UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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California Independent System Operator Corporation	)	**Docket No. EL12-73-000**
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MOTION FOR LEAVE TO ANSWER PROTESTS AND ANSWER TO PROTESTS AND COMMENTS OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION

The California Independent System Operator Corporation ("ISO") hereby submits this motion for leave to answer protest and answer to the protest filed in this proceeding by a single market participant, J.P. Morgan Venture Energies Corporation ("JPM"), regarding the ISO's June 8, 2012, petition for a declaratory order.[1] In the June 8 petition, the ISO seeks authority to resettle the ISO market to collect overpayments associated with the ISO's bid cost recovery mechanism. These overpayments were aggravated by exploitative bidding practices that the Commission addressed in response to a filing made by the ISO in March 2011. As discussed below, the protest lacks merit, and the Commission should grant the requested declaratory order.

I. SUMMARY

In its petition, the ISO seeks approval to resettle its market to recover overpayments to generators and return the overpayment amounts to load. The overpayments arose for two reasons: (1) a portion of the overpayments resulted from a settlement procedure that failed to account for payment of energy actually delivered to

[1] The ISO submits this filing pursuant to Rules 212 and 213 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §§ 385.212, 385.213.

load; and (2) a single market participant used an exploitative bidding practice to significantly enhance its bid cost recovery payments.

Bid cost recovery exists to ensure that the resources that the ISO commits or dispatches are able to recover their operational costs associated with start-up, operating at minimum load, and being dispatched above minimum load based on submitted energy bids that may not be recovered due to the marginal prices for energy and ancillary services. Most organized electricity markets have some form of bid cost recovery.

The ISO's request for resettlement authority arises because this settlement mechanism did not work as designed, resulting in an inappropriate shift of payments so load serving entities were paying more than they should have for the energy delivered in some instances. The ISO's petition identifies a total of $52 million that was overpaid by load serving entities due to the settlement error, with approximately $20 million due to the bidding behavior of a single market participant.[2] The ISO has already resettled $35 million of the overpayments, including all amounts within the ISO's requested resettlement authority associated with the exploitative bidding practice.

The Commission should approve the resettlement because it applies the ISO tariff correctly and results in the proper accounting for energy delivered to load. The ISO filed to amend and clarify its market rules to cut off the exploitative bidding conduct

[2] The ISO's March 2011 filings in Docket No. ER11-3149 and June 2011 filings in Docket No. ER11-3856 identified multiple exploitative bidding behaviors which had an estimated impact of approximately $73 million. The resettlement authority requested in this filing only addresses $20 million of the impact of this bidding behavior, with the rest subject to Commission's further actions as a result of ongoing confidential investigations acknowledged in July 2, 2012 filings by the Commission's Office of Enforcement at the U.S. District Court for the District of Columbia. *See footnote* 3, *infra*.

and ensure that all resources received appropriate bid cost recovery compensation.[3] The Commission approved the market rule changes, cutting off the opportunity for exploitation and the inadvertent overpayment to other resources as of March 26, 2011. The ISO has petitioned for resettlement pursuant to the Commission's direction in order to recover amounts overpaid due to the misapplication of the ISO tariff, some of which were exacerbated by the exploitative market behavior targeted in the ISO's March 2011 filing.

JPM is the only market participant challenging the ISO's petition. JPM does not provide any evidence to support its assertion that the settlement practice employed from April 2009 through March 25, 2011 was consistent with the ISO tariff or accurately accounted for payments the resources received for delivered energy.

JPM argues that because the ISO included the description of the erroneous settlement practice in an ISO business practice manual for an extended period of time, the resulting payments should stand even if the result is contrary to the ISO tariff. JPM's argument would require the Commission to deviate from its own precedent and the ISO tariff, both of which require that, in the event of a discrepancy between the tariff and the business practice manual, the tariff prevails.

