

Comments of Calpine Corporation on

April 27, 2011

*Impact of Convergence Bidding on
Real-Time Imbalance Energy Offset
Issue Paper and Straw Proposal*

Summary:

Calpine does not object to the CAISO proposal, as it continues to allow locational arbitrage and legitimate hedging opportunities for physical imports. We do however, recommend that the offset resettlement have a time-certain sunset date of 12 months from FERC initial acceptance.

We wish to specifically thank Don Tretheway for his patience and informative, yet open effort to educate us on the effects of the CASIO proposal.

The Structural Issues Must be Resolved

Calpine agrees with the CAISO that the end-game vision should be that HASP and RT prices vary based on fundamental changes in system conditions, and not based on structural limitations. In this end-state, any differences in price should be unbiased, and volatility would be reflective of the magnitude of market changes.

The CAISO has been pursuing changes to modeling software (e.g. load forecasts) and operator actions (biasing) in order to address any systematic price drivers. These price drivers appear to have resulted – both during and before implementation of convergence bidding – in a bias in which HASP prices were below RT prices. Indeed, addressing these structural issues has been a large focus of both the CAISO staff and DMM.

As a physical importer, Calpine seeks solutions to the energy offset concerns of the LSEs while continuing to allow legitimate hedging for the physical positions it takes at the interties.

What is Driving the Recent Flips?

The data presented in the Straw Proposal by the CAISO runs from January 2010 through March 2011. The CAISO's conclusion from the data is that “[s]ince September 2010 the offset has trended higher.”

However, this observation should be complemented by three other observations:

1. The March 2011 data represents a 30 percent decline from that of February 2011
2. On the teleconference, the CAISO indicated that the most recent data appeared to be adding a credit, rather than a liability to the energy offset
3. The energy offset amounts for June and July were higher than any period after implementation of Convergence Bidding *in spite of the fact* that the bid cap was 25 percent lower than it is now (\$750 compared to \$1000.)

These observations can not be ignored. Indeed, have the CAISO's actions to address structural issues been successful? Have bidders, seeing a persistent market condition begun taking complementary virtual positions? What is the cause of the reversal? Is it durable? Calpine seeks solutions that will continue to encourage the CAISO to evaluate price spreads and take appropriate action.

Calpine Does Not Oppose the CAISO's Proposal

After several discussions with staff, particularly Don Tretheway, Calpine understands the motivations of the CAISO and the relative elegance of the CAISO's proposal. We are convinced that locational spreads can still be arbitrated and that physical imports can be hedged without undue inference from the CAISO's proposal. As such, we do not oppose it.

Nonetheless, The CAISO Should Commit to a Sunset

Nonetheless, we believe that the CAISO should continue to evaluate and focus on solutions to the structural problems driving the HASP-to-RT spread. As such, we propose that the resettlement proposal contain a sunset of 12 months. At the end of the 9 months, the CAISO should prepare a report to file at FERC reporting the actual spreads and documenting its efforts to reduce the spread. Absent a specific *de novo* request and approval of extension, the resettlement mechanism will terminate 12 months after initial approval by FERC.

Thank you
Submitted May 11, 2011