

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

San Diego Gas & Electric Company,)	
Complainant,)	
)	
v.)	Docket No. EL00-95-012
)	
Sellers of Energy and Ancillary Services)	
Into Markets Operated by the California)	
Independent System Operator and the)	
California Power Exchange, Respondents.)	
)	
Investigation of Practices of the California)	
Independent System Operator and the)	Docket No. EL00-98-000
California Power Exchange)	
)	
California Independent System Operator)	Docket No. RT01-85-000
Corporation)	
)	
Investigation of Wholesale Rates of Public)	
Utility Sellers of Energy and Ancillary)	Docket No. EL01-68-000
Services in the Western Systems)	
Coordinating Council)	

**ANSWER OF THE CALIFORNIA INDEPENDENT SYSTEM
OPERATOR CORPORATION TO MOTIONS TO INTERVENE,
COMMENTS, MOTION FOR LEAVE TO FILE COMMENTS OUT OF TIME,
MOTION TO REJECT, AND PROTESTS OF
THE MAY, 11, 2001 COMPLAINT FILING**

On May 11, 2001 the California Independent System Operator Corporation (“ISO”) filed proposed revisions to the ISO Tariff¹ in order to comply with the Commission’s “Order Establishing Prospective Mitigation and Monitoring Plan for the California Wholesale Electric Markets and Establishing an Investigation of Public Utility Rates in Wholesale Western Energy Markets”

¹ Capitalized terms not otherwise defined herein have the same meaning set forth in the Master Definitions Supplement, Appendix A to the ISO Tariff.

issued on April 26, 2001 in the above-captioned proceeding, 95 FERC ¶ 61,115 (“April 26 Order”), and to implement various aspects of that order. The Commission’s May 15, 2001 Notice of Filing in this proceeding directed parties to comment on the ISO’s proposed Tariff revisions (the “May 11 Compliance Filing”) on or before May 22, 2001.

Pursuant to Rule 213 of the Commission’s Rules of Practice and Procedure, 18 C.F.R. § 385.213, the ISO now submits its Answer to the motions to intervene, comments, motion for leave to file comments out of time, motion to reject tariff amendments, and protests submitted in the above-captioned proceeding. The ISO does not oppose the intervention of any party that has sought leave to intervene in this proceeding. For the reasons explained below, however, the comments and protests that seek the rejection or substantive modification of the ISO’s May 11 Compliance Filing are without merit, except where the ISO has agreed to make certain minor modifications in response to such comments. The Commission should accept the ISO’s proposed Tariff revisions without condition and with only such minor modifications as the ISO agrees to below.

I. BACKGROUND

In the April 26 Order, the Commission reaffirmed its previous findings that there is a potential for the exercise of market power in the California wholesale electric markets under certain conditions and mandated that a replacement mitigation plan be put into place. The mitigation plan adopted in the April 26 Order includes:

- increased coordination, control, and reporting of outages;
- a requirement for all sellers that own or control generation in California to offer all their available power in the ISO's real-time Energy market; and
- a price mitigation mechanism for the ISO's real-time Energy market during System Emergencies.

The Commission directed the ISO to submit Tariff revisions to comply with these aspects of the Order within fifteen days and to implement the mitigation plan adopted in the April 26 Order on May 29, 2001. On May 11, the ISO submitted proposed revisions to the ISO Tariff in compliance with the Commission's directives.²

On May 18, 2001, the ISO filed a Status Report in the above-captioned proceeding to update the Commission on the ISO's progress towards implementation of the April 26 Order, to describe the ISO's plans to implement various aspects of the April 26 Order ("May 18 Status Report"). In the May 18 Status Report, the ISO requested guidance on various implementation issues, including the appropriate treatment of generators that had not provided information requested by the ISO and needed for the ISO to implement and monitor the "must-offer" and price mitigation aspects of the April 26 Order. The ISO also requested that the Commission immediately advise the ISO of any necessary modifications to the ISO's plan to implement the April 26 Order.

² In the ISO's May 11 Compliance Filing, the ISO reserved the right to seek clarification or rehearing of any aspect of that order, including those aspects of the April 26 Order to be implemented through the Tariff revisions proposed in the May 11 Compliance Filing. On May 25, 2001, the ISO filed a motion for clarification and request for rehearing of the April 26 Order in the above-captioned proceeding ("May 25 Request for Rehearing"). The ISO's instant answer to comments on the May 11 Compliance Filing addresses only the issue of whether that filing is in compliance with the April 26 Order. The ISO has not modified any of the positions set forth in its May 25 Request for Rehearing.

On May 25, 2001, the ISO filed a second Status Report in the above-captioned proceeding to update the Commission on the ISO's progress towards implementation of the April 26 Order ("May 25 Status Report"). In the May 25 Status Report, the ISO described the progress of its efforts to develop and test the software needed to implement aspects of the April 26 Order, described certain assumptions the ISO intended to utilize in determining the "Proxy Price" to be calculated pursuant to the April 26 Order, and noted the continued non-compliance of a number of generators with requests for the information needed to implement the April 26 Order. The ISO again requested that the Commission immediately advise the ISO of any necessary modifications to the ISO's plan to implement the April 26 Order.

On that same day, the Commission issued its "Order Providing Clarification and Preliminary Guidance on Implementation of Mitigation and Monitoring Plan for the California Wholesale Electric Markets," 95 FERC ¶ 61,275 ("May 25 Order"). In the May 25 Order, the Commission addressed the following four issues:

- treatment of generators who did not supply heat and emission rates;
- calculation of a natural gas proxy price;
- price mitigation in the ISO's Ancillary Service and Congestion Management markets; and
- creditworthiness issues related to implementation of the April 26 Order.

The April 26 Order originally required comments on the ISO's compliance filing within five days of the date of that filing, or May 16, 2001. April 26 Order, 95 FERC at 61,355. The Commission's May 15, 2001 Notice of Filing in this

proceeding apparently extended the date for all interventions, comments, and protests concerning the May 11 Compliance Filing to May 22, 2001. Between May 16 and May 22, 2001, a number of parties filed motions to intervene, comments, and motions concerning the May 11 Compliance Filing.³ Several parties also filed comments on the May 11 Compliance Filing after May 22, 2001.⁴ The ISO does not oppose the intervention of any party in this proceeding. As explained below, however, the comments and protests of those parties in opposition to the May 11 Compliance Filing, except where noted, are without merit and should be rejected. The ISO accordingly requests that the Commission accept the Tariff revisions proposed in the May 11 Compliance Filing, without condition or substantive modification except for such minor modifications as the ISO agrees to below, as bringing the ISO in full compliance with the April 26 Order.

³ These parties include the Cogeneration Association of California and the Energy Producers and Users Coalition (“CAC”); the California Department of Water Resources (“CDWR” or “DWR”); the California Electricity Oversight Board (“EOB”); the California Municipal Utilities Association (“CMUA”); Calpine Corporation (“Calpine”); City of Vernon, California (“Vernon”); Duke Energy North America, L.L.C., and Duke Energy Trading & Marketing, L.L.C. (“Duke”); Dynegy Power Marketing, Inc., El Segundo Power, L.L.C., Long Beach Generation, L.L.C., Cabrillo Power I, L.L.C., and Cabrillo Power II, L.L.C. (“Dynegy”); the Independent Energy Producers Association (“IEP”); the Metropolitan Water District of Southern California (“MWD”); Mirant Americas Energy Marketing, L.P., Mirant California, L.L.C., Mirant Potrero, L.L.C., and Mirant Delta, L.L.C. (“Mirant”); Modesto Irrigation District (“MID”); Northern California Power Agency (“NCPA”); Public Utilities Commission of the State of California (“CPUC”); Pacific Gas and Electric Company (“PG&E”); Reliant Energy Power Generation, Inc. (“Reliant”); the Sacramento Municipal Utility District (“SMUD”); the Salt Rive Project Agricultural Improvement and Power District (“SRP”); San Diego Gas & Electric (“SDG&E”); Southern California Edison Company (“SCE”); and Williams Energy Marketing & Trading Company (“Williams”).

⁴ These parties include the Western Power Trading Forum (“WPTF”) and AES Southland (“AES”). Since the May 22 deadline already constituted a six-day extension from the deadline for comments established by the April 26 Order, the ISO sees no reason why the Commission should entertain these comments. Nonetheless, the ISO responds to the comments filed by these parties below.

II. ANSWER TO COMMENTS, MOTION TO REJECT, AND PROTESTS⁵

A. Outage Coordination

In the April 26 Order, the Commission held that, “[t]he ISO must be provided the authority to achieve greater systematic control over all units (including those of the IOUs) that the ISO must dispatch, *i.e.*, those units that have signed PGAs [Participating Generator Agreements].” April 26 Order, 95 FERC ¶ 61,115, at 61,355. Accordingly, the Commission directed the ISO to “make a tariff filing within 15 days of this order proposing a mechanism for coordination and control of outages, including periodic reports to the Commission, consistent with the discussion in this order.” *Id.*

As explained in the ISO’s May 11 Compliance Filing, the ISO already has significant authority under its Tariff to approve and modify planned outages for Participating Transmission Owners and Reliability Must-Run (“RMR”) Generating Units. In the May 11 Compliance Filing, the ISO implemented the outage coordination requirements of the April 26 Order by modifying these existing provisions of the ISO Tariff, which the Commission has already found to be just and reasonable, to encompass all Generating Units owned or controlled by any Participating Generator. The ISO also proposed minor modifications to the

⁵ Some of the Intervenors commenting substantively on the May 11 Compliance Filing do so in portions of their pleadings variously styled as “Comments,” “Motion to Reject Tariff Amendments,” or “Protest,” without differentiation. There is no prohibition on the ISO’s responding to the comments or motions in these pleadings. The ISO is entitled to respond to these pleadings and requests notwithstanding the label applied to them. *Florida Power & Light Company*, 67 FERC ¶ 61,315 (1994). In the event that any portion of this answer is deemed an answer to protests, the ISO requests waiver of Rule 213 (18 C.F.R. §385.213) to permit it to make this answer. Good cause for this waiver exists here given the nature of this proceeding and the usefulness of this answer in ensuring the development of a complete record. *See, e.g., Enron Corporation*, 78 FERC ¶ 61,179 at 61,733, 61,741 (1997); *El Paso Electric Company*, 68 FERC ¶ 61,181 at 61,899 and n. 57 (1994).

existing schedules and deadlines for submitting requests for outage approvals to the ISO. This straightforward approach implements and is fully consistent with the Commission's mandate in the April 26 Order that the ISO achieve greater systematic control over Participating Generators.

