher than the payments due to ISO Creditors, the ISO shall allocate a payment to the Scheduling Coordinators who traded on that Trading Day pro rata to their metered Demand (including exports) in MWh of Energy for that Trading Day.

- (d) amounts required with respect to payment adjustments for regulating Energy as calculated in accordance with Section 2.5.27.1 of the ISO Tariff. These charges will be allocated amongst the Scheduling Coordinators who traded on that Trading Day pro rata to their metered Demand (including exports) in MWh for that Trading Day.

SABP 3.1.2 Treatment of Amounts Received Through Payments of Penalties

Unless a different allocation method is specified in another section of the ISO Tariff and protocols, the ISO shall hold penalty amounts collected by the ISO, as described in the sections of the ISO Tariff and protocols providing for the payment of penalties, in a trust account until the end of the calendar year, at which time the ISO shall allocate the penalty amounts, and any accrued interest held in the trust account, amongst Scheduling Coordinators in proportion to their metered Demand (including Exports) over the calendar year. The total amount of penalty collections to be allocated shall be determined after first subtracting reasonable costs incurred by the ISO over the calendar year for payments to vendors for equipment or services that are used to investigate violations of Rules of Conduct and administer penalties described in the ISO Enforcement Protocol.

SABP 3.2 Method of Settlement of Charges

SABP 3.2.1 Settlement of Payments to/from Scheduling Coordinators and Participating TOs

The ISO will calculate for each charge the amounts payable by the relevant Scheduling Coordinator, Black Start Generator or Participating TO for each Settlement Period of the Trading Day, and the amounts payable to that Scheduling Coordinator, Black Start Generator or Participating TO for each charge for each Settlement Period of that Trading Day and shall arrive at a net amount payable for each charge by or to that Scheduling Coordinator, Black Start Generator or Participating TO for each charge for that Trading Day. Each of these amounts will appear in the Preliminary and Final Settlement Statements that the ISO will provide to the relevant Scheduling Coordinator, Black Start Generator or Participating TO as provided in SABP 4.

The three components of the Grid Management Charge will be included in the Preliminary Settlement Statement and Final Settlement Statement with the other types of charges referred to in

SABP 3.1, but a separate invoice for the Grid Management Charge, stating the rate, billing determinant volume and total charge for each of its three components, will be issued by the ISO.

SABP 4

SETTLEMENT STATEMENTS

SABP 4.1

Preliminary Settlement Statements

SABP 4.1.1

Timing of Preliminary Settlement Statements

The ISO shall provide to each Scheduling Coordinator, Black Start Generator or Participating TO for validation a Preliminary Settlement Statement for each Trading Day in accordance with the ISO Payments Calendar.

SABP 6.3 Payment Process

SABP 6.3.1 Use of the ISO Clearing Account

- (a) Subject to SABP 6.1.2 each ISO Debtor shall remit to the ISO Clearing Account the amount shown on the invoice as payable by that ISO Debtor for value not later than 10:00 am on the Payment Date.
- (b) On the Payment Date the ISO shall be entitled to cause the transfer of such amounts held in a Scheduling Coordinator's ISO prepayment account to the ISO Clearing Account as provided in SABP 6.1.2(c).

SABP 6.3.1.2 Distribution to ISO Creditors

The ISO shall calculate the amounts available for distribution to ISO Creditors on the Payment Date and shall give irrevocable instructions to the ISO Bank to remit from the ISO Clearing Account to the relevant Settlement Account maintained by each ISO Creditor for same day value the amounts determined by the ISO to be available for payment to each ISO Creditor. If required, the ISO shall instruct the ISO Bank to transfer amounts from the ISO Reserve Account to enable the ISO Clearing Account to clear by the close of banking business on the Payment Date.

SABP 6.3.1.3 Grid Management Charge

The ISO is authorized to instruct the ISO Bank to debit the ISO Clearing Account and transfer to the relevant ISO account sufficient funds to pay in full the Grid Management Charge falling due on any Payment Day with priority over any other payments to be made on that or on subsequent days out of the ISO Clearing Account.

SABP 6.4 Use of the ISO Reserve Account

If there are insufficient funds in the ISO Clearing Account to pay ISO Creditors and clear the account on any Payment Date, due to payment default by one or more ISO Debtors, the ISO shall transfer funds from the ISO Reserve Account to the ISO Clearing Account to clear it by close of banking business on that Payment Date pursuant to SABP 6.7.2.

SABP 6.5 Use of the ISO Surplus Account

SABP 6.5.1 Establishment

The ISO shall establish and maintain a bank account in accordance with this Protocol denominated the "ISO Surplus Account".

SABP 6.5.2 Other Funds Used in the ISO Surplus Account.

- (a) Any amounts paid to the ISO in respect of penalties referred to in SABP 3.1.1, that are not allocated amongst Scheduling Coordinators in proportion to their metered Demand (including Exports), shall be credited to the Surplus Account.

ATTACHMENT D

Changes Concerning Allocation of Penalty Amounts:

SABP 3.1.1 Additional Charges and Payments

The ISO shall be authorized to levy additional charges or payments as special adjustments in regard to:

- (a) amounts required to round up any invoice amount expressed in dollars and cents to the nearest whole dollar amount in order to clear the ISO Clearing Account. These charges will be allocated amongst Scheduling Coordinators over an interval determined by the ISO and pro rata based on metered Demand (including exports) during that interval;
- (b) amounts in respect of penalties which may be levied by the ISO in accordance with the ISO Tariff. These charges will be levied on the Market Participants liable for payment of the penalty; and, if applicable, distributed as payments to Scheduling Coordinators entitled to receive them.
- (c) amounts required to reach an accounting trial balance of zero in the course of the Settlement process in the event that the charges calculated as due from ISO Debtors are lower than payments calculated as due to the ISO Creditors for the same Trading Day. These charges will be allocated amongst the Scheduling Coordinators who traded on that Trading Day pro rata to their metered Demand (including exports) in MWh of Energy for that Trading Day. In the event that the charges due from ISO Debtors are higher than the payments due to ISO Creditors, the ISO shall allocate a payment to the Scheduling Coordinators who traded on that Trading Day pro rata to their metered Demand (including exports) in MWh of Energy for that Trading Day.
- (d) amounts required with respect to payment adjustments for regulating Energy as calculated in accordance with Section 2.5.27.1 of the ISO Tariff. These charges will be allocated amongst the Scheduling Coordinators who traded on that Trading Day pro rata to their metered Demand (including exports) in MWh for that Trading Day.

SABP 3.1.2 Treatment of Amounts Received Through Payments of Penalties

Unless a different allocation method is specified in another section of the ISO Tariff and protocols, the ISO shall hold penalty amounts collected by the ISO, as described in the sections of the ISO Tariff and protocols providing for the payment of penalties, in a trust account until the end of the calendar year, at which time the ISO shall allocate the penalty amounts, and any accrued interest held in the trust account, amongst Scheduling Coordinators in proportion to their metered Demand (including Exports) over the calendar year. The total amount of penalty collections to be allocated shall be determined after first subtracting reasonable costs incurred by the ISO over the calendar year for payments to vendors for equipment or services that are used to investigate violations of Rules of Conduct and administer penalties described in the ISO Enforcement Protocol.

SABP 6.5.2 Other Funds Used in the ISO Surplus Account.

- (a) Any amounts paid to the ISO in respect of penalties referred to in SABP 3.1.1, that are not allocated amongst Scheduling Coordinators in proportion

to their metered Demand (including Exports), shall be credited to the Surplus Account. |

- (b) The funds referred to in SABP 6.5.2(a) pertaining to Penalties as provided in SABP 3.1.1 shall first be applied towards any expenses, loss or costs incurred by the ISO. Any excess will be credited to the Surplus Account pursuant to SABP 6.5.2(a).

Prohibition on Scheduling on Zero-Rated Paths:

2.2.9 ~~{Not Used}~~ Prohibition on Scheduling Across Out-of-Service Transmission Paths

Scheduling Coordinators shall not submit any Schedule using a transmission path for any Settlement Period for which the Operating Transfer Capability for that path is zero MW. The ISO shall reject Schedules submitted for transmission paths on which the Operating Transfer Capability is zero MW. If the Operating Transfer Capability of a transmission path is reduced to zero after Final Day-Ahead Schedules have been submitted, then, if time permits, the ISO shall direct the responsible Scheduling Coordinators to reduce all Schedules on such zero-rated transmission paths to zero in the Hour-Ahead Market. As necessary to comply with Applicable Reliability Criteria, the ISO shall reduce any non-zero Final Hour-Ahead Schedules across zero-rated transmission paths to zero after the close of the Hour-Ahead Market. No Usage Charges will be assessed, nor will any Usage Charges for counter-flow be paid, for Schedules across a path with an Operating Transfer Capability of zero.

