

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Dynergy Power Marketing, Inc.,)	Docket No. EL01-23-000
El Segundo Power, LLC,)	
Long Beach Generation LLC,)	
Cabrillo Power I LLC,)	
Cabrillo Power II LLC)	
)	
v.)	
)	
California Independent System)	
Operator Corporation)	

**ANSWER OF THE CALIFORNIA INDEPENDENT
SYSTEM OPERATOR CORPORATION
TO COMPLAINT REQUESTING FAST-TRACK PROCESSING
FILED BY
DYNEGY POWER MARKETING, INC., EL SEGUNDO POWER, LLC,
LONG BEACH GENERATION LLC, CABRILLO POWER I LLC,
AND CABRILLO POWER II LLC**

I. INTRODUCTION AND SUMMARY

Pursuant to Rule 213 of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission ("Commission"), 18 C.F.R. §§ 385.213 (2000), the California Independent System Operator Corporation ("ISO")¹ hereby submits its Answer to the Complaint Requesting Fast-Track Processing ("Complaint") filed by Dynergy Power Marketing, Inc., El Segundo Power, LLC, Long Beach Generation LLC, Cabrillo Power I LLC, and Cabrillo Power II LLC (collectively, "Dynergy") on December 22, 2000. For the reasons described below, the Complaint should be denied.

II. ANSWER

A. The ISO Has Consistently Exercised Its OOM Authority In Accordance With the Requirements of the ISO Tariff

The essence of Dynegy's Complaint is that the ISO has abused its authority to call Generating Units "out-of-market" (OOM) in order to avoid a threatened or imminent System Emergency and to pay the unit owners according to the two payment options described in Section 11.2.4.2 of the ISO Tariff. The ISO's OOM authority is well established.² The Commission has also approved the two payment options: each Scheduling Coordinator elects once a year to receive, for the next year, either (1) payment based on the Uninstructed Imbalance Energy Charge price as calculated using the Hourly Ex Post Price, or (2) payment based on a calculated price comprised of a capacity payment, an Energy payment, verifiable fuel-related start-up costs, and verifiable gas imbalance charges.³

Dynegy makes four allegations regarding the ISO's supposed abuse of its OOM authority. None has merit.

1. The ISO Has Not Violated Section 2.3.5.1.5 of the ISO Tariff.

Dynegy's first allegation is that the ISO is violating the Commission's directive that the ISO pursue a more forward approach to purchasing resources necessary to operate the Grid.⁴ Dynegy points to Section 2.3.5.1.5 of the ISO

¹ Capitalized terms not otherwise defined herein are defined in the Master Definitions Supplement, Appendix A to the ISO Tariff.

² See *California Independent System Operator Corporation*, 90 FERC ¶ 61,006, at 61,010-11 (2000).

³ See *id.* at 61,014-15.

⁴ See *San Diego Gas and Electric Company et al.*, 92 FERC ¶ 61,172, at 61,607-08 (2000) ("August 23 Order")

Tariff, which provides that the ISO shall take such action as it deems necessary, consistent with Good Utility Practice, to ensure compliance with Applicable Reliability Criteria, including the negotiation of contracts through processes other than competitive solicitations. According to Dynegy, by refusing to negotiate prices with generators for OOM calls, the ISO fails to use this authority but instead “employ[s] OOM provisions before exhausting competitive offers to remedy potentially thin markets”⁵ Neither the Commission nor the ISO Tariff, however, requires the ISO to engage in negotiation when making OOM calls.

Dynegy’s argument is based on a fundamental misunderstanding of the ISO’s OOM authority. That authority arises from Sections 2.3.2.2 and 5.6.1 of the ISO Tariff. Section 2.3.5.1.5 serves a different, but related, purpose. As stated in Section 2.3.5.1, Section 2.3.5.1.5 describes the steps that the ISO must take to ensure that Generation reserve criteria are met. It provides the opportunity for the ISO, when taking action sufficiently in advance of a threatened System Emergency, to turn to the super peak PX and APX markets. It does not, however, obligate the ISO to do so. As the ISO noted in its transmittal letter accompanying Amendment No. 30, which the ISO filed to clarify its authority to engage in forward contracts pursuant to Section 2.3.5.1.5:

[C]onsistent with the Commission's directive in *San Diego*, the ISO has begun to examine the opportunities that may be available to it to forward contract. The ISO Tariff amendments submitted with this filing are necessary to permit the ISO to go forward. The ISO does not, however, read that directive as a *requirement* that it forward contract if, in its judgment, appropriate prices and contractual terms are unavailable or if the load serving entities receive and exercise

⁵ See Complaint at 2-3, 6.

the authority to discharge a responsibility that more properly is theirs.⁶

In filing Amendment No. 30, the ISO indicated that it was seeking the tools necessary to enable it to contract if available forward commitments appear reasonable. In approving Amendment No. 30, the Commission expressed no disagreement.⁷

2. The ISO Has Complied With the Commission Order On Amendment No. 23.

Dynegy's second assertion is that the ISO has ignored outstanding offers. Dynegy points to the order on Amendment No. 23, in which the Commission directed that the ISO, prior to calling upon a unit out-of-market, must accept all bids capable of resolving the problem.⁸ Dynegy asserts that, in a period prior to the Commission's December 15 Order regarding California markets, Dynegy submitted via facsimile bids above the ISO's real-time Energy price cap, which the ISO rejected without making a counter-offer. Dynegy claims that its submittal of bids via facsimile was necessary because, if it bid into the ISO's real-time market for the hours involved, its bids would be subject to the ISO's real-time price cap.⁹

First, the Commission recognized in approving the alternative payment option for OOM calls in the ISO Tariff, that there would be occasions on which the payment option would result in payments higher than necessary and that

⁶ Transmittal Letter for Amendment No. 30, Docket Nos. EL00-95-002 and EL00-98-002 (Sept. 11, 2000), at 2.

⁷ See *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Services Into Markets Operated By the California Independent System Operator and the California Power Exchange et al.*, 93 FERC ¶ 61,294, at 61,990, 62,020 (2000) ("December 15 Order").

⁸ See *California Independent System Operator Corporation*, 90 FERC at 61,011.

⁹ See Complaint at 7-8.

there would be other occasions on which the payment option would fail to consider all of a Generator's costs.¹⁰ Second, as described in more detail below, the Commission's acceptance of a "soft-cap" approach in Amendment No. 33 on December 8, 2000, and in its December 15 Order, allows a Generator to recover its costs through the ability to be paid its bid price (i.e., "as bid").

Bids available to the ISO for real-time Imbalance Energy are in the Imbalance Energy market and the Energy bids for units accepted in the ISO's Ancillary Services market. The ISO understands the circumstances to which Dynegy refers to be instances where the ISO calls upon the unit to be running in advance in order to have the unit available to address a threatened System Emergency. Under such circumstances, Dynegy appears to believe the ISO should accept bids outside of the Imbalance Energy market for the hours involved and the Ancillary Services market. Because the ISO does not have a market for an advance commitment of a unit, however, there can be no "bids" that the ISO can accept for the hours outside of its normal markets, even if a Generator submits an "offer" via facsimile. Instead, a Generator notified in advance of the ISO's need for its Energy may, at any time after the Day-Ahead Market closes, submit Supplemental Energy bids covering the intervening hours and may, pursuant to the December 15 Order, be paid as bid when dispatched for those hours.

Dynegy also suggests that Section 2.3.5.1.5 requires the ISO, when it receives an offer such as one of Dynegy's facsimiles, to negotiate. As discussed above, Section 2.3.5.1.5 makes no such requirement. Moreover, requiring the

¹⁰ *California Independent System Operator Corporation*, 90 FERC at 61,015.

ISO to negotiate prices when faced with a possible System Emergency would provide Generators with enormous leverage. It is precisely because it should not be negotiating with Generators at such times that the ISO proposed the penalties included in Amendment No. 33 to the ISO Tariff, which the Commission has approved.¹¹ Additionally, requiring ISO operators to engage in Generator-by-Generator negotiations at the same time their full attention should be focused on averting a System Emergency is counter-productive.

Moreover, Dynegy has no need to negotiate because, as described above, its concerns for recovering its costs are mooted by the December 15 Order, in which the Commission authorized bids above a \$150 “soft cap,” if such bids reflect a Generator’s costs.¹² Dynegy can submit Supplemental Energy bids that reflect its costs, including start-up costs, for each hour for which the ISO has instructed it to run. For the Energy instructed by the ISO, Dynegy will be paid according to those bids. The December 15 Order, therefore, ensures Dynegy a compensatory rate, even when the Market Clearing Price is lower.