1. Types of Generating Units Subject to ISO Outage Coordination and Scheduling

Notwithstanding the clarity of the April 26 Order, a number of parties challenge the scope of the ISO's outage coordination proposal, arguing for exemptions for various categories of Generating Units owned or controlled by Participating Generators. These protests are plainly complaints about the direction provided in the April 26 Order, not about the ISO's implementation of that direction. As noted above, the April 26 Order directed the ISO to expand its outage coordination and control authority to encompass all "units that have signed PGAs." The April 26 Order did not exempt those Generating Units that are Qualifying Facilities,⁶ hydroelectric facilities,⁷ jointly owned with non-Participating Generators,⁸ or owned or controlled by Participating Generators that are municipal utilities.⁹ Comments objecting to the scope of units subject to increased ISO coordination of outages under the April 26 Order therefore go beyond the only relevant question for this docket: whether the ISO's May 11 Compliance Filing appropriately implements that order. Those objections must

⁶ See CAC at 2-5.

⁷ See DWR at 3.

⁸ See SRP at 5,10.

⁹ See, e.g., SMUD at 3; NCPA at 4, 8.

be raised with the Commission either through a request for rehearing or motion for clarification.

Moreover, the ISO Tariff's outage coordination and control provisions already apply to Generating Units that are designated as RMR Units, including RMR Units owned by municipal utilities, as well as hydroelectric RMR Units. The ISO's outage coordination program is sufficiently flexible to accommodate the special needs of these and other Generating Units for which intervenors seeks exemptions. In contrast, the categorical exemptions sought by these intervenors would undermine the objective of the April 26 Order: enhancing the ability of the Commission and the ISO to ensure that generators do not abuse the outage scheduling process to exploit opportunities to exercise market power.

The Tariff revisions concerning outage coordination submitted in the May 11 Compliance Filing only extend the ISO Tariff outage coordination requirements to "Participating Generators". The ISO Tariff already provides that "Operators" (*i.e.*, owners of transmission facilities that comprise the ISO Controlled Grid) must coordinate their transmission outages with the ISO. The ISO's proposed Tariff language merely modifies the definition of "Operators" to include Participating Generators, thus complying with the April 26 Order. Accordingly, the ISO's proposed Tariff revisions reflect the fact that the ISO's outage coordination program includes (1) all transmission facilities that comprise the ISO Controlled Grid and (2) all Generating Units subject to Participating Generator Agreement.

2. Consideration of Market Impacts In Scheduling and Approving Outages

In its order accepting Amendment No. 25 to the ISO Tariff, the Commission authorized the ISO to cancel approved maintenance outages of transmission facilities forming part of the ISO Controlled Grid, when necessary to preserve System Reliability or to avert “unduly significant market impacts,” provided the ISO compensates the affected Participating TO for the direct and verifiable costs associated with the outage cancellation. *California Independent System Operator Corp.*, 90 FERC ¶ 61,316 (2000); *see also California Independent System Operator Corp.*, 91 FERC ¶ 61,341 (2000) (accepting the ISO’s definition of “unduly significant market impacts”). In the May 11 Compliance Filing, consistent with the approach described above, the ISO extended this provision, too, to encompass Participating Generators.

Despite the Commission’s previous approval of such authority, nine parties argue that the ISO should not consider potential adverse market impacts in the ISO’s outage coordination and scheduling program.¹⁰ Two parties agree, however, that the ISO should consider market impacts in approving and canceling outages.¹¹

The ISO strongly urges the Commission to continue to recognize that both System Reliability and market impact considerations are essential factors to be considered both in the scheduling and canceling of Approved Maintenance Outages. As discussed above, the Commission has already approved the ISO’s

¹⁰ These parties are SMUD, SRP, Mirant, CMUA, Duke, Reliant, Dynegy, WPTF and AES.

¹¹ These parties are PG&E and MID.

authority to consider market impacts in scheduling transmission facility outages. In expanding the ISO's outage coordination program to include Generating Units owned or controlled by Participating Generators, it is reasonable to include the outages of those facilities, as well, within that existing authority. As is the case with transmission facility outages, some generation outages may have such a significant impact on the California wholesale energy markets that no prudent utility would have scheduled such outages had it anticipated the effect the outage would have. The Commission has recognized as much in the April 26 Order when it expressed concern that uncontrolled outages were significantly contributing to the excessive prices in the California wholesale markets.

For example, circumstances can arise where a forced generation or transmission outage coupled with an approved generation outage may require the curtailment of firm load if the ISO were unable to reschedule the planned generation outage. While curtailment may be acceptable from the perspective of maintaining the reliability of the transmission system, the market impacts may be unacceptable. Thus the ISO must be able to consider both System Reliability and market impacts in coordinating and scheduling outages. The ISO believes that its ISO's May 11 Compliance Filing appropriately includes unduly significant market impacts as one of several factors to be considered in coordinating outages.

3. Compensation for Canceled Outages

As noted above, the Commission's prior approval of the ISO's authority to cancel Approved Maintenance Outages was conditioned upon compensation to

the affected Participating TO for the direct and verifiable costs associated with the outage cancellation.¹² Consistent with that requirement, the ISO proposed revisions to Section 2.3.3.6.3 in the May 11 Compliance Filing that will provide Participating Generators with the opportunity, under certain conditions and subject to specified requirements and limitations, to obtain compensation for the direct and verifiable costs that a Participating Generator incurs due to the ISO's "last-minute" cancellation of an Approved Maintenance Outage. In the May 11 Compliance Filing, the ISO explained that, although Participating Generators with market-based rates have a much greater opportunity to protect themselves from the costs of last-minute cancelled outages than do Participating Transmission Owners under a regulated cost-of-service rate structure, the ISO has elected to afford comparable treatment to Participating Generators and Participating Transmission Owners subject to the ISO Tariff's outage coordination requirements.

Six parties comment in favor of the ISO proposal to compensate generators for costs incurred as a result of ISO cancellation of approved outages.¹³ In addition, however, these parties argue that the ISO should be required to reimburse generators for additional costs, other than those enumerated in the proposed Tariff revisions. That is, they argue that Participating Generators should receive greater compensation for cancelled generation outages than Participating TOs receive for cancelled transmission

¹² *California Independent System Operator Corp.*, 90 FERC ¶ 61,316 at 62,050-51 (2000).
¹³ These parties are Mirant, NCPA, DWR, AES, Duke and WPTF.

outages. On the other hand, the CPUC asserts that the ISO should not reimburse generators for cancellation costs of approved outages because Participating Generators “with market-based rates have a much greater opportunity to protect themselves from the costs of last-minute cancelled outages than do [PTOs] under cost-of-service rate structure.” CPUC at 5.

The arguments of those intervenors seeking additional compensation for cancelled outages ignore the fact that a limitation to direct costs was deemed sufficient for Participating TOs and are insulting in the face of the profits reaped by such generation owners over the past year. Predictably, these generation owners want to the ISO and consumers to assume all of their market risk – an argument that is facially at odds with the precepts of a competitive marketplace; principles that they repeatedly champion.. If anything, Participating Generators should be entitled to less compensation for cancelled outages, because their ability to earn market-based rates allow them to mitigate the risks of cancelled outages to a far greater extent than Participating TOs – who are limited to cost-based recovery for transmission costs. Nonetheless, and with the noted reservation, the ISO’s May 11 Compliance Filing treats both entities alike.

Quantification of indirect costs is difficult and typically a highly subjective exercise. As such, the potential for reimbursement of indirect costs is susceptible to abuse and difficult to police. Even without compensation for lost profits and other indirect costs, the requirement that the ISO compensate a Participating Generator for the direct costs attributable to a cancelled outage will represent a significant expense associated with the exercise of that authority.

Such a requirement thus will provide substantial assurance that the ISO will not abuse the authority.

4. The Proposed Tariff Revisions Are Not Too Vague

Seven parties suggest that the ISO Tariff revisions relating to outage coordination are too vague and/or broad and contend that the ISO's proposal to continue to post operating procedures and changes to such procedures on the ISO's Home Page is unacceptable.¹⁴

These objections ignore the fact that the ISO has made very limited changes to its existing outage coordination program other than the simple expansion of the relevant Tariff provisions to include Generating Units covered by a Participating Generator Agreement. What was acceptable for Participating TOs and RMR Units is acceptable as applied to Participating Generators. Moreover, the ISO has had in place a policy concerning the promulgation and revision of ISO Operating Procedures since June of 1999 and this policy includes an opportunity for stakeholder input.

The ISO's outage coordination process, as it existed before, and as supplemented by the May 11 Compliance Filing, is substantially more detailed than those of other independent system operators. For example, PJM's outage coordination provisions consist, in total, of a single paragraph, supplemented by unfiled manuals. See PJM OA, Schedule 1, § 1.9.3. The ISO, in contrast, has filed many pages of detailed Tariff provisions, supplemented by the filed Outage Coordination Protocol. Those detailed provisions more than satisfy the statutory

¹⁴ These parties include IEP, SCE, Duke, Reliant, Dynegy, WPTF and AES.

requirements. At the same time, they give the ISO the necessary flexibility to make minor adjustment to its procedures, as circumstances require.

In determining what level of detail needs to be included in a filed tariff, the Commission applies a “rule of reason.” The Commission uses this “rule of reason” to decide which of an “infinite of practices affecting rates and services” must be submitted for Commission approval and to determine the level of detail concerning those practices which must be included in jurisdictional filings.¹⁵ The Commission has held in numerous cases that the rule of reason does not require submission of every document which describes the details of how a utility will implement its rates, terms and conditions. More specifically, the Commission has held on several occasions that ISO Operating Procedures need not be filed with the Commission. *See, e.g., California Independent System Operator Corp.*, 90 FERC ¶ 61,316, at 62,046 (2000) (“Under our existing ‘rule of reason,’ we agree with the ISO that technical standards for the provision of regulation imports need not be included in its tariff.”).