APPENDIX A

Master Definitions Supplement:

<u>Operating Transfer Capability</u>	<u>The maximum capability of a transmission path to transmit real power, expressed in MW, at a given point in time.</u>
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Hour-Ahead Ancillary Services Buy-Back:

2.5.21 Scheduling of Units to Provide Ancillary Services.

The ISO shall prepare supplier schedules for Ancillary Services (both self provided and purchased by the ISO) for the Day-Ahead and the Hour-Ahead Markets. The ISO shall notify each Scheduling Coordinator no later than 1:00 p.m. of the day prior to the Trading Day of their Ancillary Services schedules for the Day-Ahead and no later than one hour prior to the operating hour of their Ancillary Services schedules for the Hour-Ahead. The ISO Protocols set forth the information, which will be included in these schedules. Where long-term contracts are involved, the information may be treated as standing information for the duration of the contract.

If, at any time after the issuance of Final Day-Ahead Schedules for the Trading Day and before the close of the Hour-Ahead Market for the first Settlement Period of the Trading Day, the ISO determines that it requires Ancillary Services in addition to those included in the Final Day-Ahead Schedule (in the appropriate zone if procuring zonally), the ISO may procure such additional Ancillary Services by providing Scheduling Coordinators with amended supplier schedules for the Day-Ahead Markets that include Ancillary Services for which previously submitted (but not selected) bids remain available and have not previously been withdrawn. The ISO shall select such Ancillary Services in price merit order (and in the relevant zone if the ISO is procuring Ancillary Services on a zonal basis). Such amended supplier schedules shall be provided to the Scheduling Coordinators no later than the close of the Hour-Ahead Market for the first Settlement Period of the Trading Day.

Once the ISO has given Scheduling Coordinators notice of the Day-Ahead and Hour-Ahead schedules, these schedules represent binding commitments made in the markets between the ISO and the Scheduling Coordinators concerned, subject to any amendments issued as described above. Any minimum energy input and output associated with Regulation and Spinning Reserve services shall be the responsibility of the Scheduling Coordinator, as the ISO's auction does not compensate the Scheduling Coordinator for the minimum energy output of Generating Units bidding to provide these

services. Accordingly the Scheduling Coordinators shall adjust their schedules to accommodate the minimum outputs required by the Generating Units included on the Schedules.

Notwithstanding the foregoing, a Scheduling Coordinator who has sold or self-provided Regulation, Spinning Reserve, Non-Spinning Reserve or Replacement Reserve capacity to the ISO in the Day-Ahead Market shall be required to replace that capacity in whole or in part from the ISO if the scheduled self-provision is decreased between the Day-Ahead and Hour-Ahead Markets, or if the Ancillary Service associated with a Generating Unit, Curtailable Demand, or System Resource successfully bid in a Day-Ahead Ancillary Service Market is reduced in the Hour-Ahead Market, for any reason (other than the negligence or willful misconduct of the ISO, or a Scheduling Coordinator's involuntary decrease in such sold capacity or scheduled self-provision on the instruction of the ISO). The price for such replaced Ancillary Service shall be the greater of the Market Clearing Price in the Hour-Ahead Market or the Market Clearing Price in the Day-Ahead Market for the Ancillary Service for the Settlement Period concerned for the Zone in which the Generating Units or other resources are located. The ISO will purchase the Ancillary Service concerned from another Scheduling Coordinator in the Hour-Ahead Market in accordance with the provisions of the ISO Tariff.

* * *

Schedules and Bids Protocol:

SBP 5.3 Buy Back of Ancillary Services

A Scheduling Coordinator who has sold or self-provided Regulation, Spinning Reserve, Non-Spinning Reserve or Replacement Reserve capacity to the ISO in the Day-Ahead Market shall be required to replace such capacity to the extent scheduled self-provision is decreased between the Day-Ahead and Hour-Ahead Markets, or to the extent the Ancillary Service associated with a Generating Unit, Curtailable Demand, or System Resource successfully bid in a Day-Ahead Ancillary Service Market is reduced in the Hour-Ahead Market, for any reason (other than the negligence or willful misconduct of the ISO, or a Scheduling Coordinator's involuntary decrease in such sold capacity or scheduled self-provision on the instruction of the ISO). The price for such replaced Ancillary Service shall be the greater of the Market Clearing Price in the Hour-Ahead Market or the Market Clearing Price in the Day-Ahead Market for the same Settlement Period for the Ancillary Service capacity concerned.

* * *

Scheduling Protocol:

SP 9.1 Bid Evaluation and Scheduling Principles

The ISO will evaluate Ancillary Services bids based on the following principles:

- (a) the ISO will not differentiate between bidders other than through reserve (Regulation and Operating Reserves) price and capability to provide the reserve service, and the required locational mix of services;
- (b) to minimize the costs to users of the ISO Controlled Grid, the ISO will select the bidders with lowest bids for reserve which meet its technical requirements, including location and operating capability;
- (c) the ISO will (to the extent available) procure sufficient Ancillary Services to meet its technical requirements as defined in the ASRP;
- (d) the ISO will evaluate and price only those Ancillary Services bids received in accordance with the SBP;
- (e) the ISO will require SCs to honor their Day-Ahead Ancillary Services schedules and/or bids when submitting their Hour-Ahead Ancillary Services schedules and/or bids. A Scheduling Coordinator who has sold or self-provided Regulation, Spinning Reserve, Non-Spinning Reserve or Replacement Reserve capacity to the ISO in the Day-Ahead Market shall be required to replace such capacity to the extent scheduled self-provision is decreased between the Day-Ahead and Hour-Ahead Markets, or to the extent the Ancillary Service associated with a Generating Unit, Curtailable Demand, or System Resource successfully bid in a Day-Ahead Ancillary Service Market is reduced in the Hour-Ahead Market, for any reason (other than the negligence or willful misconduct of the ISO, or a Scheduling Coordinator's involuntary decrease in such sold capacity or scheduled self-provision on the instruction of the ISO). The price for such replaced Ancillary Service shall be at the greater of the Market Clearing Price in the Day-Ahead Market or the Market Clearing Price in the Hour-Ahead Market for the same Settlement Period for the Ancillary Service capacity concerned. Increases in each Scheduling Coordinator's self-provided Ancillary Services between the Day-Ahead and Hour-Ahead Markets shall be limited to the estimated incremental Ancillary Service requirement associated with the increase between the Day-Ahead and Hour-Ahead Markets in that Scheduling Coordinator's scheduled Zonal Load. Notwithstanding this limit on increases in Hour-Ahead self-provision, a Scheduling Coordinator may buy or sell Ancillary Services through Inter-Scheduling Coordinator Ancillary Service Trades in the Hour-Ahead Market;
- (f) due to the design of the ISO's scheduling software, the ISO will not take into account Usage Charges in the evaluation of Ancillary Services bids or in price determination and, in the event of Congestion in the Day-Ahead Market or Hour-Ahead Market, Ancillary Services will be procured and priced on a Zonal basis; and
- (g) due to the design of the ISO's scheduling system, any specific resource can bid to supply a specific Ancillary Service or can self-provide such Ancillary Service but cannot do both in the same Settlement Period.

SP 9.3

Scheduling Ancillary Services Resources

- (a) SCs are allowed to self-provide all or a portion of the following Ancillary Services to satisfy their obligations to the ISO:
 - (i) Regulation;
 - (ii) Spinning Reserve;
 - (iii) Non-Spinning Reserve; and
 - (iv) Replacement Reserve.
- (b) The ISO will reduce the quantity of Ancillary Services it competitively procures by the corresponding amount of the Ancillary Services that SCs self-provide.
- (c) The ISO shall prepare supplier schedules for Ancillary Services (both self-provided and purchased by the ISO) for the Day-Ahead Market and the Hour-Ahead Market.
- (d) The Ancillary Services schedules shall contain the information set out in the SBP for each Settlement Period of the following Trading Day in the case of the Day-Ahead schedules or for a specific Settlement Period in the case of Hour-Ahead schedules.
- (e) Once the ISO has given SCs notice of the Day-Ahead and Hour-Ahead schedules, these schedules represent binding commitments made in the reserve markets between the ISO and the SCs concerned. A Scheduling Coordinator who has sold or self-provided Regulation, Spinning Reserve, Non-Spinning Reserve or Replacement Reserve capacity to the ISO in the Day-Ahead Market shall be required to replace such capacity to the extent scheduled self-provision is decreased between the Day-Ahead and Hour-Ahead Markets, or to the extent the Ancillary Service associated with a Generating Unit, Curtailable Demand, or System Resource successfully bid in a Day-Ahead Ancillary Service Market is reduced in the Hour-Ahead Market, for any reason (other than the negligence or willful misconduct of the ISO, or a Scheduling Coordinator's involuntary decrease in such sold capacity or scheduled self-provision on the instruction of the ISO). The price for such replacement shall be at the greater of the Market Clearing Price in the Hour-Ahead Market or the Market Clearing Price in the Day-Ahead Market for the Ancillary Service for the Settlement Period concerned for the Zone in which the Generating Unit or other resources on behalf of which the Scheduling Coordinator buys back the capacity, are located. The ISO will purchase the Ancillary Service concerned from another Scheduling Coordinator in the Hour-Ahead Market in accordance with the provisions of the ISO Tariff.
- (f) Any minimum Energy output associated with Regulation and Spinning Reserve services shall be the responsibility of the SC, as the ISO's auction does not compensate the SC for the minimum Energy output of its Generating Units or System Unit, if any, bidding to provide these services. Accordingly, the SCs shall adjust their Balanced Schedules to accommodate the minimum Energy outputs required by the Generating Units or System Units, if any, included in the Ancillary Services schedules.
- (g) SCs providing one or more of the Ancillary Services cannot change the identification of the Generating Units System Units or external imports of System Resources, if any, or Curtailable Demands offered in the Day-Ahead Market, in the Hour-Ahead Market, or in the Real Time Market (except with respect to System Units, if any, in which case SCs are required to identify and disclose the resource specific information for all Generating Units and

Curtable Demands constituting the System Unit scheduled or bid into the ISO's Day-Ahead Market and Hour-Ahead Market as required in SP 3.3.2(e).