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[3] *See* ISO March 2011 filings in Docket No. ER11-3149. In a filing made by the Commission's Office of Enforcement in the U.S. District Court for the District of Colombia, the Office of Enforcement identified JP Morgan as the entity that was the subject of the ISO's filings to change its market rules. "Though not named in the Orders, JP Morgan is the entity that engaged in the bidding conduct described in each of these four Orders." *Federal Energy Regulatory Commission v. J.P. Morgan Ventures Energy Corp.*, U.S. District Court for the District of Colombia, Misc. No. 00352-CKK, Memorandum in Support of Petition by Federal Energy Regulatory Commission For an Order to Show Cause Why this Court Should Not Enforce Subpoenas for Production of Documents, filed July 2, 2012, p. 12. This filing goes on to state that "Enforcement is now investigating several different bidding strategies by JP Morgan in CAISO and MISO to evaluate whether they violated the Commission's Anti-Manipulation Rule, including each of the strategies described in the CAISO and MISO filings cited above." *Id*.

JPM further contends that even if the settlement practice was inconsistent with the ISO tariff, the Commission should nonetheless deny retroactive resettlement authority. In cases like this, whether to order refunds, or retroactive resettlement, is a matter of equity within the Commission's discretion. There are few circumstances where the equities could be more in favor of resettlement than here. First, no suppliers will be left financially exposed because even with the resettlement each receives its proper bid cost recovery. Absent a resettlement, there would be an inequitable windfall to a single market participant that exploited the misapplication of the ISO tariff at the expense of California load. Failure to resettle would also leave other entities overcompensated for the energy they delivered, due to the misapplication in the settlement process over the period that resulted in overpayment under certain circumstances not associated with the exploitative bidding practices.

The Commission has the authority to approve the resettlements requested by the ISO. The requested resettlements will prevent California consumers from bearing the costs of overpayments that are contrary to the correct interpretation of the ISO tariff and aggravated by the exploitative bidding behavior of a single market participant. No resource will be harmed by the requested resettlements because all resources, including JPM, will be assured that they will fully recover their bid costs under the requested resettlements. Based on a consideration of the equities in this case, the Commission should grant the ISO's request for resettlement authority.

II. BACKGROUND

The ISO's petition seeks the Commission's approval to resettle bid cost recovery payments, in a manner consistent with the ISO tariff. The resettlement period covers the period beginning with ISO operations under its current rate design on April 1, 2009, to March 25, 2011, when the Commission approved the ISO's request to modify the market rules. The ISO explained that its original settlement of bid cost recovery payments during this resettlement period was inconsistent with the express language and the intent of section 11.8.2.2 of the ISO tariff. The ISO has already undertaken resettlement for trade dates from August 1, 2010, to March 25, 2011. If it receives Commission approval, the ISO will resettle the remaining trade dates from April 1, 2009, through July 31, 2010. If the Commission denies the petition, the ISO will reverse the prior resettlement of the bid cost recovery amounts, with appropriate interest.

The ISO compensates all resources for energy provided, both above and below minimum load, at the locational marginal price. Resources may submit their minimum load costs as a separate component of their bid. Through the bid cost recovery mechanism, the ISO ensures that resources committed or dispatched by the ISO fully recover their start-up and minimum load bid costs and their energy bid costs. In order to avoid overpayment, section 11.8 of the ISO tariff provides for a resource to recover bid costs only to the extent that the resource does not otherwise recover those costs through its receipt of the locational marginal price for the energy it actually delivers. Offsetting bid costs in this manner avoids over-recovery from ISO markets, the costs of which would be borne by load and ultimately by consumers in California. Thus, in order to appropriately offset calculated bid costs, the ISO must also calculate the market revenues associated with delivered portions of the day-ahead schedule, both above and below minimum load. If the resource fully recovers its bid costs from the market, additional payments are not justified.

To facilitate the calculation of energy actually delivered relative to the amount of energy scheduled or dispatched, the ISO developed a settlement calculation tool called the metered energy adjustment factor (“MEAF”), the use of which was set forth in the Business Practice Manual for Settlements and Billing. The MEAF compares the portion of metered energy above the resource’s minimum load and self-schedule for a given resource to its portion of the day-ahead schedule above the resource’s minimum load and self-schedule. While this tool is very effective in measuring the energy delivered above minimum load, it does not properly capture market revenues associated with delivered energy at or below minimum load. When the resource is at or below minimum load, the MEAF goes to zero. It does so because it is designed to capture delivered energy above minimum load and in such circumstances the delivered energy is at or below minimum load. When the MEAF is zero, the settlement practice used during the resettlement period nullified any market revenues from the portions of bid curve to which is applied.