5. The Proposed Change To Tariff Section 2.3.3 to Change the Lead Time for Requesting Outages From 3 to 5 Days is Reasonable

One of the few changes to the ISO’s existing outage coordination and provisions proposed in the May 11 Compliance Filing was an extension from three days to five days of the lead time for an Operator’s scheduling of a Maintenance Outage not included in its annual plan or the rescheduling of a

¹⁵ *See, e.g., Prior Notice and Filing Requirements Under Part II of the Federal Power Act*, 64 FERC ¶ 61,139, at 61,988 (1993), *citing City of Cleveland v. FERC*, 773 F.2d 1368 (D.C. Cir. 1985).

Maintenance Outage included in the plan. Five intervenors objected to this change.¹⁶ This modest extension, however, is plainly reasonable in light of the expanded scope of the ISO's outage coordination responsibilities under the April 26 Order. In addition to transmission facilities and RMR Units, the ISO now will have to schedule Maintenance Outages for all Generating Units owned or controlled by Participating Generators. It will necessarily require more time for the ISO to process requests for modifications of outage schedules. Extending this lead time also encourages good outage scheduling practices by generators and minimizes their ability to manipulate outages to take advantage of anticipated changes in short-term market conditions. The ISO also notes that a five (5) day notice is considerably shorter than that employed by, for example, the Northwest Power Pool Coordinated Outage System. Under that system, a generator must provide a 45-day advance notice of outages that are not included in that generator's long-range outage plan.

Finally, the intervenors fail to note that the requirement for five days notice is not absolute. Section 2.3.3.3 provides that an outage will be approved with less than five days notice if it is one that could not have been foreseen in enough time to be included in the coordination process described in the ISO Tariff, it will not compromise reliability, and it will not cause unduly significant market impacts. Intervenors identify no reason why an Operator should be permitted to schedule a Maintenance Outage on less than five days notice if these criteria are not met.

¹⁶ These parties include DWR, PG&E, MID, Reliant and Dynegy.

6. Automatic Sunset of the Outage Coordination Provision is Not Appropriate

Several parties suggest that the ISO's expanded outage coordination provisions should only apply for a limited period.¹⁷ These comments are misplaced. As an initial matter, there is nothing in the April 26 Order which suggests that sunset provisions should be included in the ISO Tariff's outage coordination provisions. Moreover, the April 26 Order applies a sunset date only to the price mitigation mechanism it prescribes, not to the extension of ISO outage coordination processes to Generating Units covered by a Participating Generator Agreement. The need for increased outage coordination will remain and, indeed, increase should price mitigation measures expire.¹⁸ Further, other independent system operators presently have such outage coordination authority that applies to all generators. There is no reason why the ISO's similar authority should require reauthorization. Lastly, expanded outage coordination provisions are necessary to comply with California state law, which has no automatic sunset provision.

7. The Appropriate Appeals and Dispute Resolution Processes Are Already In Place

Several generator intervenors argue that a special dispute resolution process, administered by the Commission, should be instituted for outage scheduling disputes.¹⁹ No special provisions, however, are required. The ISO

¹⁷ These parties include SMUD, Reliant, WPTF and SCE.

¹⁸ As explained in the ISO's May 25 Request for Rehearing, the ISO does not believe there is any justification for allowing price mitigation measures to expire in one year.

¹⁹ See Duke at 4, Reliant at 10-11; Dynegy at 11.

Tariff already includes a detailed dispute resolution process that has been approved by the Commission. Further, consistent with the April 26 Order and the ISO's May 11 Compliance Filing, to forward to the Commission information on all questionable outages and disputes that are not settled within existing ISO processes.

8. There is No Justification for Alternative Outage Procedures

Reliant and WPTF argue that the ISO should adopt new procedures to resolve incompatible outage requests. Reliant proposes a system in which the ISO would give generators a chance to submit alternative outage proposals and to reschedule outages voluntarily. Reliant at 10-12. WPTF recommends that outages be scheduled on a first-come, first-served basis, in which the ISO's only role is to time stamp requests so that priorities can be established. WPTF at 5.

Both of these proposals go well beyond the ISO's May 11 Compliance Filing, which relies on the use of the ISO's existing outage coordination program. This program includes substantial reliance on the first-come, first-served principle advocated by WPTF and on the ability of Operators to propose outage schedules and revised schedules, as Reliant recommends. These parties go too far and depart from the direction of the April 26 Order, however, when they urge a more passive role for the ISO in outage coordination and control. The April 26 Order relies on the ISO's active participation in the outage coordination process to maintain System Reliability and to deny Market Participants the opportunity to exercise market power through the scheduling of outages. The ISO's May 11

Compliance Filing appropriately implements the approach required by the Commission.

9. ISO Sanctions

The CPUC “believes it would be a waste of resources for the ISO to make a filing at FERC over every dispute with a recalcitrant Participating Generator. The ISO should be empowered to impose monetary and/or other sanctions on Participating Generators who fail to comply. . .” CPUC at 6. On the other hand, Dynegy and AES propose elimination of pre-existing ISO Tariff Section 2.3.2.9.3 (providing that the ISO may impose sanctions on Transmission Owners or generators if the ISO finds that the entity’s operation and maintenance practices prolong the response time or prolong an outage during a system emergency). Dynegy at 5-6; AES at 4.

The ISO proposed no revisions to Section 2.3.2.9.3 in the May 11 Compliance Filing. The ISO currently has certain sanction and penalty authority as provided under the Tariff, and has not proposed to reduce or expand such authority. Comments on the May 11 Compliance Filing are inappropriate vehicles for intervenors to object to existing Tariff provisions that are unaffected by that filing. Modifications to the ISO’s existing authority would require the institution of a proceeding under Section 206 of the Federal Power Act and a specific Commission finding that the existing provisions of the ISO Tariff are unjust and unreasonable. Further, the ISO, in its May 11 Compliance Filing specifically complied with the intent of the April 26 Order that the ISO’s outage coordination requirements should foster cooperation rather than penalize

generators. To the extent circumstances warrant in the future, however, the ISO stands ready to propose expanded sanction authority, most notably with respect to Forced Outages that have not been sufficiently justified

10. The May 11 Compliance Filing’s Reference to State Law Is Appropriate

The EOB’s comments speak favorably of the ISO’s reference to Executive Order D-23-01 and the ISO observation in the May 11 Compliance Filing that, should the California legislature enact new laws addressing the ISO and outage coordination, the ISO may be required to propose additional Tariff revisions in the future. EOB at 2. On the other hand, Dynegy and AES object to these same references, commenting that state law is irrelevant to outage coordination and constitutes a collateral attack on the Commission’s order. Dynegy at 7; AES at 3.

The reference to State legal requirements in the ISO’s May 11 Compliance Filing is factual. In that filing, the ISO proposes only to confirm that it will coordinate generator outages “in accordance with applicable law.” It is inconceivable that this statement, in and of itself, can be construed as something objectionable or contrary to the April 26 Order. To the extent that a State law may require the ISO to further modify Tariff provisions governing the ISO outage coordination program, the ISO will make an appropriate filing with the Commission in the future.

11. Operation of The ISO Outage Coordination Office

SCE suggests that, given the scope of power and responsibility that the ISO proposes to vest in the Outage Coordination Office, this office must be operated 24 hours a day and seven days a week. SCE at 8-9. As an initial

matter, the ISO notes that this comment does not address the Tariff revisions submitted in the May 11 Compliance Filing and is therefore beyond the scope of this proceeding. Nonetheless, the ISO recognizes the need to have personnel available to address outage coordination concerns at all times. This is especially true in light of the ISO's expanded duties in this area. The ISO does not believe, however that the Outage Coordination Office needs to be manned 24 hours a day, seven days a week. For the most part, the generator and Transmission Owner representatives that interact with the ISO Outage Coordination Office do not work 24 hours per day. The ISO's outage personnel therefore would have no one with whom to coordinate during non-business hours. In the event there is a need to coordinate an outage request outside normal business hours, the ISO does have Operations staff available at all times who are prepared to address urgent outage coordination requests, however rare they may be. Thus, the ISO is prepared to assume the responsibilities that come with the expanded outage coordination authority conferred by the April 26 Order, as reflected in the ISO's May 11 Compliance Filing.

B. Selling Obligation

In the April 26 Order, the Commission established a requirement that all non-hydroelectric generators in the State of California “offer the ISO all of their capacity in real time during all hours if it is available and not already scheduled to run through bilateral agreements.” April 26 Order, 95 FERC at 61,356. This requirement applies not only to Participating Generators, but to all “non-public utility sellers that own or control generators in California” as a condition to their

participation in the ISO's markets or use of the ISO Controlled Grid. *Id.* As discussed below, all such entities are also subject to the price mitigation aspects of the April 26 Order. The ISO was directed to modify its Tariff to reflect these conditions and this requirement.

In the May 11 Compliance Filing, the ISO proposed Tariff revisions to make it clear that the selling obligation established by the April 26 Order is applicable to all "Must-Offer Generators," defined as either a Participating Generator or any entity that owns or controls one or more non-hydroelectric Generating Units located in California from which Energy or capacity is either: (i) sold through any market operated by the ISO, or (ii) transmitted over the ISO Controlled Grid.²⁰ This obligation applies to all available capacity from the Must-Offer Generator for which Energy is not scheduled in the responsible Scheduling Coordinator's Final Hour Ahead Schedule.

1. Applicability of the Must-Offer Requirement.

A number of parties contend that they should be exempt from the requirement that they offer all available non-hydroelectric generation in the ISO's real-time Energy market or take issue with the ISO's proposed definition of "Must-Offer Generator."

Many of these comments challenge the requirements imposed by the April 26 Order itself, as opposed to the proposed Tariff revisions implementing those

²⁰ This would include units in Control Areas in California other than the ISO Control Area. As explained below, the ISO believes slight modifications to the proposed definition of "Must-Offer Generator" are appropriate in order to make it clear that the requirement applies to generating units in the State of California but outside of the ISO Control Areas. The defined term "Generating Unit" in the ISO Tariff is limited to units located within the ISO Control Area.

requirements. For example, SMUD objects to the applicability of the must-offer requirement to generation owned or controlled by entities that are not “public utilities” under the Federal Power Act, such as municipal utilities, and notes that this issue will be raised in SMUD’s request for rehearing of the April 26 Order. SMUD at 7-8. SMUD does not contend that the ISO’s proposed Tariff revisions fail to implement that aspect of the April 26 Order and, indeed, its comments acknowledge that the April 26 Order explicitly subjects municipal utilities to the must-offer requirement. Comments objecting to the scope of this requirement go beyond the question of whether the ISO’s May 11 Compliance Filing appropriately implements the April 26 Order and must be raised with the Commission either through a request for rehearing or motion for clarification.