Changes Concerning Cut Counter-Flow Schedules:

7.3.1.5.2 If a Scheduling Coordinator fails to provide the scheduled flows in a counter direction, it must reimburse the ISO for the ISO's costs of buying or selling Imbalance Energy in each of the Zones affected by the non-provided scheduled flows in a counter direction, at the ISO's Zonal Imbalance Energy prices. That is, for any Scheduling Coordinator that does not produce, in real time, the amount of Energy scheduled in the Day-Ahead Market or Hour-Ahead Market will be deemed to have purchased/sold the amount of Energy under/over produced in the real time imbalance market at the real time price. In addition, to the extent that any Scheduling Coordinator would receive a Usage Charge payment for Energy that was scheduled in a counter direction over an inter-tie in the Day-Ahead or Hour-Ahead Market but was not delivered in real time, that Usage Charge payment will be eliminated, pro rata, based on the difference between the scheduled counter-flow in the Hour-Ahead Market, and the final real-time Schedule in the counter direction.

For purposes of any adjustments to Usage Charges under this provision, scheduled flows in the counter direction and any related Usage Charges shall be determined relative to the direction of the final Hour-Ahead flow on the inter-tie. If Congestion reverses direction in the Hour-Ahead relative to Day-Ahead, the Day-Ahead Usage Charge deemed to have been paid to the Scheduling Coordinator in the counter direction is \$0/MWh (not the negative of the Day-Ahead Usage Charge).

* * *

Changes Concerning Schedules and Bids Being Binding Obligations:

2.3.1.2.1 Comply with Operating Orders Issued. With respect to this Section 2.3.1.2, all Market Participants within the ISO Control Area and all System Resources shall comply fully and promptly with the ISO's operating orders, unless such operation would impair public health or safety. In this regard, Final Hour-Ahead Schedules for Energy for Generating Units, System Resources, System Units, and Curtailable Demand are deemed to be operating orders. As such, these Schedules are binding obligations and must be fulfilled unless otherwise directed by the ISO. Any Hour-Ahead Ancillary Services Schedule or Supplementary Energy Bid is a binding obligation, and a resource so scheduled or bid cannot be made unavailable or otherwise fail to respond to ISO operating orders except for conditions beyond the control of the resource owner. Any Day-Ahead commitment of a resource, either self-scheduled or committed in the Day-Ahead Market, is a binding obligation, and such resource cannot be de-committed or otherwise be made unavailable except for conditions beyond the control of the resource owner or as approved by the ISO. The ISO will honor the terms of Existing Contracts, except during a System Emergency and circumstances in which the ISO considers that a System Emergency is imminent or threatened. In a System Emergency and circumstances in which the ISO considers that a System Emergency is imminent or threatened, Existing Rights Holders must follow ISO operating orders even if those operating orders conflict with the terms of Existing Contracts. For this purpose ISO operating orders to shed Load shall not be considered as an impairment to public health or safety.

* * *

Draft Proposed New Tariff Section Addressing Circular Schedules:

7.3.1.5.3 Scheduling Coordinators shall not receive a Usage Charge payment for scheduled flows in a counter direction if such scheduled flow is the result of a Circular Schedule.

APPENDIX A

Master Definitions Supplement:

<u>Circular Schedule</u>	<u>A Schedule or set of Schedules that creates a closed loop of Energy Schedules between the ISO Controlled Grid and one or more other Control Areas that do not have a source and sink in separate Control Areas, which includes Energy scheduled in a counter direction over a Congested Inter-Zonal Interface through two or more Scheduling Points. A closed loop of Energy Schedules that includes a transmission segment on the Pacific DC Intertie shall not be a Circular Schedule because such a Schedule directly changes power flows on the network and can mitigate Congestion between SP15 and NP15.</u>
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Schedules and Bids Protocol:

SBP 2.1.7 No Scheduling Coordinator shall submit a Circular Schedule. The ISO may periodically provide examples of such Circular Schedules under the ISO Home Page.

Sharing Confidential Information with Oversight and Enforcement Agencies:

20.3.5 Disclosure to Oversight and Enforcement Agencies

Notwithstanding anything in this Section 20.3 to the contrary, the ISO may disclose information otherwise required to be maintained in confidence under the ISO Tariff to an Oversight and Enforcement Agency, on the terms and conditions hereinafter described.

(a) The ISO may disclose to an Oversight and Enforcement Agency individual bids, schedules, outage plans, and other information routinely collected by the ISO for purposes of monitoring the ISO markets and analyzing market performance, subject to the limitations stated below. The ISO may make such disclosures to an Oversight and Enforcement Agency on a routine or periodic basis, with or without advance notice to Market Participants, if all of the following requirements have been met:

- (1) The ISO has identified each category of information that it intends to disclose to an Oversight and Enforcement Agency under this Section 20.3.5 in a market notice issued at least thirty (30) days in advance of the disclosure;
- (2) Each category of information that the ISO proposes to disclose is of a type wherein each Market Participant has access to that portion of the information pertaining to it (e.g., an Energy Bid) contemporaneous with the disclosure, through each Market Participant's systems or records;
- (3) The proposed disclosure relates to the ISO markets as a whole and is comprised of information on all Market Participants for which such information is available to the ISO, rather than comprised of a subset of available information focusing on a particular Market Participant or Market Participants; and
- (4) Each of the Oversight and Enforcement Agencies to which the ISO makes such disclosure is bound legally, by virtue of applicable law, regulation, protective order, contract, or other means, to treat the information as confidential under terms no less protective than the requirements stated in subsection (c) below.

(b) The ISO may disclose any information required to be maintained in confidence under the ISO Tariff to any of the Oversight and Enforcement Agencies, without meeting the requirements stated in subsection (a) above, if all of the following requirements have been met:

(1) The ISO has a reasonable belief that the Market Participant or Market Participants to which the disclosure pertains may have violated an applicable market rule, tariff provision, protocol, regulation, or law;

(2) Each of the Oversight and Enforcement Agencies to which the information is to be disclosed has oversight or enforcement authority over the potential violation;

(3) The ISO has a reasonable belief that the information to be disclosed would be relevant to an investigation of the potential violation;

(4) The ISO provides notice to the Market Participant or Market Participants that is or are the subject of the disclosure five (5) business days in advance of the proposed disclosure, unless affording such notice could jeopardize a pending or anticipated investigation by the ISO or by the Oversight and Enforcement Agency to whom the disclosure is to be made, in which case, no notice will be required; and

(5) Each of the Oversight and Enforcement Agencies to which the ISO makes such disclosure is bound legally, by virtue of applicable law, regulation, protective order, contract or other means, to treat the information as confidential under terms no less protective than the requirements stated in subsection (c) below.

(c) Each of the Oversight and Enforcement Agencies to which information is disclosed under this section must be bound, at a minimum, to a legal obligation that sets forth in writing the terms applicable to the treatment of confidential and/or commercially sensitive information, and that obligates the agency not to disclose to any third party information provided under this section without providing written notice to the ISO and the Market Participant that is the subject of the disclosure at least five (5) business days in advance of the intended date of release. The Market Participant may, at its sole discretion and own cost, direct any challenge to or defense against the proposed disclosure and the ISO shall cooperate as provided in Section 20.3.4(b).

(d) Nothing in this section shall limit the ability of an Oversight and Enforcement Agency to seek information in accordance with the provisions of Section 20.3.4(b), nor limit the ability of the ISO to disclose information in accordance with that section.