During the resettlement period, in order to calculate the day-ahead energy payments for delivered energy, the ISO applied the day-ahead MEAF to the entirety of day-ahead energy revenues – both the minimum load and the above-minimum load revenues – even though the day-ahead MEAF was calculated based solely on above-minimum load schedules and deliveries. This application failed to account for, and net, the entirety of the minimum load revenues received. Accordingly, the ISO overpaid supply and overcharged demand. A similar issue arose with the application of the real-time MEAF to the real-time instructed energy, which also resulted in the under-accounting of real-time market revenues.

Under normal circumstances, and as was evident from the bid cost recovery costs incurred in the first eighteen months of the ISO's new market design, the MEAF does not tend to zero and actually does capture some of the minimum load market revenues. The flaw in the ISO's application of the MEAF was thus not readily apparent during that period. This issue came to light when one market participant exploited the flaw, and reaped millions of dollars in an inequitable windfall of bid cost recovery payments. The market participant's strategy was to submit high minimum load costs coupled with the submission of day-ahead bids that were low enough – sometimes negative – to ensure that the resources would be scheduled in the day-ahead market. Then the market participant would submit very high bids in the real-time market such that the resources would be dispatched at a very low level or not at all. This would essentially drive the ISO to dispatch the resource to its minimum load or below its minimum load in the real-time. At that point, because the delivered energy above minimum load was small (or nonexistent) relative to the day-ahead scheduled energy above minimum load, the MEAF would be at or close to zero. When the MEAF was applied to the day-ahead minimum load revenues, the settlement calculations would thus disregard all or the vast majority of the market revenues actually received by this market participant. The market participant thus received bid cost recovery for all or most of its high minimum load costs, providing a windfall even after the market participant bought back the day-ahead energy.

Investigating the events further, the ISO also determined that its then existing use of the MEAF was inconsistent with tariff section 11.8, including section 11.8.2.2 and 11.8.4.2 for reasons explained more fully in the ISO's petition. The ISO explained in its petition how resettlement of bid cost recovery payments for the resettlement period is therefore appropriate to properly apply the filed rate.

Eight parties have filed motions to intervene in this proceeding. One party filed comments supporting the petition. Only JPM filed a protest. The ISO does not oppose the motions to intervene.

III. MOTION TO FILE ANSWER

Rule 213(a) (2) of the Commission's Rules of Practice and Procedures generally prohibits answers to protests.[4] The Commission has accepted answers that are otherwise prohibited if such answers clarify the issues in dispute[5] and where the information assists the Commission in making a decision.[6]

As discussed below, JPM presents a number of arguments that the ISO had no cause to address in its petition and raises some issues that are not central to the petition but that the Commission may now consider as a result of JPM's filing. The ISO believes that understanding the ISO's response to these arguments will clarify the issues and assist the Commission's understanding. The ISO therefore requests that the Commission accept this answer.

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4 18 C.F.R. § 385.213(a)(2) (2011).

5 *See Southwest Power Pool, Inc.,* 89 FERC ¶ 61,284 at 61,888 (1999).

6 See *El Paso Electric Co., et al. v. Southwestern Pub. Serv. Co*., 72 FERC ¶ 61,292 at 62,256 (1995).

IV. ANSWER

JPM's arguments fail to refute the ISO's demonstration that the use of the metered energy adjustment factor was in certain conditions contrary to the ISO tariff and that the error should be rectified given the financial impact to the market.

A. JPM Fails to Provide any Evidence That the ISO's Application of the MEAF to Determine Market Revenues of Delivered Minimum Load Energy Was Consistent with the ISO Tariff.

1. JPM distorts the plain meaning of the ISO tariff.

JPM challenges the ISO's assertion that the use of the MEAF to calculate market revenues, as previously set forth in the business practice manual, is inconsistent with the tariff requirement that bid cost recovery be limited to unrecovered costs associated with delivered energy. JPM fails to provide any evidence or analysis that demonstrates that the use of the day-ahead MEAF documented in the business practice manual was adequate for measuring the market revenues associated with delivered energy.