Some municipal utilities suggest that they are not subject to the must-offer requirement despite the plain language of the April 26 Order. These municipal utilities object to aspects of the May 11 Compliance Filing that would include municipally-owned units within the definition of “Must-Offer Generators.” For example, Vernon explains that its Generating Units, including two older diesel Generating Units being brought back into service this summer to alleviate the risk of rolling blackouts in Vernon’s service territory, are utilized solely to serve Vernon’s retail customers. Vernon contends that the delivery of Energy or capacity from these units does not involve the use of the ISO Controlled Grid and that these units therefore are not subject to the must-offer requirement of the April 26 Order. The ISO is sympathetic to Vernon’s concern that it retain the ability to serve Vernon’s customers from the generation that it owns. As

discussed below, the ISO agrees in this Answer to modify the proposed definition of “Available Generation” in Section 5.11.2, in order to take into account generation committed to serve a Load-serving entity’s native load customers in real-time. While not explicit in the Commission’s April 26 Order, the ISO believes that this is a reasonable interpretation of the must-offer requirement. However, to the extent practicable, the ISO intends to monitor and determine a unit’s available capacity and report to the Commission all instances where the ISO believes Must-Offer Generators have inappropriately withheld capacity from the ISO’s real-time market on the premise such capacity was necessary to serve native load obligations. Such concerns aside, however, Vernon’s claim that generation and Load behind the Vernon city-gate does not involve the use of the ISO Controlled Grid is incorrect.

As Vernon notes in its comments, Vernon’s Generating Units are both within the State of California and the ISO’s Control Area. Vernon at 6.²¹ As a Control Area Operator, the ISO has responsibilities to maintain the reliability of Control Area transmission facilities. Among other things, these responsibilities include the procurement of Operating Reserves sufficient to ensure reliable service to the Load and generation of entities like municipalities and Qualifying Facilities (“QFs”) that is currently “behind-the meter.” In an ongoing proceeding currently being litigated before an FERC Administrative Law Judge, a witness for the Western Systems Coordinating Council (“WSCC”) has confirmed that the ISO

²¹ In fact, Vernon is a Participating Transmission Owner that has executed the Transmission Control Agreement with the ISO and transferred operational control of its transmission facilities to the ISO.

must procure sufficient Operating Reserves (*i.e.*, Ancillary Services) for such behind-the-meter Load in order for the ISO to satisfy WSCC Minimum Operating Reliability Criteria (“MORC”) and to maintain the reliability of the ISO Controlled Grid. See Deposition of Joseph W. Comish, Docket Nos. ER98-997-000, et al. (Feb. 14, 2001) at 12:8-13:20. The statements of the WSCC confirm that the ISO must have data on all Load within the ISO Control Area if the ISO is to fulfill its statutory and regulatory obligation to satisfy WSCC reliability criteria. Because the ISO must obtain Operating Reserves to cover the potential loss of generation serving Load behind a municipality city-gate and Energy from those reserves will be delivered using the ISO Controlled Grid when generation behind the city-gate is lost, the generation owned by a municipality such as Vernon and dedicated to the service of native-load customers involves the use of the ISO Controlled Grid. Such generation would therefore be subject to the must-offer requirement of the April 26 Order.

Vernon requests that the Commission order the ISO to provide a mechanism for entities that seek to sell available generation in the ISO’s real-time Energy market (*e.g.*, entities that are subject to the must-offer requirement) under which such entities would not be subject to the terms and conditions of a Participating Generator Agreement. Vernon at 7-9. There is no justification for such a request. The ISO Tariff currently provides that the owners or operators of all Generating Units from which Energy or Ancillary Services are sold in the ISO’s markets must undertake to be bound by the ISO Tariff through a Participating Generator Agreement. See Section 5 of the ISO Tariff; definition of “Participating

Generator.” Although the April 26 Order imposes a new requirement on many entities to sell available generation into the ISO’s real-time Energy market, it does not modify the existing requirements of the ISO Tariff. Thus, to the extent that Vernon or other entities have “Available Generation” in real-time, they are required to sell that generation into the ISO’s real-time Energy market and are subject to the terms of the ISO Tariff applicable to generators that participate in the ISO’s markets, whether or not they have executed a Participating Generator Agreement.²²

Several parties suggest that the April 26 Order’s requirement that generators in California sell available energy into the ISO’s real-time Energy market does not or should not apply to QFs. See IEP at 4-6, Calpine at 5-7. They argue that the ISO’s proposed definition of “Must-Offer Generator” should be modified to exclude QFs, or at least those QFs that are selling power pursuant to existing Power Purchase Agreements (“PPAs”). As with the applicability of the April 26 Order to municipal utilities, the question of whether the April 26 Order’s “must-offer” requirement *should* apply to QFs must be taken up with the Commission through a rehearing request. It is clear from the April 26 Order, and the more recent May 25 Order, however, that QFs currently are subject to this requirement. The April 26 Order establishes that “*all* sellers of energy that own or control [non hydro-electric] generators in California” are subject to this

²² The ISO notes that, even under the April 26 Order, entities such as Vernon need not bid their Available Generation directly into the ISO’s real-time Energy market if they have made arrangements to sell such Energy to another party, such as CDWR through a bilateral transaction and schedule that Energy in the ISO’s Day-Ahead or Hour-Ahead Market .

requirement. April 26 Order, 95 FERC at 61,358 (emphasis added). The Commission exempted only hydro-electric generation from this requirement; it made no exception for non-hydro QFs.

Moreover, the May 25 Order further demonstrates that the must-offer requirement is applicable to QFs. In the May 25 Order, the Commission noted that owners and operators of numerous Generating Units, including many QF units, have not provided the Commission and the ISO with some or all of the information needed to implement the April 26 Order. The Commission therefore accepted the ISO's proposal to utilize a \$0/MWh standing real-time Energy bid for such non-compliant units. The Commission cited its May 16, 2001, order addressing pricing for QF Energy sales in the ISO's real-time market²³ as support for the statement that "[t]o the extent a non-compliant seller does not wish to be treated as a price-taker, the ISO's approach will provide such entities with an incentive to provide the ISO and the Commission with the requisite data," May 25 Order, slip op. at 4.

The ISO issued a Market Notice on May 16, 2001, addressing the applicability of the April 26 Order to QFs.²⁴ In that Market Notice, the ISO explained that the April 26 Order's must-offer and price mitigation requirements apply to all QFs in California because "[a]ll QFs in California use the interstate transmission facilities operated by the ISO, whether supplying power under

²³ *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.*, 95 FERC ¶ 61,226 ("May 16 QF Order").

²⁴ A copy of that market notice (the "May 16 Market Notice") is provided as Attachment A to this Answer.

power purchase agreements (PPA) with the UDCs or engaging in bilateral transactions.” Calpine suggests that the following language from the May 16 Market Notice creates some ambiguity as to whether the ISO intends to apply the must-offer provisions to QFS with PPAs:

If a QF has either: (1) a PPA with the UDC that has expired (or who has received a regulatory or court order allowing the QF to sell the contracted-for capacity to third parties) or (2) capacity in excess of the amounts under contract to the UDCs, then the QF is subject to the "must-offer" condition and it must comply with reporting requirements outlined below.

Calpine at 4-5. There is no ambiguity in the May 16 Market Notice. The notice clearly states that all QFs in California are subject to the must-offer requirement. The language cited by Calpine simply addresses the question of whether a QF will be considered to have “Available Generation.” As a practical matter, only Energy from those QFs with Available Generation (*i.e.*, whose output is not fully committed under a PPA) will be offered in the ISO’s real-time Energy market. As such, it is only those QFs with “Available Generation” that must offer such Available Generation to the ISO in real-time and thus satisfy the Commission’s must-offer requirement.

Calpine suggests that QF power delivered to a California utility pursuant to a PPA should not be subject to the must-offer requirement because “QFs do not schedule this power over the ISO controlled grid nor do they require the services provided through the ISO’s open access transmission tariff in any way.” Calpine at 6. This is an inaccurate statement. First, and most importantly, while there may be disputes as to whether the full output of each QF is included in schedules, the host Utility Distribution Company of each QF is currently

responsible for submitting a schedule that reflects QF output. Thus, QF output is already scheduled with the ISO. Moreover, as noted above, a representative of the WSCC has confirmed that the ISO must procure Operating Reserves to serve Load “behind-the-meter” at the site of a QF. In its Initial Brief in a pending proceeding relating to the obligations of QFs under the *pro forma* Participating Generator Agreement and the ISO Tariff, the ISO explains that it therefore must have data on all Load served by QF generation in order to fulfill its reliability obligations. To the extent that QF Load is not supported by self-provided Ancillary Services, the ISO also must procure Operating Reserves and other Ancillary Services for such QF Load and must use the ISO Controlled Grid to deliver these Ancillary Services. Thus, even those QFs with PPAs rely upon the ISO Controlled Grid and make use of services provided by the ISO pursuant to the ISO Tariff.

Calpine further argues that QFs selling power under PPAs should be exempted from the definition of “Must-Offer Generators” because such units “are not required to execute PGAs.” Calpine at 5. To the extent QFs are Generating Units in the state of California, they are subject to the April 26 Order’s must-offer requirement regardless of whether they are Participating Generators, and are appropriately within the definition of “Must-Offer Generators.” Nonetheless, most QFs in the State of California are currently the subject of a Participating Generator Agreement. Those QFs that have not directly entered into a PGA but which have a Power Purchase Agreement with a Participating TO like PG&E or SCE are listed on the PGA of that Participating TO.