APPENDIX A

Master Definitions Supplement:

<u>Oversight and Enforcement Agency</u>	<u>Any of the following: FERC, the United States Department of Justice or any of its subdivisions, the California Department of Justice or any of its subdivisions, the California Public Utilities Commission, or the California Electricity Oversight Board.</u>
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ISO MARKET MONITORING AND INFORMATION PROTOCOL

Table of Contents

MMIP 1	OBJECTIVES, DEFINITIONS, AND SCOPE	494
MMIP 1.1	Objectives	494
MMIP 1.1.1	Means and Actions	494
MMIP 1.1.2	Reporting Requirements	494
MMIP 1.2	Definitions	494
MMIP 1.2.1	Master Definitions Supplement	494
MMIP 1.2.2	Special Terms for This Protocol	495
MMIP 1.2.3	Rules of Interpretation	495
MMIP 1.3	Scope	495
MMIP 1.3.1	Scope of Application to Parties	495
MMIP 1.3.2	Liability of ISO	495
MMIP 2	PRACTICES SUBJECT TO SCRUTINY	495A
MMIP 2.1	Practices Subject to Scrutiny – General	495A
MMIP 2.1.1	Anomalous Market Behavior	496
MMIP 2.1.2	Abuse of Reliability Must-Run Unit Status	496
MMIP 2.1.3	Gaming	496
MMIP 2.1.4	ISO and PX Other Market Design Flaws	497
MMIP 2.1.5	Market Structure Flaws	497
MMIP 2.2	<u>Scrutiny of Participant Changes Potentially Affecting Market Structure</u> Practices Subject to Scrutiny Pending Divestiture	497
MMIP 2.2.1	Exercises of Horizontal Market Power	497
MMIP 2.2.2	IOU Mitigation Plans	497
MMIP 2.2.3	Effects Pending Divestiture	498
MMIP 2.3	Response Action by ISO	498
MMIP 2.3.1	Corrective Actions	498
MMIP 2.3.2	Further Actions	498
MMIP 2.3.3	Response to Gaming Behavior	499
MMIP 2.3.4	Adverse Effects of Transition Mechanisms	499

MMIP 3	<u>ISO DEPARTMENT OF MARKET ANALYSIS</u> <u>SURVEILLANCE UNIT</u>	500
MMIP 3.1	Establishment	500
MMIP 3.2	Composition	500
MMIP 3.3	Accountability and Responsibilities	500
MMIP 3.3.1	<u>Department of Market Analysis</u> <u>Surveillance Unit</u>	500
MMIP 3.3.2	CEO and ISO-MSO	500
MMIP 3.3.3	Chief Executive Officer (CEO)	500
MMIP 3.3.4	Regulatory and Antitrust Enforcement Agencies	501
MMIP 3.3.5	Complaints	501
MMIP 4	<u>SPECIFIC FUNCTIONS OF ISO MARKET SURVEILLANCE UNIT</u> <u>DEPARTMENT OF MARKET ANALYSIS</u>	501
MMIP 4.1	Information Gathering and Market Monitoring Indices for Evaluation	501
MMIP 4.1.1	Information System	501
MMIP 4.1.2	Data Categories	501
MMIP 4.1.3	Catalog of Market Monitoring Indices	502
MMIP 4.2	Evaluation of Information	502
MMIP 4.2.1	Ongoing Evaluation	502
MMIP 4.2.2	Submission of Evaluation Results	502
MMIP 4.3	<u>Review of Activity-Rules of Conduct</u>	502
MMIP 4.4	Reports and Recommendations	502
MMIP 4.4.1	ISO CEO and Governing Board	502
MMIP 4.4.2	Regulatory Agencies	503
MMIP 4.4.3	ISO Market Surveillance Committee	503
MMIP 4.5	<u>ISO Market Participants</u>	503
MMIP 4.5.1	Collection of Data	503
MMIP 4.5.2	Provision of Data by ISO Participants	503
MMIP 4.5.2 ³	Dissemination of Data	504
MMIP 4.6	External Consulting Assistance and Expert Advice	504
MMIP 4.7	<u>Cooperation with PX Compliance Unit and Market Monitoring Committee</u>	504
MMIP 4.7⁸	Liability for Damages	505

MMIP 5	ISO-MARKET SURVEILLANCE COMMITTEE	505
MMIP 5.1	Establishment	505
MMIP 5.2	Composition	505
MMIP 5.2.1	Qualifications	505
MMIP 5.2.2	Criteria for Independence	505
MMIP 5.3	Appointments to the ISO-MSC	506
MMIP 5.4	Compensation and Reimbursements	506
MMIP 5.5	Liability for Damages	506
MMIP 6	SPECIFIC FUNCTIONS OF ISO MARKET SURVEILLANCE COMMITTEE (ISO-MSC)	506
MMIP 6.1	Information Gathering and Evaluation Criteria	506
MMIP 6.2	Evaluation of Information	506
MMIP 6.3	Reports and Recommendations	507
MMIP 6.3.1	Required Reports	507
MMIP 6.3.2	Additional Reports	507
MMIP 6.4	Publication of Reports and Recommendations	507
MMIP 7	IMPLEMENTATION OF RECOMMENDATIONS	507
MMIP 7.1	Plan and <u>Activity-Rules of Conduct</u> Changes	507
MMIP 7.2	Tariff Changes	507
MMIP 7.3	Sanctions and Penalties	507
MMIP 8	PUBLICATION OF INFORMATION	508
MMIP 8.1	Market Monitoring Data and Indices	508
MMIP 8.2	Regular Information Publication	508
MMIP 8.23	Reports to Regulators	508
MMIP 9	AMENDMENTS	508

**ISO Market Monitoring and
Information Protocol (MMIP)**

MMIP 1 OBJECTIVES, DEFINITIONS, AND SCOPE

MMIP 1.1 Objectives

This Protocol (MMIP) sets forth the workplan and, where applicable, the rules under which the ISO Department of Market Analysis and ISO Market Surveillance Committee will monitor the ISO Markets to identify abuses of market power, to ensure to the extent possible the efficient working of the ISO Markets immediately upon commencement of their operation, and to provide for their protection from abuses of market power in both the short term and the long term, and from other abuses that have the potential to undermine their effective functioning or overall efficiency in accordance with Section 16.3 of the ISO Tariff. Such monitoring activities will be carried out by, among other ISO departments, the ISO Department of Market Analysis Surveillance Unit and the ISO Market Surveillance Committee to be established and to operate under the terms of this Protocol, as set forth below. These protocols provide a general framework for the operation of the Department of Market Analysis and the Market Surveillance Committee and are not intended to limit the activities or remedies available to these entities or to the ISO as a whole elsewhere in the ISO Tariff or otherwise under law.

MMIP 1.1.1 Means and Actions

This Protocol sets forth ~~the general~~ means of data collection, analysis, decision-making, ~~and~~ formulation of corrective actions, ~~and enforcement actions~~ that will be instituted or undertaken by the ISO Department of Market Analysis and ISO Market Surveillance Committee. It describes ~~the~~ implementation mechanisms to be created by the ISO to serve these purposes.

MMIP 1.1.2 Reporting Requirements

This Protocol sets forth the information dissemination, publication and reporting activities and other means of providing information that the ISO generally will undertake to meet its reporting requirements to regulatory agencies, ~~ISO~~Market Participants and others. The goal of the reporting provisions of this Protocol is to adequately inform regulatory agencies, law enforcement agencies, policymakers, ISOMarket Participants and others of the state of the ISO Markets, especially their competitiveness and efficiency. This function is designed to facilitate efficient corrective actions to be taken by the appropriate body or bodies when required.

MMIP 1.2 Definitions

MMIP 1.2.1 Master Definitions Supplement

Any word or expression defined in the Master Definitions Supplement to the ISO Tariff shall have the same meaning where used in this Protocol. References to a Section or Appendix are to a Section or an Appendix of

the ISO Tariff. References to MMIP are to this Protocol or to the stated section, paragraph or appendix of this Protocol.

MMIP 1.2.2 Special Terms for This Protocol

In this Protocol, the following words and expressions shall have the meanings set opposite them:

“Department of Market Analysis (DMA) Surveillance Unit” means the unit established under MMIP 3.1.

“Rules of Conduct” has the same meaning as provided for in the Enforcement Protocol.

“ISO Market Surveillance Committee (ISO-MSC)” means the committee established under MMIP 5.1.

“Activity Rules” means the rules relating to the activities of ISO or PX Participants set forth in or referred to in the ISO and PX Tariff and Protocols.

“ISO Home Page” means the ISO internet home page at <http://www.caiso.com> or such other internet address as the ISO shall publish from time to time.

MMIP 1.2.3 Rules of Interpretation

MMIP 1.2.3.1 Unless the context otherwise requires, if the provisions of this Protocol ~~conflict with~~ the ISO Tariff ~~and/or the Enforcement Protocol~~ conflict, the ISO Tariff ~~and the Enforcement Protocol~~ will prevail to the extent of the inconsistency. The provisions of the ISO Tariff have been summarized or repeated in this Protocol only to aid understanding.

MMIP 1.2.3.2 A reference in this Protocol to a given agreement, ISO Protocol or instrument shall be a reference to that agreement or instrument as modified, amended, supplemented or restated through the date as of which such reference is made.

MMIP 1.2.3.3 The captions and headings in this MMIP are inserted solely to facilitate reference and shall have no bearing upon the interpretation of any of the terms and conditions of this Protocol.

MMIP 1.2.3.4 This Protocol shall be effective as of January 1, 1998. Any amendment to this Protocol shall be effective as of the date of such amendment, or as of the date such amendment is approved by FERC.

MMIP 1.3 Scope

MMIP 1.3.1 Scope of Application to Parties

The MMIP applies to:

MMIP 1.3.1.1 All ISO Market Participants;

~~**MMIP 1.3.1.2** PX Participants;~~

MMIP 1.3.1.23 The ISO;

MMIP 1.3.1.3 The Market Surveillance Committee.

MMIP 1.3.2 Liability of ISO

Any liability of the ISO arising out of or in relation to this Protocol shall be subject to Section 14 of the ISO Tariff as if references to the ISO Tariff were references to this Protocol.

