Stakeholder Comments Template

Subject: Capacity Procurement Mechanism, and Compensation and Bid Mitigation for Exceptional Dispatch

Submitted by	Company	Date Submitted
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This template was created to help stakeholders structure their written comments on topics related to the July 15, 2010 Straw Proposal for Capacity Procurement Mechanism ("CPM"), and Compensation and Bid Mitigation for Exceptional Dispatch. Please submit comments (in MS Word) to bmcallister@caiso.com no later than the close of business on July 30, 2010.

Please add your comments where indicated responding to the topic or question raised. Your comments on any aspect of the straw proposal are welcome. The comments received will assist the ISO with the development of the Draft Final Proposal.

Please provide your comments on the following topics and questions. Your comments will be most useful if you provide the reasons and the business case for your preferred approaches to these topics.

CPM

1. The appropriate duration of the tariff provisions associated with the CPM: should they be permanent or terminate on a certain date or under certain conditions? If the CPM should terminate, please be specific about the date or conditions upon which it would terminate and indicate the reasons for your proposal.

   The CPM provisions could be permanent if the CAISO re-evaluated the CPM, in particular the pricing terms, through a stakeholder process on a regular (e.g., two-year) basis. This would provide an opportunity for transparent review. Additionally, the CAISO should be required to re-file the pricing terms every two years. This will help ensure that the CPM price remains reasonable.

2. The appropriate treatment of resources that may be procured through CPM or Exceptional Dispatch but then go out on Planned Outage during the period for

which the resource has been procured. What are your views on the proposed formula in the straw proposal for compensating such resources?

Where a planned outage would reduce the duration of a 30-day CPM designation, Dynegy would prefer the resource owner to have the option to shorten the CPM term or to provide substitute capacity. Automatically shortening the CPM term for a period less than the FERC-approved 30 days could encourage the selection of a resource that will be going on a planned outage.

3. Modification of the criteria for choosing a resource to procure under CPM (section 43.3) to provide the ISO with the ability to procure non-use limited capacity over use-limited capacity.

   Dynegy supports adding criteria that would allow the CAISO to procure non-use-limited capacity over use-limited capacity. Such criteria, and their application, should be transparent.

4. The three new types of procurement authority for generic backstop capacity the ISO is proposing.

   Dynegy strongly supports using CPM to procure capacity needed to support planned maintenance. It is grossly inequitable to utilize Exceptional Dispatch for non-RA resources to support the transmission maintenance programs of entities that did not provide the generating resources needed to support maintenance of their transmission systems with capacity contracts. Further, Dynegy supports any and all efforts to reduce the amount of Exceptional Dispatch.

   Dynegy also supports using CPM to backstop less-than-expected output from intermittent resources. However, to the extent this is a problem, it is a problem because the RA counting rules continue to exaggerate the dependable capacity values of intermittent resources. The CAISO must not simply propose to use CPM to backstop inadequate RA counting rules; it must also take aggressive action to fix the counting rules.

   Dynegy questions the use of CPM to prevent resources needed for reliability from shutting down. The entire premise underlying this proposal seems flawed; if a resource is needed for reliability, why isn't it under an RA or RMR contract that provide sufficient revenues to ensure continued operation? Given that generating units cannot be moved or staffed for only parts of the year, and incur fixed costs year-round, short-term CPM designations should not be used as a short-term fix as a substitute for longer-term capacity contracts. Moreover, the CAISO should fundamentally re-examine its markets to see why resources needed for reliability are not receiving sufficient revenues.

5. The compensation that should be paid for generic capacity procured under CPM and Exceptional Dispatch. Which method do you support: Option A – CONE net

of peak energy rent; or Option B – going forward costs? Are there further modifications needed to either of these pricing options? If you have a specific alternative pricing proposal, please provide it and indicate the reasons for your proposal.

Dynegy supports Option (A) – a sloped demand curve with a ceiling of CONE and a floor of going forward costs. It is appropriate to price CPM capacity near net CONE in areas that are deficient. It is also appropriate to have a floor price to ensure that capacity does not become valueless. (The fact that the CAISO needs such capacity to maintain reliability, even if it is "generic" capacity, is a de facto indication that the capacity is not valueless.)

While Dynegy supports a sloped demand curve for CPM pricing, Dynegy acknowledges that designing the energy and ancillary service net revenue deduction is likely to be a very complex and contentious matter. One benefit of an administrative price with no such net revenue deduction is that it avoids the need to design such a deduction. That said, Dynegy would prefer that the CPM price provide appropriate compensation and meaningful price signals.