Several parties raise additional issues about the applicability of the must-offer requirement. IEP suggests revisions to the definition of “Must-Offer Generator” in Section 5.11.1 which would limit the applicability of that provision. Specifically, IEP proposes replacing the language which would apply the requirement to the entities that own or control non-hydroelectric Generating Units located in California from which energy or capacity is “transmitted over the ISO Controlled Grid” with the following: “(ii) purchased or sold in transactions that require the person to acquire transmission services from the ISO to effectuate such purchases for resale or sales for resale.” IEP at 2-3. There is nothing in the April 26 Order to support such a change. The April 26 Order does not limit the must-offer requirement to only those entities that obtain transmission service from the ISO. Instead, the requirement applies to “all sellers of energy that own or control generators in California, including non-public utilities, whose power is transmitted over the ISO-controlled interstate transmission facilities.” April 26 Order, 95 FERC at 61,356. Thus, the requirement would apply to all entities that make use of the ISO Controlled Grid, whether that use is pursuant to the terms of the ISO Tariff or an alternative arrangement such as an Existing Transmission Contract. Moreover, as noted above, the ISO is required to take all Load and generation in its Control Area into account in order to satisfy WSCC reliability criteria. Thus, the ISO must procure a sufficient amount of Operating Reserves to reliably serve that Load and therefore must utilize the ISO Controlled Grid to deliver such reserves. For these reasons IEP’s proposed changes are inappropriate.

SRP objects to the use of the term “Generating Units, System Units, and System Resources” in some of the revised Tariff provisions proposed in the May 11 Compliance Filing. SRP contends that the April 26 Order applies only to in-state units and argues that these Tariff provisions should be modified to reflect such a limitation. SRP at 5-7. The ISO agrees that, under the April 26 Order, the must-offer requirement applies only to Participating Generators and other generators in the State of California. There are generators, however, that are within the State of California but that are not in the ISO’s Control Area. Such generators would be subject to the must-offer requirement even though they would be considered “System Resources” and not “Generating Units” as that term is defined in the ISO Tariff. As noted above, the term “Generating Unit” as defined in the ISO Tariff is limited to units within the ISO Control Area. In order to cover all of the resources subject to the must-offer requirement under the April 26 Order, *i.e.*, all generators in the State of California, the ISO believes that proposed Section 5.11.1 should be modified as follows:

5.11.1 Applicability

The requirements of Section 5.11 shall apply to (a) all Participating Generators, and (b) all persons, regardless of whether the person is a “public utility” as defined in Section 201 of the Federal Power Act, that own or control one or more non-hydroelectric Generating Units, System Units or System Resources located in California from which energy or capacity is either: (i) sold through any market operated by the ISO, or (ii) transmitted over the ISO Controlled Grid. Each person described in this Section 5.11.1 is referred to in the ISO Tariff as a “Must-Offer Generator.” The requirements of this Section 5.11 shall apply to all non-hydroelectric Generating Units located in California that are owned or controlled by a Must-Offer Generator.

In addition, the specific provision that SRP seeks to modify – Section 2.5.23.3.5 – implements the price mitigation aspects of the April 26 Order and not the must-offer requirement of the April 26 Order. The price mitigation aspects of the order are not limited to in-state entities.²⁵ For these reasons, the changes sought by SRP would be contrary to the April 26 Order.

2. Definition of Available Generation

Some parties raise issues concerning the proposed definition of “Available Generation” in the May 11 Compliance Filing. A number of parties, including Reliant and Duke (Reliant at 6; Duke at 11-13), urge that the definition of “Available Generation” be revised to recognize the April 26 Order’s directive that “Under the must-offer obligation, no generator will be required to run in violation of its certificate or applicable law.” April 26 Order, 95 FERC at 61,357. The ISO agrees that the definition of “Available Generation” should be revised to reflect this limitation, but believes that the revisions proposed by Duke are too ambiguous. The ISO instead agrees to the revisions described below to address these concerns.

SMUD asserts that the definition of “Available Generation” should be modified to account for capacity committed by a Load-serving entity to serve its

²⁵ The April 26 Order provides that “bids must be accepted from resources located outside California, and these bidders, if dispatched, can elect to be paid the market clearing price or can submit their own bid price. If they submit their own bids, such bids will not be used in setting the market clearing price during mitigated periods.” April 26 Order, 95 FERC at 61,359. The order does not expressly state that out-of-state Generators must provide justification for their bids above the MCP, although there are indications that the Commission intended this requirement to apply to them. In the ISO’s March 25, 2001 Request for Rehearing in this Proceeding, the ISO requested confirmation that these bids are also subject to justification and review by the Commission.

native load customers. SMUD at 8-13. The ISO agrees that such a modification is appropriate, although it does not agree with the extensive Tariff revisions proposed by SMUD. In order to address these comments, the ISO instead commits to modify Section 5.11.2 in a subsequent compliance filing to be submitted in this proceeding as follows:

5.11.2 Available Generation

For the purposes of this Section 5.11, a Must-Offer Generator's "Available Generation" from a non-hydroelectric Generating Unit shall be (a) the Generating Unit's maximum operating level adjusted for any outages or reductions in capacity reported to the ISO in accordance with Section 2.3 or 5.11.3 and for any limitations on the Generating Unit's operation under applicable law, which shall be reported to the ISO, (b) minus the Generating Unit's scheduled operating point as identified in the ISO's Final Hour-Ahead Schedule, (c) minus the Generating Unit's capacity committed to provide Ancillary Services to the ISO either through the ISO's Ancillary Services market or through self provision by a Scheduling Coordinator, and (d) minus the capacity of the Generating Unit scheduled to deliver Energy to the Must-Offer Generator's Native Load.

The ISO also commits to add the following definition of "Native Load" to Appendix A to the ISO Tariff: "Load required to be served by a vertically integrated utility within its Service Area pursuant to applicable law, franchise, or statute."

In addition to these changes, however, some parties request revisions to the definition of "Available Generation" that are not justified. For example, some parties suggest that Must-Offer Generators should not be required to submit real-time Energy bids for Generating Units that have available capacity but which are subject to daily and annual emissions limits. *See, e.g.*, NCPA at 8-9. The ISO has already agreed to modify the definition of "Available Generation" to ensure that no unit will be required to operate in violation of applicable law. In the April

26 Order, however, the Commission determined that it “will not exempt gas-fired resources from the must-offer obligation, simply because they may have environmental limitations.” April 26 Order, 95 FERC at 61,357. Moreover, the ISO believes that issues related to air emissions credits are economic issues. Local air quality districts in California have provided generators with the opportunity to purchase additional air emissions credits and all indications are that such opportunities will continue to be available.²⁶ Thus, entities such as NCPA are at no risk of exhausting resources that are intended to serve native load customers. At worst, such entities may incur additional costs in order to obtain additional air emissions credits or pay mitigation costs. Under the April 26 Order, as implemented in the May 11 Compliance Filing, such additional costs can be included in the bids for real-time Energy which must be submitted for all Available Generation, and may be subject to cost-justification.

Reliant suggests that the definition of “Available Generation” fails to clearly exclude a seller’s bilateral contractual obligations, as required by the April 26 Order. Reliant at 5-6. However, as Reliant itself concedes, the proposed definition does take into account bilateral transactions to the extent such transactions are identified in a unit’s Final Hour-Ahead schedule. The Commission has recognized on numerous occasions the need for all bilateral transactions to be forward scheduled with the ISO.²⁷ The proposed definition of

²⁶ See the discussion of NOx emissions issues in the ISO’s May 25 Request for Rehearing of the April 26 Order at pp. 51-55.

²⁷ See, e.g., *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 62,002 (2000).

Available Generation therefore allows Must-Offer Generators the ability to fully protect bilateral transactions provided that Must-Offer Generators satisfy their scheduling obligations.

Calpine raises issues related to the Commission's May 16 QF Order – which requires QFs to determine the amount of “excess QF power” that will be available for third party sales. Calpine claims that, until the issue of what constitutes “excess QF power available from each QF is resolved,” none of the capacity of *any* QF should be considered “Available Generation” for purposes of compliance with the April 26 Order. Calpine at 7-8. Although the ISO is not the appropriate entity to determine what constitutes “excess QF power” for any given Qualifying Facility, the ISO believes that the May 16 QF Order makes it quite clear that the Commission expects QFs to sell such excess QF power into the California wholesale markets as soon as possible. Indeed, the May 16 QF Order is “designed to ensure that the maximum amount of QF power will be available to the California market this summer.” May 16 QF Order, slip op. at 2. The May 16 QF Order provides that “[s]ales of QF power made pursuant to this order may be made either pursuant to bilateral contracts at negotiated rates, *or into the Cal ISO's real-time market*” and provides that “QFs that choose the real-time market will be required to be price takers and accept the market clearing price.” *Id.*, slip op. at 11, n.14 (emphasis added). Exempting the excess QF power of all QFs from the definition of “Available Generation” would therefore be completely inconsistent with the goals of the May 16 QF Order.

A number of entities raise issues about the definition of a Generating Unit's "maximum operating level" as used in the proposed definition of "Available Generation." Two parties suggest that, for Participating Generators, the ISO should use a unit's "normal maximum operating limit," as set forth in Schedule 1 of the PGA to determine a unit's "Available Generation" SMUD at 13-16, Reliant at 6. The ISO instead intends to use the Pmax data for each Generating Unit contained in the ISO's Master File as the basis for each Generating Unit's "maximum operating level." This data is based on objective testing and certification of a Generating Unit's performance capabilities, and is therefore more accurate than the limits specified in Schedule 1 of the PGA, which are not based on any objective testing criteria. In practice, the ISO expects that the Pmax data will generally be consistent with a unit's "normal maximum operating limit," as set forth in Schedule 1 of the PGA. To the extent any Must-Offer Generator believes that the data in the Master File is inaccurate or out-of-date, that Generator can advise the ISO of any temporary limitations that apply due to ambient conditions or an equipment outage or de-rate, or request re-certification of the Master File data through their ISO Client Representative.

In addition, in order to be able to accurately monitor compliance with the Commission's must-offer requirement, the ISO believes that it is imperative that each Generating Unit subject to the requirement update the ISO on a timely basis regarding any change in unit performance or availability. The ISO notes that efforts are currently underway, including the redesign of the ISO's Scheduling Logging for the ISO of California ("SLIC") system, which will allow

Generation owners to provide the ISO with more timely information about Unit outages and similar information. Moreover, to the extent that the ISO attempts to Dispatch a unit beyond its physical capabilities due to a change in a unit's operating capabilities or a change in dynamic system conditions, the ISO's current Dispatch procedures permit the Generation owner to inform the ISO why a unit is unable to be dispatched.²⁸ Generating Unit status, availability and performance information submitted to the ISO via the Outage Coordination Office or SLIC will ensure a formal record regarding such matters, a record that will assist in determining ultimate compliance with the Commission's must-offer requirement.