MMIP 2 PRACTICES SUBJECT TO SCRUTINY

MMIP 2.1 Practices Subject to Scrutiny - General

~~The Market Surveillance Unit~~Department of Market Analysis shall monitor the activities of Market Participants and other entities described in MMIP 1.3.1. It shall monitor such activities that affect the operation of the ISO Markets and that provide indications of the phenomena set forth below in this Section 2.1, and, where appropriate, it will take such further action as it considers necessary under Section 2.3.

MMIP 2.1.1 Anomalous Market Behavior

Anomalous market behavior, which is defined as behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or as behavior leading to unusual or unexplained market outcomes. Evidence of such behavior may be derived from a number of circumstances, including:

- MMIP 2.1.1.1** withholding of Generation capacity under circumstances in which it would normally be offered in a competitive market;
- MMIP 2.1.1.2** unexplained or unusual redeclarations of availability by Generators;
- MMIP 2.1.1.3** unusual trades or transactions;
- MMIP 2.1.1.4** pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions, e.g., prices and bids that appear consistently excessive for or otherwise inconsistent with such conditions; and
- MMIP 2.1.1.5** unusual activity or circumstances relating to imports from or exports to other markets or exchanges.

~~The Market Surveillance Unit~~Department of Market Analysis shall evaluate, on an ongoing basis, whether the continued or persistent presence of such circumstances indicates the presence of behavior that is designed to or has the potential to distort the operation and efficient functioning of a competitive market, e.g., the strategic withholding and redeclaring of capacity, and whether it indicates the presence and exercise of market power or of other unacceptable practices.

MMIP 2.1.2 Abuse of Reliability Must-Run Unit Status

Where Generating Units are determined by the ISO to be Reliability Must-Run Units, circumstances that indicate that such Generating Units are being operated in a manner that will adversely affect the competitive nature and efficient workings of the ISO Markets.

MMIP 2.1.3 Gaming

"Gaming", or taking unfair advantage of the rules and procedures set forth in the PX or ISO Tariffs, Protocols or Activity Rules of Conduct, or of transmission constraints in periods in which exist substantial

Congestion, to the detriment of the efficiency of, and of consumers in, the ISO Markets. "Gaming" may also include taking undue advantage of other conditions that may affect the availability of transmission and generation capacity, such as loop flow, facility outages, level of hydropower output or seasonal limits on energy imports from out-of-state, or actions or behaviors that may otherwise render the system and the ISO Markets vulnerable to price manipulation to the detriment of their efficiency.

MMIP 2.1.4 ISO and ~~PX~~Other Market Design Flaws

Design flaws and inefficiencies in the ISO Tariff, ISO Protocols and operational rules and procedures of the ISO, including the potential for problems between the ISO and other independent power markets or exchanges including the PX, insofar as they affect the ISO Markets, which may be evident from anomalous market behavior monitored under MMIP 2.1.1 above, from evidence of gaming monitored under MMIP 2.1.3 above, or from other activities.

MMIP 2.1.5 Market Structure Flaws

With respect to flaws in the overall structure of the California energy markets that may reveal undue concentrations of market power in Generation or other structural flaws, the ~~Market Surveillance Unit~~Department of Market Analysis shall provide such information or evidence of such flaws and such analysis as it may conduct to the ISO CEO ~~and/or, the ISO Market Surveillance Committee~~ or to the ISO Governing Board, subject to due protections of confidential or commercially sensitive information. After due internal consultation, if instructed by any of such ISO institutions or persons, the ~~Market Surveillance Unit~~Department of Market Analysis shall also provide such information or evidence to the Market Surveillance Committee, the appropriate regulatory and antitrust enforcement agency or agencies, subject to due protections of confidential or commercially sensitive information. The ~~Market Surveillance Unit~~Department of Market Analysis shall, at the direction of the ISO CEO and/or the ISO Governing Board, or their designee, provide such other evidence, views, analyses or testimony as may be appropriate or required and as it is reasonably capable of providing to assist the investigations of such agencies.

MMIP 2.2 ~~Practices Subject to Scrutiny Pending Divestiture~~Scrutiny of Participant Changes Potentially Affecting Market Structure

~~In the transition periods pending completion of the various divestiture plans undertaken by certain of the IOU's ("the pre-divestiture period"),~~ ~~†The Market Surveillance Unit~~Department of Market Analysis ~~may shall~~ undertake the following measures to monitor the special circumstances that may affect the operation of the ISO Markets due to corporate reorganizations including bankruptcies or changes in affiliate relationships during this period and may recommend corrective actions as provided in Section 2.3.

MMIP 2.2.1 Exercises of Horizontal Market Power

~~The Market Surveillance Unit~~Department of Market Analysis may shall consider analyze the impact of changes in market structure on the ability of issues that have been raised that some ISO Market Participants may be able to exercise short-term horizontal market power in the short term during this transition period.

MMIP 2.2.2 IOU Mitigation Plans

~~The Market Surveillance Unit shall review all IOU mitigation plans, as approved and modified by the FERC and other regulatory agencies, that might affect the competitiveness of and the efficient operation of the ISO Markets. In consultation with the Compliance Unit of the PX, the Market Surveillance Unit shall analyze what further actions may be necessary to ensure the effective implementation of these mitigation plans with respect to the ISO Markets, and may make such recommendations for further actions as it considers appropriate to the ISO CEO and Governing Board, the FERC, the CPUC or other regulatory agencies. The Market Surveillance Unit shall monitor the ongoing implementation of such plans to the extent feasible within the area of its responsibility, capability and resources.~~

MMIP 2.2.3 Effects Pending Divestiture

~~In the pre-divestiture period, the Market Surveillance Unit shall monitor and analyze the combined effect of the operations of the CTC and the rate freeze under which the Companies are required to operate during the pre-divestiture period on the state of competition in and the efficient operation of the ISO Markets; and the Market Surveillance Unit shall consult with the Compliance Unit of the PX with respect to such effects on both the PX and ISO Markets.~~

MMIP 2.3 Response Action by ISO

MMIP 2.3.1 Corrective Actions

Where the monitoring activities or any consequent investigations carried out by the ~~Market Surveillance Unit~~Department of Market Analysis pursuant to MMIP 2 and MMIP 4 reveal a significant possibility of the presence of or potential for exercises of market power that would adversely affect the operation of the ISO Markets, or ~~other~~the markets interconnected to or interdependent on the ISO Markets, administered by the PX or otherwise operating in the State of California, the ~~Market Surveillance Unit~~Department of Market Analysis shall take the appropriate measures under this section and under MMIP 4, 6, and 7 to institute the corrective action most effective and appropriate for the situation or, in the case of markets ~~administered by the PX or otherwise operating in the State of California~~interconnected to or interdependent on the ISO Markets, the ~~Market Surveillance Unit~~Department of Market Analysis may recommend corrective actions to the PX or to the appropriate regulatory agencies.

MMIP 2.3.2 Further Actions

Where the monitoring activities of or any consequent investigations carried out by the ~~Market Surveillance Unit~~ Department of Market Analysis pursuant to MMIP 2.1 and 2.2 reveal that activities or behavior of Market Participants in the ISO Markets have the effect of, or potential for, undermining the efficiency, workability or reliability of the ISO Markets to give or to serve such Market Participants an unfair competitive advantage over other Market Participants, the ~~Market Surveillance Unit~~ Department of Market Analysis shall fully investigate and analyze the effect of such activities or behavior and, where appropriate, make recommendations to the ISO CEO and the ISO ~~Governing Board~~ MSC for further action by the ISO or, where necessary, by other entities. The ISO may publicize such activities or behavior and its recommendations thereof, in whatever medium it believes most appropriate. The ~~Market Surveillance Unit~~ Department of Market Analysis may, where appropriate, make specific recommendations to the ISO CEO and to the ISO Governing Board for amendment to rules and protocols under its control, ~~or for referral to the PX as to rules and protocols under the PX's control, or for changes to the structure of the ISO Markets, or by referral to the PX, of the markets administered by the PX,~~ and the ~~Market Surveillance Unit~~ Department of Market Analysis may recommend actions, including fines or suspensions, against specific entities in order to deter such activities or behavior.

