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Gila River Power (Gila) appreciates the opportunity to make comments regarding the real-time imbalance energy offset charge. We believe that excessive real-time energy offset charges are a symptom of an inefficient market that does not minimize total procurement costs. As a strong proponent of competitive markets, Gila believes that only market forces and a robust market design can achieve the efficiency desired by CAISO, Gila, and other market participants.

The fundamental cause of the energy imbalance charges in question is CAISO's process of only financially binding some participants to HASP and others to RTD. All load and internal generation cannot participate in HASP to satisfy shortfalls or sell excess energy. The opposite scenario is occurring at the interties as they are unable to purchase or sell at the RTD price. Since the HASP solution takes into account all bids and known system conditions, the HASP price, in theory, should be very similar to the RTD price. However, since the inception of MRTU, these prices have been inconsistent.

Instead, HASP prices have been systematically lower for various reasons. Gila believes the independent settlement processes for HASP and RTD is a market design flaw. Since load is unable to bid in HASP it is not surprising that the price discrepancy persists. The logical solution is to allow load to bid in HASP and, reciprocally, to allow interties the ability to choose to be settled in RTD or HASP. The excerpt below from CAISO's 2010 Market Issues & Performance Annual Report (see page 68) provides insight into Gila's view of the root cause:

*“Divergence in prices can pose additional inefficiencies and costs on the system. When net imports decrease in the hour-ahead market, but real-time imbalance energy increases, the decrease in net imports may be inefficient.<sup>61</sup> Such reductions are inefficient if hour-ahead prices are systematically lower than real-time prices, so that the ISO is selling energy in the hour-ahead at a low price and then dispatching additional energy in real-time at a higher price.*

<sup>61</sup> *“The inter-tie prices are relative to prices in neighboring systems. If prices outside of the ISO system are higher, it makes economic sense for net imports to decrease in the hour-ahead market. This can be accomplished by either reducing imports or increasing exports.”*

CAISO proposes to mitigate real-time energy offset charges by implementing a change in its settlement rules. However, this solution does not address the underlying issues causing these charges. While CAISO's solution will redistribute costs and revenues among market participants, it will not produce market efficiencies. The proposed solution is likely to produce undesirable side effects which contribute to additional market inefficiencies.

For example, market participants will suppress their participation in convergence bidding to avoid inadvertently triggering the HASP-RTD settlement rule. Since market participants may have several traders submitting convergence bids independently of each other, the inadvertent triggering of the proposed settlement rule is a genuine concern. This side effect could undermine convergence bidding and lead to price divergence.

The proposal will not do anything to offset the natural proclivity of the market to have aggregate balanced positions even if individual SCs refrain from having balanced positions within their portfolios. If this proposal is implemented, SCs that were previously creating balanced positions will likely choose to take one side or the other. In the aggregate, market participants will create the same balanced positions even though few individuals will have a balanced portfolio. Since the proposal doesn't do anything to address the underlying issue, CAISO is unlikely to see the relief it expects. As the settlement rule only applies to individual SCs whose portfolios are balanced, the CAISO will have the same problem that it has now.

CAISO has identified many issues that tend to increase the spread between RTD and HASP prices. One of the proposed solutions is the realtime ramping constraint which should lessen or eliminate the price spikes that are seen in RTD. The CAISO in the last month has implemented a HASP load adjustment feature. This has led the realtime imbalance energy offset charge to decrease dramatically. It is preferable, in Gila's view, to undertake fundamental fixes rather than tamper with settlement rules which only serve to distort markets.

In the first stakeholder process for this charge code, Gila proposed implementing a full Hour-Ahead market. The CAISO has deemed this as a low priority since the 2009 Initiatives Roadmap. A fully functional Hour-Ahead market is the best way to minimize this charge code. This is because CAISO would no longer be selling low priced power just to repurchase it at higher prices. It is unknown to Gila what the costs have been as a result of having this inefficient design persist. Whatever those costs are, they are likely in excess of the costs that balanced convergence bids may place on it. The CAISO should use their resources to fix issues that have the biggest impacts before they spend resources to implement what can, at best, be called a temporary measure.