Some parties express concern that the ISO's definition of "Available Generation" will not take into account generation that is unavailable due to the dynamic impact of ambient conditions (such as air temperature) on certain Generating Units. IEP at 6-8, Calpine at 10-11. As noted above, the ISO intends to determine the level of Available Generation as adjusted for any outages reported to the ISO and capacity scheduled with the ISO. As noted above, these concerns can be addressed by providing the ISO with the most up-to-date information on the status of its Generating Units.

Dynergy expresses concerns about the definition of "Available Generation" as applied to units with extremely long start-up times. Dynergy at 8. The April 26

²⁸ Under Section 5.6.3.2, Participating Generators are subject to penalties for failure to comply with ISO dispatch instructions during System Emergency conditions, but will not be subject to such penalties if it provides the ISO with information demonstrating that the applicable Unit was physically incapable of complying with the ISO's instruction.

Order does not exempt Generating Units from the must-offer requirement based on their start-up times. As such, there is no justification for the ISO's compliance filing to make exceptions for units with long start-up times. The ISO expects – and believes that the Commission intended – that all units to which the must-offer requirement applies will maximize their availability to the ISO during all hours and will promptly notify the ISO if they are not available. The must-offer obligation imposed by the April 26 Order is meaningless otherwise. To the extent that the ISO dispatches these units and determines they are unavailable, the units may be subject to compliance penalties. Of course, when considering the application of penalties for failure to follow an ISO Dispatch instruction the ISO, and ultimately the Commission, must determine whether such unit provided timely and accurate information to the ISO (either via the Outage Coordination Office or SLIC). Such units will not be considered to have Available Generation to the extent they are on legitimate outages. In addition, the ISO notes that Must-Offer Generators have a number of opportunities to recover the costs associated with operating such units to satisfy the obligation to offer Available Generation in real-time. For example, if such units are selected to provide Replacement Reserves, Must-Offer Generators would be guaranteed a capacity payment for such units. Moreover, Must-offer Generators can factor ongoing operating costs into the bids they submit to the ISO and can use as justification for those bids the fact that they incurred certain costs as a result of making themselves available to the ISO for Dispatch at all times.

3. Use of Standing Bids

Duke objects to the ISO's proposal to utilize standing bids for a Must-Offer Generator's Available Generation if that Must-Offer Generator fails to submit a bid in compliance with the April 26 Order. Duke at 14. This objection is unfounded. The Commission has already approved the ISO's proposal to use standing \$0/MWh bids for some Must-Offer Generators in its May 25 Order, stating "the ISO's approach will provide such entities with an incentive to provide the ISO and the Commission with [requested] data." May 25 Order, slip op. at 4. Proposed Section 5.11.5 provides similar incentives for Must-Offer Generators to comply with the April 26 Order. Indeed, Duke offers no explanation of why Must-Offer Generators would be unable to avoid the use of standing bids by simply submitting bids for all of their Available Generation.

Dynergy argues that the ISO should use the calculated Proxy Price rather than a \$0/MWh bid as the standing bid for those Must-Offer Generators that fail to submit bids for Available Generation. Dynergy at 5. This comment is apparently based on a misreading of the ISO's May 11 Compliance Filing because that is exactly what the ISO has proposed to do. Specifically, Section 5.11.5 provides that the ISO will use the calculated Proxy Price as the standing bid for all gas-fired Generating Units with available generation that are not separately bid into the ISO's real-time Energy market. The ISO will only use a \$0/MWh "price taker" bid as the standing bid for those Generating Units that are not gas-fired or for which the ISO does not have adequate information to calculate the Proxy Price.

As explained in a recent notice to Market Participants, the ISO is not currently inserting price-taker bids for capacity from Generating Units for which the ISO has no visibility.²⁹ The ISO is considering options to verify the compliance of such units with the April 26 Order's must-offer requirement and may raise this issue in a future filing to the Commission.

4. Credit Support Issues

Vernon argues that the obligation of publicly-owned entities to comply with the April 26 Order's must-offer requirement should be conditioned upon ISO assurances of creditworthy buyers to pay for Energy dispatched pursuant to the must-offer requirement. Vernon at 10. The Commission addressed this issue in its May 25 Order in response to a motion for clarification in this proceeding filed by the Cities of Anaheim, Azusa, Banning, Colton, and Riverside, California. May 25 Order, slip op. at 6. To the extent the ISO intends to address this issue further, it will do so through either a motion for clarification or request for rehearing of the May 25 Order.

5. Obligation to Offer Available Generation

Only one party raises an issue with respect to proposed Section 5.11.4. Duke states that the ISO Tariff does not include a definition for an "Imbalance Energy market" and argues that proposed Section 5.11.4 should be modified as follows:

All Must-Offer Generators shall offer to sell in the ISO's Real Time Market for Imbalance Energy market, in all hours, all their Available Generation as defined in Section 5.11.2.

²⁹ See the ISO's Supplemental Market Notice of June 5, 2001, provided as Attachment B to this Answer.

Duke at 14. The ISO has no objection to this change and agrees to make it in a subsequent compliance filing to be submitted in this proceeding.

C. Price Mitigation

In the April 26 Order, the Commission adopted a price mitigation plan under which:

each gas-fired generator in California (both those signing PGAs and covered non-public utility gas-fired generators) will file with the Commission and the ISO (on a confidential basis) the heat rate and emission rate for each generating unit. These heat rates must reflect operational heat rates that do not include start-up and minimum load fuel costs because, in a declared emergency, the market clearing price should reflect the cost to generate at or near maximum outputs. The ISO will use these heat rates to calculate a marginal cost for each generator [the generator's "Proxy Price"] by using a proxy for the gas costs, emission cost, and a \$2.00 adder for operation and maintenance expenses.

April 26 Order, 95 FERC at 61,358-59. These Proxy Prices will form the basis for the April 26 Order's price mitigation plan, which is to apply only in the ISO's real-time market and during "emergency situations beginning at Stage I (*i.e.*, when reserves are 7.5 percent or less)." *Id.* at 61,358. During such conditions, bids for Energy from gas-fired Generating Units may be submitted at their Proxy Price, and "[a]ll generators who elect the proxy will be paid a single market clearing price reflecting the highest priced unit dispatched calculated using the proxy prices." *Id.* at 61,359. Bids for Energy from gas-fired Generating Units that are above the Proxy Price and are accepted by the ISO will be paid as-bid but are subject to refund if the Commission determines that a bid is not cost-justified, following its review of reports that such generators must submit to the Commission and the ISO. During System Emergencies, Energy from Generating

Units that are not gas-fired units and all other resources may be bid into the ISO's markets to be dispatched at the Market Clearing Price determined by the ISO in accordance with this mitigation scheme (the "Marginal Proxy Clearing Price" in the proposed Tariff language). Such other resources may also bid Energy above that Market Clearing Price, subject to cost justification before the Commission and refund liability.

1. When is Price Mitigation in Effect

The ISO's May 11 Compliance Filing proposed Tariff language which provides that the April 26 Order's price mitigation scheme shall be in effect "during System Emergencies." A number of parties argue that price mitigation should only apply during periods when the reserves available to the ISO are "7.5 percent or less" and claim that the ISO is attempting to broaden the scope of price mitigation in its compliance filing. Reliant at 3-4, Duke at 15-16, SRP at 7-8. These comments ignore both the language of the April 26 Order and the operational requirements under which the ISO operates.

In the overview of the April 26 Order, the Commission states that "The mitigation plan adopted here . . . will establish price mitigation for available capacity in real time when there is a reserve *deficiency during emergency stages beginning with stage 1.*" April 26 Order, 95 FERC at 61,351 (emphasis added). In the body of the Order, the Commission again explains that the mitigation measures will apply during all System emergencies, beginning with Stage 1 System Emergencies: "the Commission will require price mitigation for all generators in California, including non-public utility generators, with available

capacity during periods of reserve deficiency, defined as emergency situations beginning at stage 1 (*i.e.*, when reserves are 7.5 percent or less).” *Id.* at 61,358. In one other place in the April 26 Order, the Commission states that “it will make price mitigation applicable to all conditions defined by the ISO as beginning when reserves fall below 7.5%.” *Id.* at 61,361.

The April 26 Order apparently treats System Emergencies (beginning with Stage I emergencies) as synonymous with conditions where reserves fall below 7.5 percent. It is unclear why the Commission uses the 7.5 percent figure. As explained in the ISO’s May 25 Request for Rehearing of the April 26 Order, the WSCC requires that the ISO (and all other transmission providers in the WSCC) maintain Spinning Reserves and Non-Spinning Reserves equal to the greater of: (1) the loss of generating capacity due to forced outages of generation or transmission equipment that would result from the most severe single contingency, or (2) the sum of five percent of the load responsibility served by hydro generation and seven percent of the load responsibility served by thermal generation. WSCC Rate Schedule No. 1, First Revised Sheet No. 27. In the case of the ISO it is the latter 5 percent and 7 percent reserve responsibility which is most often applicable. Thus, there are circumstances where the ISO has less than 7.5 percent Operating Reserves available, but the prerequisites for declaring a Stage 1 System Emergency – an Operating Reserve shortfall that exists or is unavoidable – have not yet been satisfied.

Nonetheless, the operative language of the April 26 Order focuses on “emergency stages beginning with stage 1” and not on the 7.5 percent figure.

The ISO's May 11 Compliance Filing is therefore fully consistent with this aspect of the order.

Some parties argue that application of price mitigation during ISO-declared System Emergencies will allow the ISO to abuse its discretion to declare System Emergencies. The Commission explicitly considered and rejected such arguments in the April 26 Order:

Generators further suggest that the ISO will have an incentive to declare emergency conditions to invoke mitigated prices, rather than because supply and demand conditions dictate. The WSSC establishes standards for reserve requirements, as well as reporting requirements, and the ISO must observe those standards in declaring emergencies. The Commission also is requiring the ISO to file weekly reports with the Commission, so that the Commission will have information available to review the ISO's actions.

April 26 Order, 95 FERC at 61,362. This discussion makes it clear that the Commission intended "mitigated prices" to apply when the ISO "declare[s] emergency conditions." There is no basis in the April 26 Order to contend that price mitigation should not apply during all System Emergencies.