3. The ISO Has Not Discriminated Against In-State Generators.

Dynegy’s third claim is that the ISO is unjustifiably discriminating against in-state Generators “by forcing those generators to supply deliveries in situations not contemplated by the ISO Tariff, while providing similarly situated off-system

¹¹ See *California Independent System Operator Corporation*, 93 FERC ¶ 61,239 (2000). The ISO specifically noted in filing Amendment No. 33 to the ISO Tariff, which included penalties for nondelivery of Energy in response to OOM orders, that the need for the amendment arose because Generators were refusing to deliver Energy unless the ISO negotiated prices. See Transmittal Letter for Amendment No. 33, Docket No. ER01-607-000 (Dec. 8, 2000), at 2-3, 5-6.

¹² See December 15 Order, 93 FERC at 62,010.

generators higher prices and more favorable terms.”¹³ This claim is premised on the assertion that the ISO is acting outside its Tariff, which, as explained above, the ISO is not. Moreover, even if an out-of-state Generator might be able to negotiate a price above its costs when its Energy is required to resolve a System Emergency, there would be no undue discrimination. Quite simply, Dynegy and other in-state Generators are within the ISO’s Control Area. The ISO ensures reliable service and, through the Participating Generator Agreement, the Generator agrees to certain conditions – including being subject to dispatch – in return. Out-of-state Generators are in another control area. They have similar responsibilities in their own control areas. Under such circumstances, it would be unjust to subject out-of-state Generators to dispatch by the ISO.¹⁴

4. The ISO Has Complied with the Terms of the Reliability Must-Run Service Agreements.

Dynegy’s final argument is that the ISO has used its OOM authority to call upon Cabrillo Power I LLC, even though those units are under a Reliability Must-Run (“RMR”) Contract, i.e., the Must-Run Service Agreement (“MSRA”).¹⁵ The ISO has issued OOM calls to these units, but has only done so for system-wide reliability concerns, i.e., for Imbalance Energy. While the ISO can call upon any unit, including an RMR Unit, for Imbalance Energy under the authority of Section 5.6.1 of the ISO Tariff, it cannot call a Unit for that purpose under the authority of

¹³ See Complaint at 8.

¹⁴ Cf. *San Diego Gas & Electric Company*, 93 FERC ¶ 61,333, at 62,132-33 (2000) (denying request that “wheel-out” or “wheel-through” customers be made subject to Reliability Must-Run charges applicable to the San Diego Gas & Electric Company control area, based on the rationale that “[w]heel-out’ and ‘wheel-through’ transactions ultimately serve loads in other areas and potentially would be subject to any RMR costs incurred for the operation of the local system associated with the load such transactions serve.”).

¹⁵ See Complaint at 8-9.

the MSRA. Both at the insistence of the RMR owners, who feared the ISO would call on RMR Units to furnish service other than that needed to ensure local reliability, and the Participating Transmission Owners, who, because they pay the costs incurred under the MSRA, objected to bearing solely a cost for service (i.e., Imbalance Energy) that provided a control-area-wide benefit, Section 4.1b of the MSRA specifically prohibits the ISO from calling upon RMR Units for Imbalance Energy. Therefore, the ISO could not permissibly substitute RMR calls for the OOM calls in question.

Perhaps in recognition of this fact, Dynegy argues that OOM calls must have been used address locational reliability problems, which is the purpose of the MSRAs, because the ISO has directed multiple units to run at minimum operating levels rather than a single unit at higher levels. In recent months, however, in order to avoid a threatened System Emergency attributable to an insufficiency of Generation to meet Demand, it has been necessary to have virtually every available Generating Unit in California online, including units with low ramp rates. Under such circumstances, the ISO has no option but to make OOM calls to multiple units to run at minimum levels, expecting the need to fully load each unit. If the full extent of the System Emergency is not realized, some of the units may not be needed. If, however, Demand appears as forecast, not having those units on-line and available to ramp up could require severe curtailments and possible blackouts.

B. Dynegy's Requested Relief Is Unnecessary and Inappropriate

Dynegy requests six types of relief. None is appropriate.