MMIP 2.3.3 Response to Gaming Behavior

If evidence of "gaming" or taking undue advantage exists, as described in MMIP 2.1.4, the ~~Market Surveillance Unit~~ Department of Market Analysis shall, ~~in cooperation with the PX Compliance Unit where appropriate,~~ review the "gaming" behavior and/or the relationship between system conditions and market behavior and pricing in order to assess the potential for and impact of such gaming behavior, with a view to taking appropriate action, if necessary, either with respect to structural changes such as ~~Zone changes,~~ or to changes to the ISO or ~~PX Tariffs, Protocols or Activity Rules of Conduct,~~ or to proscribe specific behavior by Market Participants, as provided for in the Enforcement Protocol. In carrying out such activities the ~~Market Surveillance Unit~~ Department of Market Analysis shall in appropriate circumstances seek the advice of the ISO ~~MSC~~ on the merits of such actions. ~~In appropriate circumstances, the Market Surveillance Unit may institute or arrange for ADR procedures involving Market Participants with conflicting perspectives, e.g. as to whether a particular practice is better characterized as improper gaming or legitimate aggressive competition or as to whether rule changes may resolve conflicts.~~

MMIP 2.3.4 Adverse Effects of Transition Mechanisms

Should the monitoring and analysis conducted under MMIP 2.2.3 reveal significant adverse effects of transition mechanisms on competition in or the efficient operation of the ISO Markets, the ~~Market Surveillance Unit~~ Department of Market Analysis shall examine and fully assess the

efficacy of all possible measures that may be taken by the ISO and, in consultation with the Compliance Unit of the PX, all possible measures that may be taken by the PX, in order to prevent or to mitigate such adverse effects. The Market Surveillance Unit/Department of Market Analysis shall make such recommendations to the CEO of the ISO and to the ISO Governing Board/MSG as it considers appropriate, for action in this regard by the PX or the ISO and/or for referral to the regulatory or law enforcement agencies. Such proposed measures may include, but shall not be limited to the following:

- MMIP 2.3.4.1** the use of direct bid caps as a mechanism to prevent or mitigate artificially high Market Clearing Prices caused by abuses of market power;
- MMIP 2.3.4.2** the use of contracts for differences for eliminating the incentive for Generators to bid ISO prices to artificially high levels enabled by the presence of market power;
- MMIP 2.3.4.3** calling upon Reliability Must-Run Units to operate; and to modify Reliability Must-Run Contracts;
- MMIP 2.3.4.4** bid floors to prevent or mitigate the possible exercise of below-cost bidding or predatory pricing that may arise from the incentives provided by the combined effect of the CTC and the rate freeze when the IOUs are not buyers of Energy.

The CEO and the ISO/MSG shall consult on such recommendations and each may, after due consideration, propose any of such measures to the ISO Governing Board. In the event that the ISO Governing Board adopts, and where necessary obtains regulatory approval for, any measure proposed pursuant to MMIP 2.3.4, the Market Surveillance Unit/Department of Market Analysis shall develop an implementation plan for such measure, and shall submit such plan to the CEO and ISO/MSG. Upon approval of such plan by the CEO, the Market Surveillance Unit shall monitor the implementation and effect of such measure on the state of the ISO Markets and shall periodically report on them to the CEO and the ISO Governing Board/MSG.

MMIP 3 **ISO MARKET SURVEILLANCE UNIT/DEPARTMENT OF MARKET ANALYSIS**

MMIP 3.1 **Establishment**

There shall be established on or before ISO Operations Date within the ISO a Market Surveillance Unit/Department of Market Analysis that shall be responsible for the ongoing development, implementation, and execution of the ISO Market monitoring and information scheme described in this MMIP and the adherence to its objectives, as set forth in MMIP 1.1.

MMIP 3.2 **Composition**

The Market Surveillance Unit/Department of Market Analysis shall be adequately staffed by the ISO with full-time ISO staff with the experience and qualifications necessary to fulfill the functions referred to in this MMIP. Such qualifications may include professional training

pertinent to and experience in the operation of markets analogous to ISO Markets, in the electric power industry, and in the field of competition and antitrust law, economics and policy. The ~~Market Surveillance Unit~~ Department of Market Analysis shall be directed by a ~~Compliance Director who shall be under the general management of the ISO Chief Legal Counsel and the ISO CEO, provided that the CEO may designate another ISO officer (currently the General Counsel) for day-to-day oversight of the Department.~~

MMIP 3.3 Accountability and Responsibilities

MMIP 3.3.1 ~~Market Surveillance Unit~~ Department of Market Analysis

The ~~Market Surveillance Unit~~ Department of Market Analysis shall report to and be accountable to the ISO CEO ~~and his or her designee through the Chief Legal Counsel~~ on all matters pertaining to policy and other matters that may affect the effectiveness and integrity of the monitoring function referred to in this Protocol, including matters pertaining to market monitoring, information development and dissemination and pertaining to generic or entity-specific investigations, corrective actions or enforcement.

MMIP 3.3.2 CEO and ISO-MSO

The ISO CEO and the ~~ISO-MSO~~ shall each have the independent authority to refer any of the matters referred to in MMIP 3.3.1 to the ISO Governing Board for approval of recommended actions.

MMIP 3.3.3 Chief Executive Officer (CEO)

MMIP 3.3.3.1 The ~~Market Surveillance Unit~~ Department of Market Analysis shall report to and be accountable to the ISO CEO ~~and his or her designee through the Chief Legal Counsel~~ on all matters relating to the day-to-day administration of the ~~Market Surveillance Unit~~ Department and the internal resources and organization of the ISO in accordance with MMIP 3.3.3.2.

MMIP 3.3.3.2 The ISO, ~~through its CEO and Governing Board,~~ shall ~~determine~~ ensure that the ~~Market Surveillance Unit~~ Department of Market Analysis has adequate resources and full access to data and the full cooperation of all parts of the ISO organization in developing the database necessary for the effective functioning of the ~~Market Surveillance Unit~~ Department of Market Analysis and the fulfillment of its monitoring function. ~~The ISO CEO shall institute within the ISO such data collection, organization and analytic activities as may be necessary for the Market Surveillance Unit to fulfill its functions and responsibilities.~~

MMIP 3.3.4 Regulatory and Antitrust Enforcement Agencies

Where considered necessary and appropriate, or where so ordered by the regulatory or antitrust agency with jurisdiction over the matter in question, or by a court of competent jurisdiction, the ~~ISO Market Surveillance Unit~~ shall refer a matter ~~through the ISO CEO~~ to the regulatory or antitrust enforcement agency concerned, e.g., in cases of serious abuse requiring expeditious investigation or action by the agency. In all such cases of direct referral, the ISO CEO shall promptly

inform the ISO Governing Board and the ISO-MSB of the fact of and the content of the referral.

MMIP 3.3.5 Complaints

Any Market Participant, or any other interested entity, may at any time submit information to or make a complaint to the ~~Market Surveillance Unit~~ Department of Market Analysis concerning any matter that it believes may be relevant to the ~~Market Surveillance Unit's~~ Department of Market Analysis's monitoring responsibilities. Such submissions or complaints may be made on a confidential basis in which case the ~~Market Surveillance Unit~~ Department of Market Analysis shall preserve the confidentiality thereof. The ~~Market Surveillance Unit~~ Department of Market Analysis, at its discretion, may request further information from such entity and carry out any investigation that it considers appropriate as to the concern raised. The ~~Market Surveillance Unit~~ Department of Market Analysis shall periodically make reports to the ISO CEO and ISO Governing Board on complaints received.

MMIP 4 SPECIFIC FUNCTIONS OF ISO MARKET SURVEILLANCE UNIT
DEPARTMENT OF MARKET ANALYSIS

MMIP 4.1 Information Gathering and Market Monitoring Indices for Evaluation

MMIP 4.1.1 Information System

The ~~Market Surveillance Unit~~ Department of Market Analysis shall be responsible for developing an information system and criteria for evaluation that will permit it to effectively monitor the ISO Markets to identify and investigate abuses of that market, whether caused by exercises of market power or by other actions or inactions.

MMIP 4.1.2 Data Categories

To develop the information system set forth in MMIP 4.1.1, the ~~Market Surveillance Unit~~ Department of Market Analysis shall initially develop, and shall refine on the basis of experience, a detailed catalog of all the categories of data it will have the means of acquiring, and the procedures it will use (including procedures for protecting confidential data) to handle such data.

MMIP 4.1.3 Catalog of Market Monitoring Indices

The ~~Market Surveillance Unit~~ Department of Market Analysis shall initially develop, and shall refine on the basis of experience, a catalog of the ISO Market monitoring indices that it will use to evaluate the data so collected.

MMIP 4.2 Evaluation of Information

MMIP 4.2.1 Ongoing Evaluation

The ~~Market Surveillance Unit~~ Department of Market Analysis shall evaluate and reevaluate on an ongoing basis the data categories and market monitoring indices that it has developed under MMIP 4.1.2 and 4.1.3, and the information it collects and receives from various other

sources, including and in particular the ISO's operation of the ISO Markets. Such ongoing evaluations shall provide the basis for its reporting and publication responsibilities as set forth in this Protocol, for recommendations on proposed changes to the ISO Tariff and ISO Protocols and other potential rules affecting the ISO Markets, and for the development of criteria or standards for the initiation of proposed corrective or enforcement actions. In evaluating such information, the ~~Market Surveillance Unit~~Department of Market Analysis may consult the ISO-MSC or such external bodies as may be appropriate.

MMIP 4.2.2 Submission of Evaluation Results

The final results of the ~~Market Surveillance Unit's~~Department of Market Analysis's ongoing evaluations under MMIP 4.2.1 shall routinely and promptly be submitted ~~simultaneously to the ISO CEO and to the ISO MSC~~ for comment.

MMIP 4.3 Review of Activity Rules of Conduct

~~When an iterative bidding process is developed that requires the application of Activity Rules, whether developed by the ISO or the PX,~~ The Market Surveillance Unit~~Department of Market Analysis~~ shall review such Activity Rules of Conduct for their effectiveness and consistency with its market monitoring activities and standards. The ~~Market Surveillance Unit~~Department of Market Analysis may at that time, and from time to time thereafter based on its experience in monitoring the ISO Markets, propose to the ISO CEO and/or the ISO Governing Board that changes be made in such Activity Rules of Conduct.