Conversely, PG&E asserts that applicability of price mitigation only during System Emergencies could lead to the anomalous result of producing lower total costs during emergency hours than during non-emergency hours. PG&E at 4. The ISO strongly agrees with this statement. As explained in detail in the ISO's May 25, 2001, Motion for Clarification and Request for Rehearing of the April 26 Order, price mitigation must apply in all hours and during all system conditions if California's wholesale electricity markets are to produce just and reasonable rates.

2. Establishment of the Market Clearing Price Through the Lesser of the Marginal Unit's Proxy Price or Actual Bid

In the May 11 Compliance Filing, the ISO noted that the April 26 Order provides little detailed guidance as to how the Market Clearing Price will be calculated during periods of price mitigation. The ISO explained that it will use the highest Proxy Price calculated for a gas-fired Generating Unit dispatched during a System Emergency to set the Market Clearing Price for that settlement interval, even if the bid for the Generating Unit in question is greater than that unit's Proxy Price. To the extent that the bid for the marginal unit selected by the ISO is less than that unit's Proxy Price, however, that unit's actual bid would set the Market Clearing Price. That is, for each settlement interval in which price mitigation applies, the ISO will both dispatch (*i.e.*, establish the merit order stack) and determine the Marginal Proxy Clearing Price based on the lesser of each gas-fired resources' actual bid or its applicable Proxy Price. This approach was reflected in the Tariff revisions submitted in the May 11 Compliance Filing.

Several parties object to the ISO's proposal to use the marginal unit's actual bid to set the Market Clearing Price if that unit is bid at below the applicable Proxy Price. Williams at 2-3, Dynegy at 3-4, Reliant at 4-5. These parties contend that the ISO's proposal is inconsistent with the April 26 Order and would allow the ISO to manipulate the merit order stack of real-time Energy bids (the "BEEP Stack") to result in lower prices.

These objections are difficult to fathom coming from parties that are such strong advocates of market-based approaches. In short, these parties are arguing that suppliers of electricity should not be *permitted* to submit bids to

supply Energy during Emergency conditions that are below a presumably cost-based proxy – or at least not bids that have any meaningful impact on the price paid for that Energy. These parties argue that the ISO will use a supplier’s actual bids to manipulate the BEEP stack, but do not explain how the acceptance of submitted Bids (as opposed to an administratively-determined Proxy Price) constitutes “manipulation.” Presumably, suppliers know whether the bid submitted for their units is sufficient to recover their operating costs. The only explanation for this position is that these parties only favor market-based outcomes when they result in *increased* prices for electricity, and not when such outcomes might mitigate Energy prices. Moreover, these parties’ positions raise concerns as to whether the Proxy Price methodology will result in an accurate or reasonable approximation to true operating costs.

If the California wholesale markets even approach truly competitive conditions, as the Commission has found in its grant of market-based rate authority, then there may be circumstances, even during System Emergencies, where a supplier may choose to bid below its Proxy Price. A supplier may choose to submit bids below a unit’s Proxy Price if that unit is a “marginal unit” that may or may not be called by the ISO and if the marginal costs of generating electricity from that unit are below the Proxy Price for that unit. For example, a gas-fired unit in northern California may have marginal costs of generating electricity that are lower than the calculated Proxy Price for that unit due to the fact that northern California natural gas prices are significantly lower than Southern California gas prices, but the Proxy Prices are based on an average of

gas prices from both regions. It would be completely inconsistent with the April 26 Order's intent to "achieve mitigation by emulating a competitive marketplace" to prevent such bids from establishing the Market Clearing Price if submitted for the marginal unit dispatched by the ISO.

The ISO also urges the Commission to take note of the comments of the CPUC on this issue. CPUC at 9-10 Using the Proxy Price of the marginal unit to set the Market Clearing Price, even when all accepted bids are below that price, would deprive purchasers of whatever efficiencies the market is providing and is inconsistent with the underlying premises of the market-based rate structure that the Commission seeks to advance in the April 26 Order.

For all these reasons, the ISO's proposal to use the marginal unit's actual bid to set the Market Clearing Price if that unit is bid at below the applicable Proxy Price must be accepted.

3. Calculation of the Proxy Price

In the ISO's May 11 Compliance Filing, it explained that it will calculate the Proxy Prices for gas-fired Generating Units using the following methodology: The ISO will use the provided average heat rate data to calculate an incremental heat rate step function for each gas-fired Generating Unit. To determine the Proxy Price at each operating level, the ISO will calculate the incremental heat rate cost

using a daily gas price index, add the applicable emission cost and a \$2.00 adder for operation and maintenance expenses.³⁰

Several parties take issue with the ISO's proposal to use a simple average of the Gas Daily midpoint index prices for Malin, PG&E Citygate, and SoCalGas large packages as the daily gas price index to be used in calculating the Proxy Price. Dynegy at 10-11, Reliant at 6-7, SMUD at 17-18. The Commission has addressed this issue in its May 25 Order, and the ISO is complying with that order. May 25 Order, slip op. at 4. To the extent the ISO intends to address this issue further it will do so through either a motion for clarification or request for rehearing of the May 25 Order.

One party contends that the ISO's use of heat rate curve to calculate the Proxy Price is inconsistent with the April 26 Order. Dynegy at 6-9. As the ISO explained in its May 11 Compliance Filing, use of average heat rate data to calculate an incremental heat rate step function for each gas-fired Generating Unit will result in the most accurate Proxy Price. The Commission endorsed such an approach in the May 25 Order, where it accepted the ISO's proposal to "use data from a viable alternative source (*e.g.*, either current or pre-existing Reliability Must-Run Contracts" for "the generating units that have not provided the requisite data or whose data the ISO believes to be inadequate (*the*

³⁰ As explained in the ISO's May 25 Status Report, based on the reply of the South Coast Air Quality Management District ("SCAQMD") to the Commission's May 9, 2001 request for additional information on nitrogen oxide (NOx) emission costs, the ISO is currently using a \$0.00 emissions rate for calculating the Proxy Price.

submitted data only covers one operating point).” May 25 Order, slip op. at 4 (emphasis added).

Mirant contends that the ISO should provide additional detail on the methodology for calculating the proxy price, arguing that, at a minimum, the ISO should publish an algorithm showing the points on the heat rate curve that will be used to develop its heat rate step function, and should provide an explanation of the method it will use to calculate the average daily gas price. Mirant at 2-3. The ISO has already done so. On May 24, 2001, the ISO issued a Market Notice concerning implementation of the April 26 Order that included an example of the Proxy Price calculation and the algorithm used by the ISO to calculate the Proxy Price. A copy of that Market Notice (the “May 24 Market Notice”) is provided as Attachment C to this Answer.³¹

Two parties object to the requirement in Section 2.5.23.3 of the proposed Tariff language that Must-Offer Generators provide periodic updates of heat and emissions rates used to calculate the Proxy Price upon the direction of either the Commission or the ISO. Mirant at 3, Dynegy at 9. They contend that Must-Offer Generators should be permitted to unilaterally file updates of heat and emissions rates, but that the ISO should only be permitted to request updates with the approval of the Commission. These objections are unfounded. There may be many circumstances where the ISO may appropriately request updates. For

³¹ The ISO notes that the May 24 Market Notice was issued prior to the Commission's issuance of the May 25 Order. To the extent the notice is inconsistent with the requirements of the May 25 Order, the ISO has modified its implementation to comply with the May 25 Order, as described in a Market Notice issued on May 26, 2001, provided as Attachment D to this Answer.

example, installation of new equipment at a Generating Unit, such as Selective Catalytic Reduction technology, could result in altered heat or emissions rates. In such circumstances, it would be burdensome to both the ISO and the Commission for the ISO to obtain Commission approval prior to seeking updated data from Must-Offer Generators. The ISO will only exercise its authority to request updates under Section 2.5.23.3 where the ISO has a reasonable expectation that a change in circumstances concerning the applicable Generating Units justifies such a request. The Commission should therefore approve Section 2.5.23.3 as proposed.

4. Confidentiality of Data

Several parties argue that the ISO should automatically treat all heat and emissions rates data provided to the ISO pursuant to the April 26 Order as confidential. Mirant at 3-4, Dynegy at 9, Duke at 16-17. In proposed Section 2.5.23.3, the ISO has committed to apply the confidentiality provisions of Section 20.3.4 of the ISO Tariff to such data upon request of the Must-Offer Generator. Such an approach is appropriate because much of this data is already public. As the Commission noted in its May 25 Order, May 25 Order, slip op. at 4, much of this data is available in current or pre-existing Reliability Must-Run Contracts. These contracts are publicly filed with the Commission and are not subject to any form of confidentiality protection. In light of this fact, the ISO believes it is wholly appropriate for the Must-Offer Generators to inform the ISO of what data they wish to be treated as confidential. The proposed burden to obtain confidential

treatment of such data – nothing more than a request to the ISO – is minimal. The Commission should approve this provision as proposed.

Duke requests that proposed Section 2.5.23.3.5 be modified to provide for the confidentiality of cost justification data submitted to the ISO and to the Commission. Duke at 19. Although the ISO does not agree with the specific language proposed by Duke, the ISO does agree that data submitted to justify individual bids may include data which is rightfully subject to confidentiality protection. Accordingly, the ISO commits to modify Section 2.5.23.3.5 in a subsequent compliance filing to be submitted in this proceeding as follows:

2.5.23.3.5 Requirement to Justify Bids Above the Proxy Price

The following entities shall be required to provide cost justification for Supplemental Energy bids submitted to the ISO:

- (a) Scheduling Coordinators for gas-fired Generating Units owned or controlled by Must-Offer Generators that submit bids for the supply of Imbalance Energy during System Emergencies above the Proxy Price for those Generating Units; and
- (b) Scheduling Coordinators for all other Generating Units, System Units, and System Resources that submit bids for the supply of Imbalance Energy during System Emergencies above the Marginal Proxy Clearing Price determined in accordance with Section 2.5.23.3.1.

Scheduling Coordinators subject to the cost justification requirement shall provide such justification in writing to the ISO and the FERC by no later than seven (7) calendar days after the end of the month in which the bid was submitted. The cost justification for bids submitted on behalf of Must-Offer Generators and other Generating Units and System Units shall include a detailed breakdown of the component costs associated with such bids. The cost justification for bids submitted on behalf of non-Scheduling Coordinator Market Participants shall include a detailed breakdown of the prices paid by that non-Scheduling Coordinator Market

Participants for the Energy bid. Cost justifications provided pursuant to this Section 2.5.23.3.5 shall not include components representing scarcity rents or opportunity costs. If requested by a Scheduling Coordinator, the ISO will treat the cost justifications provided to the ISO in accordance with this Section 2.5.23.3.5 as confidential and will apply the procedures in section 20.3.4 of ISO Tariff with regard to requests for disclosure of such information. Amounts collected by Scheduling Coordinators subject to the cost justification requirement in excess of the Proxy Price or Marginal Proxy Clearing Price, as applicable, shall be subject to refund, as may be ordered by the FERC.