Instead, JPM first asserts that it is inconsistent for the ISO to apply the day-ahead MEAF to the amount of scheduled energy under section 11.8.2.1.5 of the ISO tariff, but not to market revenues under section 11.8.2.2. JPM ignores the fact that bid costs are calculated separately for minimum load, start-up, and scheduled energy above the higher of minimum load or self-schedules.[7] The MEAF is not applied to minimum load or start-up costs under section 11.8.2.1.5, but only to the scheduled energy bid cost—*i.e.,* those above minimum load. Because the MEAF is based on delivered and scheduled energy above minimum load, the MEAF tool is matched with its purpose in implementing section 11.8.2.1.5. This is an apples-to-apples calculation.

[7] Protest at 19.

Yet, under the flawed business practice manual approach that the ISO seeks to reverse, the ISO was applying the day-ahead MEAF to the totality of market revenues: energy bid costs plus minimum load costs. Thus, the calculation of market revenues in the requested resettlements, as explained in the petition, is consistent with the use of the MEAF in determining energy bid costs under section 11.8.2.1.5. On the other hand, the calculation of market revenues under section 11.8.2.2 involves circumstances where a resource may be at or below its minimum load and where the MEAF will not capture market revenues actually received by the resource. JPM therefore is incorrect in arguing that the use of the MEAF is justified for section 11.8.2.2 calculations because it is justified for calculations under section 11.8.2.1.5.

JPM does not present any argument or evidence to support that the MEAF determines revenue associated with delivered energy for portions of the energy bid curve below the resources minimum load energy under any commonly accepted meaning of "delivered" energy, *i.e.*, the energy actually produced by a generator and received by the ISO's grid. Rather, JPM essentially asserts that, because the business practice manual states that the MEAF is defined as a factor calculated for the purpose of determining the portion of the scheduled energy that is actually delivered, then the result of using the MEAF in fact defines the amount of delivered energy.[8]

Under the exploitative bidding practice discussed above, for example, the market participant's resources provided their minimum load energy to the grid and, in turn, to load. The ISO paid the market participant for the full amount. Yet, because of the application of the MEAF to those revenues, only a fraction, if any, of revenues

[8] Protest at 18-19.

associated with portions at or below minimum load energy were counted as revenues from delivered energy, resulting in an overpayment to the market participant each time the MEAF was applied. This result was exaggerated by the market participant's bidding behavior – *i.e.*, negative bids in the day-ahead and then a switch to bids calculated to be above the market clearing price in real time, driving the resources to minimum load energy which leads to the nullification of the market revenues used to offset the resource's bid cost recovery. JPM proposes that the Commission ignore the fact that the tariff requires the ISO to account for revenue earned for this energy delivered below the minimum load energy in determining the proper bid cost recovery payments. JPM further asks the Commission to pretend that, while energy below minimum load was delivered, and the market participant was paid for the delivered energy, such energy should not be counted as delivered because the use of the MEAF documented in the business practice manual did not account for such revenues.

Thus, under JPM's approach, the term "delivered" in tariff section 11.8.2.2 would have no fixed meaning. The meaning of "delivered" could be changed – intentionally or otherwise – simply by changing the manner in which the ISO settlements process calculated "delivered" energy in the business practice manual. This is simply not a reasonable approach to the application of the filed rate.

JPM further argues that the MEAF does not need to be the best means for determining market revenues associated with delivered energy to be consistent with the tariff.[9] While there may be more than one way to determine market revenues associated with delivered energy, the former use of the MEAF was not, as the ISO

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[9] *Id.* at 20.

showed in its petition, even a somewhat effective means of doing so; indeed, it was an *inaccurate* means, and, as was later demonstrated, one that provided an opportunity for exploitation, which one market participant exploited aggressively.

2. Inclusion of the MEAF in the business practice manual does not render it consistent with the ISO tariff.

JPM also argues, in essence, that inclusion of the MEAF for determining market revenues in the business practice manual somehow renders it *per se* a correct application of the ISO tariff because the business practice manual "is—by definition—consistent with the ISO tariff."[10] JPM points to the tariff section providing that the business practice manual is to be consistent with the tariff and to the business practice manual provisions stating that it is intended to be consistent with the tariff. While it is correct that the business practice manual is intended to be consistent with the tariff, and the ISO and stakeholders strive for this, unfortunately a statement of purposes does not mean that these objectives are always achieved in practice. Thus, the business practice manuals expressly provide that the ISO tariff governs in the event of a conflict with the business practice manual.[11]

JPM goes on to state the ISO's admission of inconsistency must also be an admission of a violation of the ISO's own rules. As the ISO has explained, this erroneous application of the tariff was an unintended error that was virtually undetectable until exploited by a particular bidding strategy. Under JPM's proposed approach to tariff interpretation, no matter how egregious an error in an ISO business

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10 *Id.* at 21.