If the minimum term for a CPM designation remains at 30 days, it is not at all apparent how even a price approaching net CONE – should such a price be realized – would interfere with RA contracting. The fear that rational suppliers would turn down the certainty of a multi-month or multi-year RA contract for the uncertainty of a CPM designation is not only doubtful, but is unimaginable for a long term asset.

6. The need for the ISO to procure non-generic capacity under CPM and Exceptional Dispatch to meet operational needs.

   Dynegy understands the looming operational challenges, the need to consider a resource's operational characteristics to meet those challenges, and the potential need to procure non-generic capacity through the CPM. Dynegy wants to ensure that the process and criteria the CAISO uses to procure non-generic capacity are transparent. Dynegy also wants to ensure that the CAISO appropriately values and compensates resources that provide those desired operational characteristics so those costs can serve as meaningful signals for the value of such characteristics.

7. The operational criteria the ISO is proposing to distinguish certain operational characteristics as non-generic capacity (fast ramping and load following). Are these two characteristics enough, or do you propose additional criteria for operating characteristics that would qualify for non-generic capacity?

   At this time, the CAISO should not limit the types of operational characteristics that it should consider to distinguish non-generic capacity. Others (e.g., voltage support and inertia) may and should also be considered. With the results of the *renewable integration studies not yet public, it is too early to assume this process has compiled a comprehensive list of operational characteristics that should be considered in this stakeholder process.*

8. How should non-generic capacity be compensated? What are your views on the proposal to compensate non-generic capacity by applying an adder to the price paid for generic capacity?

   In theory, the attributes for non-generic capacity should be compensated through markets for those specific attributes, so that the prices in those markets will serve as meaningful price signals for the value of such attributes. However, given the large volumes of capacity under control of buyers, and the corresponding amount of ancillary services self-provision and energy self-scheduling that takes place, there is no guarantee that the CAISO's market prices will provide such meaningful price signals. As a result, while it is not the ideal theoretical approach, Dynegy believes that it would be appropriate to provide an adder to the price of non-generic capacity to reflect the additional value of the operational characteristics associated with that capacity.

<u>Exceptional Dispatch</u>

1. Should energy bids for resources dispatched under Exceptional Dispatch continue to be mitigated under certain circumstances? Should such mitigation continue the current practices of bid mitigation as outlined in the straw proposal?

   Dynegy does not object to retaining the two current categories of mitigation of Exceptional Dispatch (non-competitive paths and Delta Dispatch). However, given Dynegy's recent experience, in which its energy bids were mitigated without reason, Dynegy is even more concerned with the CAISO's continued refusal to aggressively implement dynamic competitive path assessment. Even though the CAISO does not intend to include changes to the competitive path assessment as part of the CPM initiative, Dynegy urges the CAISO to implement dynamic competitive path assessment as soon as possible.

2. Should the ISO change the categories of bids subject to mitigation under Exceptional Dispatch (Targeted, Limited and FERC Approved) and extend the bid mitigation for the existing categories?

   No and yes.

3. What is the appropriate compensation for non-RA, non-RMR and non-CPM capacity that is Exceptionally Dispatched? Should the current compensation methodology be extended, updated to agree with what is put in place for CPM for generic capacity procurement?

The current requirement that Exceptionally Dispatched non-RA, non-RMR and non-CPM capacity be provided with a 30-day CPM designation should, at a minimum, be retained. Assuming that the minimum term or price of the CPM is not degraded in this stakeholder process, the CPM minimum term and price should be extended to designations resulting from Exceptional Dispatch.

<u>Other</u>

1. Do you have any additional comments that you would like to provide?

Dynegy appreciates that the CAISO is considering expanding the situations under which it would procure capacity (outages, inadequate performance of intermittent resources, to forestall retirement). While backstop procurement is not as ideal as reflecting the need for capacity through market prices, it is preferable to procuring such capacity services through Exceptional Dispatch.

The 30-day minimum term for CPM procurement still pales in comparison to the one-year term afforded units procured under RMR contracts, or to the multi-month RA season. The disparities between the terms of these reliability capacity procurement mechanisms continues to invite selective arbitrage between these procurement mechanisms to the detriment of the capacity suppliers, as short-term capacity procurement does not reflect the reality that costs are incurred on an annual basis. The CAISO's real, binding operational requirements should be reflected in RA requirements, which, in most, if not all, other venues are imposed for annual terms. To the extent they are not, CPM serves as a way to acquire needed reliability services on the cheap and for short minimum terms that do not reflect the fact that the units that provide these reliability services incur costs the year around. (This is also a shortcoming of the monthly RA process.)

Dynegy appreciates the opportunity to submit these comments.