MMIP 4.4 Reports and Recommendations

MMIP 4.4.1 ISO CEO and Governing Board

On the basis of the evaluation conducted under MMIP 4.2 or the review conducted under MMIP 4.3, the ~~Market Surveillance Unit~~Department of Market Analysis shall prepare periodic reports, as required by the ISO CEO, and specific ad hoc reports as appropriate, for the ISO CEO and ISO Governing Board on the state of competition in or the efficiency of the ISO Markets; and on its monitoring activities, the results of its evaluation and review activities, and its development and implementation of recommendations. Where appropriate, the ISO ~~Market Surveillance Unit~~Department of Market Analysis may recommend to the ISO CEO and/or the ISO Governing Board actions to be taken, including the amendment of the ISO Tariff and ISO Protocols and corrective or enforcement action against specific entities. Such reports shall be made not less frequently than quarterly in the case of the ISO CEO and ISO-MSC and annually in

the case of the ISO Governing Board and shall contain such information and be in such form as specified by such entities. Such reports shall be made public and publicized as specified by such entities except to the extent that they contain confidential or commercially sensitive information or to the extent such entities determine that effective enforcement of the monitoring function dictates otherwise.

MMIP 4.4.2 Regulatory Agencies

As required in the ISO Tariff or by the ISO CEO and ISO Governing Board, or as required by the regulatory agency with jurisdiction over the matters in question, the ~~Market Surveillance Unit~~ Department of Market Analysis shall prepare reports to the FERC and other regulatory agencies, which shall be reviewed and approved by the ISO CEO or his or her designee and Governing Board and then submitted as required. When publicly available reports are made to one regulatory agency with competent jurisdiction, such as the FERC, the ~~Market Surveillance Unit~~ Department of Market Analysis may simultaneously make such reports available to other regulatory agencies with legitimate interests in their contents, such as the Electricity Oversight Board, the California Public Utilities Commission, the California Energy Commission and/or the California Attorney General CPUC and CEC.

MMIP 4.4.3 ISO Market Surveillance Committee

All reports and recommendations to be made to the ~~ISO CEO and ISO Governing Board~~ under MMIP 4.4.1, or to regulatory agencies under MMIP 4.4.2, unless urgency requires otherwise, shall first be submitted to the ISO MSC for comments, which comments shall be reflected in any the submittal to the ISO Governing Board seeking approval of any such reports or recommendations. In addition, the ~~Market Surveillance Unit~~ may submit specific reports to the ISO MSC itself, as it considers appropriate. All final reports made to external regulatory agencies shall be simultaneously submitted to the ISO MSC.

MMIP 4.5 ISOMarket Participants

MMIP 4.5.1 Collection of Data

The ~~Market Surveillance Unit~~ Department of Market Analysis may request ~~that the submission~~ Market Participants or other entities whose activities may affect the operation of the ISO markets submit any information or data determined by the ~~Market Surveillance Unit~~ Department of Market Analysis to be potentially relevant by ~~ISO Participants, the PX or other entities whose activities may affect the operation of the ISO market.~~ This data will be subject to due safeguards to protect confidential and commercially sensitive data. Failures by ~~ISO Market Participants~~ to provide such data shall be treated under the Enforcement Protocol MMIP 4.5.2. In the event of failures by other entities to provide such data, the ISO may take whatever action is available to it and appropriate for it to take, including reporting ~~Market Surveillance Unit may report the failure to the ISO CEO and Governing Board or the pertinent regulatory agency, as appropriate, after providing~~

such entity the opportunity to respond in writing as to the reason for the alleged failure.

MMIP 4.5.2 Provision of Data by ISO Participants

~~Failure by an ISO Participant to provide information requested pursuant to MMIP 4.5.1, or otherwise to cooperate in the Market Surveillance Unit's data collection or investigation activities, may be treated as grounds for action against the ISO Participant entity concerned. Such action may lead to the imposition of such penalties or sanctions as are permitted under the ISO Tariff or related protocols approved by FERC and may include possible exclusion from the ISO Markets or termination of any relevant ISO agreements or certifications. Before any such action is taken, the ISO Participant shall be provided the opportunity to respond in writing as to the reason for the alleged failure.~~

MMIP 4.5.23 Dissemination of Data

~~ISO Participants~~Any Market Participant may request that the ISO provide data that the ISO~~it~~ has collected concerning that Market Participant; and, upon approval of the ISO CEO and at his sole discretion, such data may, subject to constraints on the ISO's resources and at the ISO's sole discretion, be provided by the ISO subject to due safeguards to protect confidential and commercially sensitive data. Where such activity imposes a significant burden or expense on the ISO, the data may be provided on the condition that a reasonable contribution to the cost incurred by the ISO is made to the ISO by the requesting party.

MMIP 4.6 External Consulting Assistance and Expert Advice

In carrying out any of its responsibilities under this MMIP 4, including the development of an information system, market monitoring indices and evaluation criteria, and the catalogs associated therewith, and in its analysis and ongoing evaluation of these catalogs and of the Activity Rules of Conduct under MMIP 4.3, the ~~Market Surveillance Unit~~Department of Market Analysis may hire consulting assistance subject to the budgetary approval of the ISO CEO and may seek such expert external advice as it believes necessary.

MMIP 4.7 Cooperation with PX Compliance Unit and Market Monitoring Committee

~~In carrying out its responsibilities under this Protocol, the Market Surveillance Unit may at its discretion consult or cooperate in the manner it considers most appropriate with the PX's Compliance Unit and Market Monitoring Committee, or other entities within the PX that fulfill the analogous market monitoring functions, with respect to the following:~~

- ~~(a) exchange of data subject to any limitations on the ISO's ability to disclose commercially sensitive information from other Scheduling Coordinators to the ISO, monitoring methodologies and results, and information on corrective, referral or enforcement actions taken;~~

- ~~(b) — monitoring of market performance;~~
- ~~(c) — joint analysis of data, subject to any limitations on the ISO's ability to disclose commercially sensitive information from other Scheduling Coordinators to the ISO, and monitoring results of markets and Market Participant behavior;~~
- ~~(d) — investigations of specific market abuses; and~~
- ~~(e) — proposals for concerted action on enforcement measures, e.g., as to suspensions from trading.~~

MMIP 4.87 Liability for Damages

~~As provided in Section 14.1 and 14.2 of the ISO Tariff, the Market Surveillance Unit Department of Market Analysis, the ISO-MSC, the ISO CEO and other ISO staff, and the ISO Governing Board shall not be liable to any Market Participant under any circumstances whatsoever for any matter described in those sections, including but not limited to any financial loss or loss of economic advantage resulting from the performance or non-performance by such ISO entities of their functions under this Protocol.~~

MMIP 5 ISO MARKET SURVEILLANCE COMMITTEE

MMIP 5.1 Establishment

~~There shall be established on or before ISO Operations Date an ISO Market Surveillance Committee (ISO-MSC), whose role it shall be to provide independent external expertise on the ISO market monitoring process as described in this Protocol and, in particular, to provide independent expert advice and recommendations to the ISO CEO and Governing Board. Members of the Committee shall not be, and shall not be understood to be, are not employees or agents of the ISO. Members are not available to provide expert witness services to the ISO or any other party in a FERC proceeding relating to the ISO, except to the extent that the ISO-MSC makes an advance determination that providing such service is not inconsistent with the independence of the ISO-MSC.~~

MMIP 5.2 Composition

MMIP 5.2.1 Qualifications

The ISO-MSC shall comprise a body of three or more independent and recognized experts whose combined professional expertise and experience shall encompass the following:

- MMIP 5.2.1.1** economics, with emphasis on antitrust, competition, and market power issues in the electricity industry;
- MMIP 5.2.1.2** experience in operational aspects of generation and transmission in electricity markets;
- MMIP 5.2.1.3** experience in antitrust or competition law in regulated industries; and
- MMIP 5.2.1.4** financial expertise relevant to energy or other commodity trading.

MMIP 5.2.2 Criteria for Independence

Each member of the ISO-MSC must meet the following criteria for independence in order to be appointed:

MMIP 5.2.2.1 no material affiliation, through employment, consulting or otherwise, with any Market Participant or affiliate thereof consistent with the pertinent FERC Standards of Conduct; and

MMIP 5.2.2.2 no material financial interest in any Market Participant or affiliate thereof consistent with the pertinent FERC Standards of Conduct.

MMIP 5.2.2.3 during their time on the Committee, members may not provide paid expert witness testimony or other commercial services to the ISO or to any other party in connection with any legal or regulatory proceeding relating to the ISO or any trade or other transaction involving the ISO markets (except that the Committee may consult with and make recommendations concerning the functioning of the markets to ISO Management or the ISO Governing Board in connection with legal or regulatory proceedings).