11 For example, Section 1.3 of the Business Practice Manual for Settlements and Billing states in relevant part, "The provisions of this BPM are intended to be consistent with the CAISO Tariff. If the provisions of this BPM nevertheless conflict with the CAISO Tariff, the CAISO is bound to operate in accordance with the CAISO Tariff."

practice manual, the ISO and the Commission must allow that error to stand. This novel principle has no basis in logic or precedent, and certainly no merit given the equities in this matter as discussed further below.

JPM nonetheless argues that, under Commission precedent, independent system operators are not free to disclaim statements in published manuals.[12] It first cites *PPL EnergyPlus, LLC v. NYISO*, 115 FERC ¶ 61,383 (2006). Nothing in that proceeding is relevant here. *PPL EnergyPlus* concerned the timeliness of a request for allocation of available import capacity rights from the New York Independent System Operator. The relevant practice manual stated that the fax time-stamp determined the priority of allocations. It did not specify the mechanism for determining timeliness – *i.e.,* whether the New York Independent System Operator received the request before or after the opening of the request window. A guidance bulletin, however, stated that the fax time-stamp determined timeliness.

The New York Independent System Operator argued that under the practice manual it could use an official time source to determine timeliness. The Commission rejected that interpretation of the practice manual because nothing in the practice manual or the tariff allowed the use of "official" time. It also found that the guidance document reinforced its interpretation of the practice manual and that it was reasonable for the market participants to rely on the guidance manual. The Commission determined that the New York Independent System Operator's practice violated its tariff.

Here, the issue is not an interpretation of a business practice manual. The question is whether the business practice manual was consistent with the ISO tariff. In

12 Protest at 22.

PPL EnergyPlus, the Commission concluded that the New York Independent System Operator's practice – under its interpretation of the practice manual – was not consistent with its tariff. Here, the ISO asks the Commission to find that the practice previously documented in the business practice manual is inconsistent with the ISO tariff.

JPM also cites in this regard *Midwest Indep. Sys. Transmission Operator Corp.,* 117 FERC ¶ 61,113 (2006), *order on reh'g*, 118 FERC ¶ 61,212 (2007) ("*MISO*").[13] *MISO* concerned the inclusion of virtual supply offers in the calculation of resource sufficiency guarantee charges. The practice manual excluded them from the calculation. In the original order, the Commission had found the practice manual inconsistent with the tariff.[14] The Commission specifically ruled, "The fact that the Midwest ISO Business Practices Manuals would suggest a different result does not impact our decision. As the Commission has stated in other proceedings, business practices manuals should comply with the terms of the tariff, not the other way around."[15] The Commission originally ordered refunds in that proceeding. The original order thus supports the principle that a business practice manual can be found to be contrary to the tariff of an independent system operator.

In *MISO*, a later order in that proceeding, the Commission gave weight to market participants' reliance on the inconsistent MISO business practice manual, and reversed itself on refunds only. It did not revise its conclusion regarding the business practice manual. Even in the later order, the Commission made it clear that it could order

[13] *Id.*

[14] *Midwest Indep. Sys. Transmission Operator Corp.*, 115 FERC ¶ 61,108 at P 26 (2006).

[15] 115 FERC ¶ 61,108 at P 30. As discussed below, the Commission reiterated that conclusion in *MISO.*

refunds or resettlements contrary to the business practice manual based on a consideration of the equities involved. The ISO discusses below why considerations in this proceeding, unlike in *MISO*, require retroactive resettlement.

JPM further contends that the business practice manual was subject to extensive stakeholder review and input, and, therefore, the ISO must demonstrate that the stakeholders were wrong in order to demonstrate that the business practice was inconsistent with the tariff. Whether the former use of the MEAF was inconsistent with the tariff, however, is a simple legal question – it is not one to be decided by majority vote of the stakeholders or anyone else.[16] The ISO made the necessary legal showing in its petition. It is worth noting, moreover, that not a single market participant other than JPM has protested the interpretation set forth in the petition.