First, Dynegy requests that the Commission limit the ISO's authority to dispatch units to situations of an actual or reasonably expected emergency. Dynegy would exclude from that situation those instances in which there are bids available in the super peak PX and APX markets that would satisfy the ISO's needs.¹⁶ The ISO does not, however, call units out-of-market absent an imminent or threatened System Emergency. The ISO dispatches units in advance when it believes they will be needed to address a System Emergency. These calls, though, do not constitute OOM calls unless the Generator specifically declines to bid the unit into the Imbalance Energy market. It is thus not the ISO's failure to purchase Energy price above the cap in the super peak market that transforms the dispatch into an OOM call, but the Generator's failure to bid as permitted in the December 15 Order. If the unit is bid into the Imbalance Energy market at a level that reflects its costs, it will be paid as bid, not according to the OOM payments described in Section 11.4.2 of the ISO Tariff.

Second, Dynegy asks that, when the ISO dispatches a unit because it may be unable to meet Applicable Reliability Criteria, but an emergency does not exist, the ISO be obligated to enter into negotiations pursuant to Section 2.3.5.1.5 of the ISO Tariff.¹⁷ The scope of the ISO's ability to dispatch units pursuant to Section 5.6.1 of the ISO Tariff, however, is not limited to existing System Emergencies, but includes threatened System Emergencies. While the ISO may make use of Section 2.3.5.1.5 in lieu of such a dispatch, it is not

¹⁶ See *id.* at 14-15.

¹⁷ See *id.* at 15.

required to do so. The ISO is, however, required to pay the dispatched unit as bid if the unit owner bids the unit into the Imbalance Energy market. Thus, while Dynegy is not entitled to a negotiated price, it is entitled to a compensatory price – *if it bids the unit*.¹⁸ In this regard, prior notification of the ISO’s requirements assists Dynegy; it can be assured that, if it starts its unit, it will be compensated for the cost. Absent the ISO’s notice, it would start the unit uncertain of whether a bid sufficient to cover its costs would clear the market.

Third, Dynegy requests that the Commission direct the ISO to pay a compensatory rate when it calls a unit out-of-market, and specifies a rate equal to its marginal costs plus a fifteen percent adder to cover fixed costs.¹⁹ As emphasized above, however, Dynegy always has the option of receiving a compensatory rate by bidding into the market. If it chooses not to do so, then it should not complain about the OOM payment under Section 11.4.2 of the ISO Tariff. The Commission has already accepted the ISO’s OOM pricing provisions and has rejected El Segundo Power LLC’s own filing of price terms.²⁰

Fourth, Dynegy asks that the ISO be compelled to enter into negotiations for capacity payments when it issues OOM calls to a unit for five consecutive days.²¹ Because the dispatch orders are not OOM calls unless the unit owner fails to bid, however, the Generator is in control of the longevity of the OOM call.

¹⁸ As the Commission noted in its April 12, 2000, order, OOM pricing applies only when Dynegy has “foregone its opportunity to sell its power bilaterally or through a power exchange.” *California Independent System Operator Corporation*, 91 FERC ¶ 61,026, at 61,086 (2000). If Dynegy does not submit a bid, it is (as a Participating Generator) “bound to accept prices set forth in the ISO Tariff for OOM calls.” *Id.* at 61,087.

¹⁹ See Complaint at 15.

²⁰ See *id.* at 2 n.1, 10.

²¹ See *id.* at 15-16.

The Generator should not be allowed to command a capacity payment by its own actions.

Fifth, Dynegy asks the Commission to direct the ISO to cease and desist from unauthorized use of OOM procedures to demand Energy deliveries in non-emergency conditions.²² As noted above, the ISO does not use OOM calls except in the case of an imminent or threatened System Emergency when no bids are available. If Dynegy is suggesting that the ISO must wait for a System Emergency before making OOM calls, it is imprudently attempting to limit the ISO's authority under the ISO Tariff to prevent System Emergencies.

Finally, Dynegy asks the Commission to direct that the ISO file, within 60 days, a proposal for a third OOM payment option.²³ There is no need for a third OOM option, because every supplier has the opportunity to submit bids that are fully compensatory.

²² See *id.* at 16.

²³ See *id.* at 16-17.

III. CONCLUSION

For the foregoing reasons, the ISO respectfully requests that the Commission deny Dynegey's Complaint.

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