MMIP 5.3 Appointments to the ISO-MSC

For each position on the ISO-MSC, the ISO CEO shall conduct a thorough search and requisite due diligence to develop a nomination to the ISO Governing Board, which nomination shall be consistent with meeting the combined professional expertise and experience of the ISO MSC set forth in MMIP 5.2.1 and with the criteria for independence set forth in MMIP 5.2.2. The ISO Governing Board shall expeditiously consider such nominations. If the nomination is approved, the ISO CEO shall appoint the candidate so nominated to the ISO-MSC. If the nomination is rejected, the ISO CEO shall expeditiously proceed to develop another nomination in accordance with this MMIP.

MMIP 5.4 Compensation and Reimbursements

Members of the ISO-MSC shall be compensated on such basis as the ISO Governing Board shall from time to time determine.

Members of the ISO-MSC shall receive prompt reimbursement for all expenses reasonably incurred in the execution of their responsibilities under this MMIP 5.

MMIP 5.5 Liability for Damages

As provided in Section 14.1 and 14.2 of the ISO Tariff, the Market Surveillance Unit, Department of Market Analysis, the ISO-MSC, the ISO CEO and other ISO staff, and the ISO Governing Board shall not be liable to any Market Participant under any circumstances whatsoever for any matter described in those sections, including but not limited to any financial loss or loss of economic advantage resulting from the performance or non-performance by such ISO entities of their functions under this Protocol.

MMIP 6 SPECIFIC FUNCTIONS OF ISO-MARKET SURVEILLANCE COMMITTEE (ISO-MSC)

MMIP 6.1 Information Gathering and Evaluation Criteria

The ISO-MSC shall review the initial catalogs of information and data and of evaluation criteria developed by the ~~Market Surveillance Unit~~Department of Market Analysis pursuant to MMIP 4 and shall propose such changes, additions or deletions to such catalogs or items therein as it sees fit. In so doing, the ISO-MSC shall have full discretion to specify database items or evaluation criteria for inclusion in the pertinent catalog.

MMIP 6.2 Evaluation of Information

The ISO-MSC may, upon request of the ~~Market Surveillance Unit~~Department of Market Analysis, the ISO ManagementCEO or the ISO Governing Board, or on its own volition, evaluate such information or data, including as may be collected by the ~~Market Surveillance Unit~~Department of Market Analysis on the basis of the evaluation criteria developed by the ~~Market Surveillance Unit~~Department of Market Analysis or on such further articulated evaluation criteria developed by the ISO-MSC. ~~In carrying out such evaluations, the ISO-MSC may consult the PX's Compliance Unit and Market Monitoring Committee with respect to any matter relating to such evaluations.~~

MMIP 6.3 Reports and Recommendations

MMIP 6.3.1 Required Reports

All evaluations carried out by the ISO-MSC pursuant to MMIP 6.2, and any recommendations emanating from such evaluations, shall be embodied by the ISO-MSC in written reports to the ISO CEO and ISO Governing Board and shall be made publicly available subject to due restrictions on dissemination of confidential or commercially sensitive information. The ISO-MSC may submit any MSC report to FERC, subject to due restrictions on dissemination of confidential or commercially sensitive information.

MMIP 6.3.2 Additional Reports

The ISO-MSC may make such additional reports and recommendations as it sees fit relating to the monitoring program referred to in this Protocol, the analysis of information, the evaluation criteria or any corrective or enforcement actions proposed by the ~~Market Surveillance Unit~~Department of Market Analysis or proposed of its own volition.

MMIP 6.4 Publication of Reports and Recommendations

Upon request of the ISO-MSC, the ISO-CEO shall publish reports and recommendations of the ISO-MSC or incorporate them, if consistent, into the ISO's own reports or recommendations.

MMIP 7 IMPLEMENTATION OF RECOMMENDATIONS

MMIP 7.1 Plan and Activity-Rules of Conduct Changes

~~Following a~~Upon recommendation of the ISO-CEO, ~~acting on the advice of the Market Surveillance Unit, or based on the independent recommendation of the ISO-MSC,~~ the ISO Governing Board may make

such changes as it believes are appropriate to any ISO Protocol or Agreement or to any Activity Rules of Conduct applicable in accordance with MMIP 9.

MMIP 7.2 Tariff Changes

Upon recommendation of the ISO CEO, acting on the advice of the Market Surveillance Unit, or based on the independent recommendation of the ISO MSC, the ISO Governing Board shall consider and may adopt proposed ISO Tariff changes in accordance with MMIP 9.

MMIP 7.3 Sanctions and Penalties

Upon recommendation of the ISO CEO, acting on the advice of the Market Surveillance Unit, or based on the independent recommendation of the ISO MSC, and after an audit by the Market Surveillance Unit the ISO Governing Board may impose such sanctions or penalties as it believes necessary and as are permitted under the ISO Tariff and related protocols approved by FERC; or it may make any such referral to such regulatory or antitrust agency as it sees fit to recommend the imposition of sanctions and penalties. The audit by the Market Surveillance Unit shall investigate whether the abuse or behavior identified meets the criteria for and has such effect as to warrant the sanctions or penalties recommended.

MMIP 8 PUBLICATION OF INFORMATION

MMIP 8.1 Market Monitoring Data and Indices

The ISO Market Surveillance Unit/Department of Market Analysis shall, pursuant to MMIP 4.1, develop a catalog of data and indices. Upon approval of the ISO CEO, such catalogs shall be duly published on the ISO Home Page and disseminated to all ISO Market Participants.

MMIP 8.2 Regular Information Publication

The following information shall be published by the ISO Market Surveillance Unit, in a medium and form helpful to Market Participants, on a regular basis:

MMIP 8.2.1.1 Market Clearing Prices for Energy;

MMIP 8.2.1.2 Market Clearing Prices for Ancillary Services;

MMIP 8.2.1.3 Aggregate Supply and Demand for each Zone;

MMIP 8.2.1.4 Congestion and Congestion costs;

MMIP 8.2.1.5 Generation Unit and transmission line outages; and

MMIP 8.2.1.6 Hydro-electric Generation

MMIP 8.3 Reports to Regulators

The ISO Market Surveillance Unit shall develop a schedule, format and proposed table of contents for the annual reports of market performance for delivery to FERC, and such other reports as may be required by FERC, which shall be submitted for review as a proposal to

the ISO CEO and ISO-MSU. Upon approval of such proposal, the Market Surveillance Unit Department of Market Analysis shall proceed to prepare and submit such reports according to such schedule for approval and submission by the ISO CEO, to the ISO Governing Board and to the regulatory agency concerned.

MMIP 9

AMENDMENTS

If the ISO determines a need for an amendment to this Protocol, the ISO will follow the requirements as set forth in Section 16 of the ISO Tariff.

APPENDIX A

ISO Market Monitoring Plan

Market Mitigation Measures

* * *

4.3 Sanctions for Physical Withholding

The ISO may report a Market Participant the ISO ~~determines~~believes to have engaged in physical withholding, including providing the ISO false information regarding the derating or outage of an Electric Facility, to the Federal Energy Regulatory Commission in accordance with Section 2.3.3.9.5 of the ISO Tariff. In addition, a Market Participant that fails to operate a Generating Unit in conformance with ISO dispatch instructions shall be subject to the penalties set forth in Section 11.2.4.1.2 of the ISO Tariff.

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ATTACHMENT E

ATTACHMENT E

Background and Stakeholder Process Timeline

<u>Date</u>	<u>Activity</u>
June 14, 2002	Initiated O & I Review by market notice
June 21	Published discussion paper with preliminary market rules
June 26	Conference call to discuss Market Participant questions regarding the O & I Review
June 27	Discussed plan for O & I Review at Market Issues Forum
July 12	Modified schedule in response to stakeholder comments to delay tariff changes until September
July 16	ISO staff participated in WPTF conference on code of conduct
July 19	Published paper on use of existing authority
July 25	Discussed use of existing authority at Market Issues Forum
Aug. 1	Presented status of O & I Review at public meeting of Board of Governors
Aug. 20	Presented plan for information release and committed period penalty at public meeting of Market Surveillance Committee (MSC)
Aug. 28	Presented conceptual plan for market rules and penalties at Market Issues Forum
Aug. 29	Conference call to further discuss the ISO's conceptual proposal
Sept. 9	Published paper on ISO's conceptual proposal
Sept. 13	Conference call with Market Participants to discuss ISO's conceptual proposal
Sept. 19	ISO Board of Governors meeting; public comment and discussion of proposal
Oct. 24	ISO Board approves three O & I-related Tariff changes (intended to be Amendment No. 47)
Nov. 5	Published draft Revised Proposal for stakeholder review
Nov. 8	Conference call with stakeholders
Nov. 12	Market Issues Forum
Nov. 15	Published Board memorandum with Revised Proposal
Nov. 21	Obtained Board direction on proposal
Jan. 3, 2003	Published draft Tariff language for stakeholder review
Jan. 8	Conference call with stakeholders
Jan. 9	Published additional draft Tariff language (intended to be Amendment No. 47)
Jan. 10	Comments due on first set of Tariff language
Jan. 15	Market Issues Forum
Jan. 17	Published Board memorandum with draft Tariff language
Jan. 17	Comments due on second set of Tariff language (intended to be Amendment No. 47)

Jan. 23

Present proposal to ISO Board of Governors for approval

May 8

Presented Market Issues Forum update to Market Participants on status of O & I filing and Information Release Program

ATTACHMENT F