3. The failure to detect the flaw in the MEAF sooner does not render it consistent with the ISO tariff.

JPM makes two related points, essentially arguing that the failure to sooner detect the flaw in the use of the MEAF during the resettlement period demonstrates that the MEAF was consistent with the ISO tariff. There is no merit to this argument.

First, JPM cites an audit of the ISO's settlement system conducted by PricewaterhouseCoopers and filed with the Commission as part of the ISO's readiness certification. The audit concluded that the ISO's settlements and market clearing system generally were operating as designed and producing results that were

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[16] JPM also spends two pages reciting the ISO's statements, in amending section 11.8.2.2 to refer to delivered energy, that the amendment was consistent with the business practice manual. The ISO has explained in the petition that it was mistaken. The ISO had not yet identified the flaw in the application of the MEAF, which went undetected until it was exploited for a significant windfall by a market participant's bidding strategy. Nowhere did the ISO ever imply, or even hint, that it would be appropriate to disregard a portion of the market revenues received for minimum load costs – which is precisely the result of the application of the MEAF during the resettlement period.

consistent with the ISO tariff. JPM points out that, under section 11.29.5.4, in a dispute regarding settlement calculations; the audit report is *prima facie* proof that the charges in a settlement statement have been calculated in a manner consistent with the ISO tariff.[17]

JPM neglects to note that the same tariff section provides, "Nothing in this section will be deemed to establish the burden of proof with respect to Settlement calculations in any proceeding." The ISO demonstrated in the petition that the application of the MEAF to revenues for minimum load energy does not in fact calculate all of the revenues associated with delivered energy. The ISO's showing – which relies on the inconsistency between the manner in which the MEAF is calculated and the language of section 11.8.2.2, and was illustrated with concrete examples – was more than adequate to overcome any initial presumption of consistency with the ISO tariff. By contrast, JPM has made no showing whatsoever. Indeed, JPM's entire argument appears to be that because the inconsistency did not come to light sooner, the inconsistency does not exist. JPM cannot rely upon *prima facie* evidence to make its case in light of an uncontroverted showing that the tariff presumption does not hold. That the inconsistency did not become apparent until a market participant exploited it does mean the inconsistency did not exist.

Second, JPM contends that the interpretation of section 11.8.2.2 supported in the petition is contrary to the ISO's course of performance for the first two years of the new market design. According to JPM, "A party's consistent practice or course of performance under a contract or tariff can provide evidence that the meaning or

[17] Protest at 25.

interpretation of that contract or tariff is consistent with the course of performance."[18] As an initial matter, the ISO revised its "course of conduct" over a year ago, when it first recognized that application of the MEAF did not comport with the ISO tariff. This was not an instance of the ISO consciously deciding to change its interpretation of the ISO tariff; rather it was recognition that a practice that the ISO had previously believed properly implemented the tariff did not in fact do so. The ISO recognized this and changed this practice when the exploitative bidding strategy brought the inconsistency to light.

The two decisions that JPM cites in support of these arguments address contract interpretations, not tariff interpretations.[19] The meaning of contracts depends upon the agreement of the parties, to which course of performance is relevant. The ISO is unaware of any decision in which the Commission based a tariff interpretation on course of performance.

More importantly, as the Commission has stated, "Such evidence is only considered to ascertain the intent of the parties when the intent has been imperfectly expressed in ambiguous language and is not admissible to contradict or alter express terms."[20] In this context, the term "delivered" is not ambiguous. The energy was either delivered or it was not. The petition demonstrated conclusively that the MEAF, as used during the resettlement period, did not measure all revenues associated with delivered energy. In *MISO,* cited by JPM, the Commission very explicitly rejected arguments that

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[18] Protest at 26.

[19] *Midwest Indep. Transmission Sys. Operator*, 138 FERC ¶ 61,055 (2012); *N.Y. Indep. Sys. Operator, Inc*., 131 FERC ¶ 61,032 (2011).

[20] *MMC Energy, Inv. v. Cal. Indep. Sys. Operator Corp.,* 123 FERC ¶ 61,251 at P 80 (2008).

it “should interpret the tariff differently based on the course of conduct between the parties or the language of the business practice manuals; the filed and accepted tariff is the governing document and not the business practice manuals – the former has precedence over the later and not the other way around.”[21] There is no room here for consideration of any alleged course of conduct.