5. Cost Justification and Refund Liability

Duke argues that the Commission should require the ISO to modify proposed Section 2.5.23.3.5 to require cost justification only in cases where bids above the Proxy Price or Market Clearing Price are accepted. Duke at 18. This argument is inconsistent with the April 26 Order, which provides:

At the end of each month in which a generator submits a bid higher than the market clearing price, the generator must file with the Commission and the ISO, within seven days of the end of the month, its complete justification, including a detailed breakdown of all of its component costs, for each transaction exceeding the market clearing price established by the proxy bid. This justification must be based on a showing of actual marginal costs higher than the market-clearing price.

April 26 Order, 95 FERC at 61,359. The obligation to submit cost justification is incurred when a generator submits a bid above the Proxy Price-based Market Clearing Price, and is not contingent upon the ISO's acceptance of such a bid. As such, there is no justification for the modification requested by Duke. In addition, the ISO notes that cost justification for all bids above a gas-fired unit's Proxy Price or above the Market Clearing Price for other units is necessary if the Commission and the ISO are to monitor compliance with the April 26 Order's prohibition on anti-competitive bidding.

Duke requests additional edits to the ISO's proposed Tariff language to delineate those bids that are not subject to cost justification and refund under the April 26 Order. The ISO believes Section 2.5.23.3.5 clearly identifies those bids that are subject to cost justification and refund under the April 26 Order. Moreover, the April 26 Order speaks for itself on this issue. The Commission will be well aware of the provisions of that Order, as it may be modified on rehearing, when it determines whether refunds are justified. The modifications proposed by Duke would therefore be superfluous.

6. Mitigation of Ancillary Services and Congestion Management Markets

SCE and SDG&E vehemently oppose the aspects of the ISO's May 11 Compliance Filing which state that the ISO believes the April 26 Order removed all price mitigation in the Ancillary Service and Congestion Management markets and urge the Commission to reject these aspects of the compliance filing. SCE at 3-6, SDG&E at 2-3. Dynegy also recognizes the propriety of addressing price mitigation in these markets. Dynegy at 13-14. The Commission addressed these concerns in its May 25 Order, where it held that the April 26 Order did not remove all price mitigation in those markets. Instead, the Commission provided clarification that "the April 26 Order did not replace the ISO's current methodology for mitigating Adjustment Bid prices"³² and directed the ISO "to use each relevant average hourly mitigated Imbalance Energy price" as the basis for Ancillary Services price mitigation. May 25 Order, slip op. at 5.

³² The ISO's current methodology for mitigating Adjustment Bid prices is a \$250 "hard cap" on Adjustment Bids.

The ISO strongly supports the Commission's recognition of the need for price mitigation in the ISO's Ancillary Service and Congestion Management markets. Consistent with the May 25 Order, the ISO hereby withdraws the proposed revisions to Section 5.27.7 submitted in the May 11 Compliance Filing. In the near future, the ISO intends to submit additional revisions to Section 2.5.27.7 to implement the May 25 Order.

As noted earlier in this pleading, the ISO continues to believe that price mitigation should apply in all hours. Therefore, although the ISO strongly agrees with the Commission's determination in the May 25 Order to continue price mitigation in the ISO's Ancillary Service market, the ISO believes that such mitigation should apply in all hours. To the extent the ISO intends to further address the May 25 Order's mitigation measures for the Ancillary Service and Congestion Management markets, it will do so through either a motion for clarification or request for rehearing of the May 25 Order.

7. Conditions on Anti-Competitive Bidding Behavior

PG&E argues that the ISO should add Tariff language incorporating the examples of prohibited anti-competitive bidding behavior listed in the April 26 Order to proposed Section 2.5.23 and that the ISO should propose corresponding changes to its Market Monitoring and Information Protocol. PG&E at 4-5. The ISO fully supports the April 26 Order's: (1) conditioning of market-based rate authority upon the bidding behavior of Market Participants and (2) specifically prohibiting anti-competitive bidding behavior. The ISO intends to actively monitor bids in a comprehensive program to detect not only the

examples cited by the Commission, but other coordinated bidding practices that appear to be directed at manipulating market prices. The ISO believes that no purpose would be served by incorporating the examples of anti-competitive bidding behavior discussed in then April 26 Order to the ISO Tariff. In addition, the ISO believes that the provisions of the MMIP are already sufficiently broad to allow the ISO to address such bidding behavior.

8. Publication of ISO Market Prices

Dynegy claims that parties do not have information about clearing prices in the ISO's markets until 45 days after the market closes, when the ISO issues Preliminary Settlement Statements. Dynegy at 6. Dynegy requests that the ISO be directed to release settlement information within 3 days of closing on price mitigated days so that suppliers can determine whether to elect to bid at the proxy price and when they must justify bids above the Proxy Price. Dynegy's comments are based on a false premise. ISO Market Clearing Prices are available on a same-day basis on the ISO's web site at: <http://www.caiso.com/marketops/OASIS/pubmkt2.html>. This information is more than sufficient to enable Market Participants to comply with the reporting and cost-justification requirements of the April 26 Order. There is certainly no justification for the extreme shortening of the ISO's settlement schedule proposed by Dynegy. Moreover, such changes to the ISO's settlement schedule would require the institution of a complaint proceeding under Section 206 of the Federal Power Act.

D. Sunset of Price Mitigation and the Must-Offer Requirement

Several parties suggest that the ISO's May 11 Compliance Filing should be modified to reflect the Commission's statement in the April 26 Order that the price mitigation measures and must-sell requirements will expire in one year. Mirant at 4, Reliant at 7-8, SMUD at 18. There is no reason for such a limitation to be included in the ISO Tariff. Numerous parties, including the ISO, have sought rehearing of the April 26 Order's imposition of a sunset date for price mitigation measures. See May 25 Rehearing Request at 84-86. There is no evidence that the California wholesale electric markets will produce just and reasonable prices in one year without appropriate mitigation measures. In the absence of such evidence, a sunset of price mitigation is contrary to the Commission's statutory obligations under the Federal Power Act. The ISO believes that the Commission must therefore issue an order on rehearing eliminating the sunset of price mitigation in the California wholesale markets.

Even if the Commission were not to modify this aspect of the April 26 Order, there is no need for the sunset date to be hard-wired into the ISO Tariff at this time. The Tariff revisions needed to eliminate the April 26 Order's price mitigation measures and must-sell requirements could instead be filed next year, if appropriate. Such an approach is appropriate because it will allow the Commission the opportunity to consider the need for price mitigation in the California wholesale electric markets in mid-2002, when the current price mitigation and must-offer requirements would expire under the April 26 Order.

E. Miscellaneous Issues

A number of parties raise issues that go beyond the scope of the ISO's May 11 Compliance Filing. For example, some parties comment on the Demand Response element of the April 26 Order. Reliant at 2, Duke at 19, Dynegy at 2-3. The April 26 Order did not require the ISO to address Demand Response issues in the compliance filing to be submitted by May 11. Instead, the order requires filings addressing Demand Response from the ISO and "public utility load serving entities" by June 1, 2001. On that date, the ISO submitted a filing in the above-captioned proceeding to comply with Demand Response aspects of the April 26 Order.³³ Thus, any comments concerning the ISO's compliance with the Demand Response aspects of the April 26 Order submitted prior to June 1 are premature and should not be considered in the context of the ISO's May 11 Compliance Filing.

Dynegy argues that the ISO's retention of penalties for generators that do not comply with ISO Dispatch instructions during System Emergency conditions is inconsistent with the April 26 Order's discussion that suppliers may not bid generation in forward markets to hedge against the risk that one of their units might trip off-line. Dynegy at 11-12. This comment has nothing to do with the April 26 Order. Instead, it is but the latest attempt of Dynegy to complain of penalties approved by the Commission in Amendment No. 33 to the ISO Tariff. These penalties apply only to those generators that fail to fulfill their legal

³³ The ISO also addressed the Demand Response aspects of the April 26 Order in its May 25 Rehearing Request at 66-76.

obligations under their Participating Generator agreements and the ISO Tariff. Nothing in the April 26 Order addresses those penalty provisions. Moreover, Dynegy is incorrect in claiming that the must-offer provisions of the April 26 Order will place generators at greater risk of such penalties. Generators have always been subject to these penalties not only for failure to provide Energy bid into the ISO's markets, but also for Energy which the ISO has dispatched from a generator's "available generation" pursuant to the ISO's emergency dispatch authority.

Lastly, WPTF argues that the ISO's current governance structure is a "roadblock" to implementation of the April 26 Order. WPTF at 10. WPTF's argument is nothing but rhetoric. WPTF does not even explain how it believes that implementation of the April 26 Order will be affected by the current structure of the ISO's Governing Board. This argument should accordingly be disregarded.³⁴

³⁴ On April 26, 2001, the ISO filed revised bylaws with the Commission reflecting the current structure of the ISO Governing Board under California State law. Any comments concerning the ISO's governance structure should be addressed in response to that filing.

III. CONCLUSION

For the foregoing reasons, the Commission should accept the ISO's May 11 Compliance Filing in this proceeding with only such modifications as are described above.

Respectfully submitted,

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Dated: June 6, 2001

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Washington, DC, this 6th day of June, 2001.

Sean A. Atkins

June 6, 2001

The Honorable David P. Boergers
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, DC 20426

**Re: 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
Docket Nos. EL00-95-000, *et al.***

Dear Secretary Boergers:

Enclosed please find an original and fourteen copies of the Answer of the California Independent System Operator Corporation to Motions to Intervene, Comments, Motion for Leave to File Comments Out of Time, Motion to Reject, and Protests in the above-captioned proceeding. Also enclosed are two extra copies of the filing to be date-stamped and returned to us by the messenger. Thank you for your assistance.

Respectfully submitted,

Sean A. Atkins

Counsel for the California
Independent System Operator Corporation