B. It Is Appropriate to Resettle Bid Cost Recovery Retroactively to April 1, 2009.

JPM argues that, if the application of the MEAF to minimum load energy was inconsistent with the ISO tariff, the Commission should nonetheless deny retroactive resettlement authority. JPM cites Commission precedent declining to impose retroactive settlements in some instances where the initial settlement applied market rules inconsistent with the tariff.[22] JPM particularly cites *MISO*, where the Commission noted that market participants had relied on information in the Midwest Independent Transmission System Operator’s business practice manual that differed from the tariff.

The ISO recognizes that, as discussed in *MISO*, the decision whether to order refunds, or retroactive resettlement, is a matter of equity within the Commission’s discretion. The Commission generally considers two matters: whether the failure to direct refunds will offend “equity and good conscience” and whether it will create substantial uncertainty in the markets and undermine confidence in them.[23] The ISO submits that these considerations strongly dictate the propriety of retroactive resettlement here.

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21 *MISO* at P 47.

22 Protest at 27.

23 *MISO* at PP 94-95.

First, although the resettlement will reduce payments to energy suppliers, it will not cause any supplier to have operated at a loss. Every supplier will still receive its full unrecovered bid cost. This is the basic promise that the ISO tariff makes to suppliers as an inducement to trade, and the resettlement will do nothing to create uncertainty regarding that principle or undermine confidence in it. On the other side of the ledger, absent resettlement, load in California will be saddled with costs that were far more than was necessary in order to ensure adequate service. As explained in the ISO's petition, the excess bid cost recovery charges during the resettlement period were over $50 million.

Second, unlike the situation in *MISO*, there is evidence that the settlement of unrecovered bid costs in a manner contrary to the ISO tariff did result in a significant "inequitable windfall."[24] As noted above, and fully explained in the ISO's March 21, 2011, filing in Docket No ER11-3149 (as corrected on March 25, 2011), the ISO determined that, beginning in August 20, 2010, one market participant (as scheduling coordinator for a number of resources) began engaging in a bidding practice that exploited the flaw in the ISO's calculation of unrecovered bid costs. Between April, 2009, and July, 2010, bid cost recovery ran between $3 million and $7 million a month. From August, 2010, through February, 2011, it increased to over $20 million a month. The market participant engaging in the bidding strategy earned a significant percentage of the bid recovery costs paid out during that latter period. Under these circumstances, the failure to direct refunds will offend "equity and good conscience." Indeed, this is

[24] *Id.* at P 95.

precisely the type of inequitable windfall that retroactive resettlement is designed to recapture.

C. The ISO's Resettlement of the Bid Cost Recovery Payments Is Not Grounds for Denial of the Petition.

JPM contends that the Commission should deny the petition because the ISO already has resettled bid cost recovery during the latter part of the resettlement period. JPM asserts that the ISO action is contrary to Commission orders.[25]

The ISO explained in the petition its reasons for continuing with resettlement. In essence, the ISO concluded that, because it had already commenced resettlement and because the ISO intended to seek a Commission ruling on these resettlements, multiple rounds of resettlements could only increase uncertainty. The ISO believes that the resettlements to date have been consistent with its legal obligations. Even if the Commission were to find that the ISO should have taken a different approach, however, the appropriate remedy would be the final resettlements the ISO has already committed to undertake. Moreover, JPM's arguments fail to recognize that the Commission expressly invited the ISO to seek Commission authorization for resettlements consistent with the correct interpretation of the ISO tariff.

JPM's arguments should not distract the Commission from the simple facts that the original settlement was contrary to the tariff, that load was overcharged by $52 million, and that certain resources received an inequitable windfall. This issue should therefore not affect the Commission's decision on resettlement.

[25] Protest at 16.

V. CONCLUSION

For the reasons explained above and in the ISO's petition, the Commission should grant the requested declaratory order.

Respectfully submitted,

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Dated: July 24, 2012

CERTIFICATE OF SERVICE

I hereby certify that I have this day caused the foregoing document to be served upon each party listed on the official service list for this proceeding, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Executed at Washington, D.C. on this 24th day of July, 2012.

/s/ Michael E. Ward

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