THE UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	))	**Docket No. ER14-____-000**

PETITION FOR LIMITED WAIVER OF TARIFF PROVISIONS, REQUEST FOR SHORTENED COMMENT PERIOD, AND REQUEST FOR EXPEDITED COMMISSION ACTION BY MARCH 19, 2014

The California Independent System Operator Corporation ("ISO") respectfully requests that the Commission grant a limited waiver,[1] effective from the day this waiver is granted through April 30, 2014, of two provisions of the ISO tariff to allow the ISO to use updated natural gas price data for market execution and settlement purposes when natural gas prices for the affected trading day significantly exceed the applicable tariff-based gas price index. Natural gas prices faced by the ISO's electric suppliers in recent months have been uncharacteristically volatile and have peaked at unprecedented levels. Due to the requirement that the ISO calculate gas prices based on multiple price sources, and the timing of those publications, the gas price indices currently used to calculate fuel costs considered in the ISO day-ahead market have the potential to lead to inefficient market outcomes and unrecoverable fuel costs when significant and sudden jumps in the price of gas occur. Given the uncharacteristically volatile nature of natural gas prices observed this winter, the

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[1] The ISO submits this petition pursuant to Rule 207 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.207 (2013). Capitalized terms not otherwise defined herein have the meanings set forth in appendix A to the ISO tariff, and references to sections are references to sections of the ISO tariff unless otherwise stated.

waiver requested in this filing is necessary to provide temporary relief and protection against potential adverse outcomes in the ISO's day-ahead market.

The ISO requests that the Commission issue an order granting this petition by March 19, 2014. Today the ISO is also filing a more limited version of this petition which requests waiver of the same tariff provisions but is limited to updating gas prices solely for use in financial settlements. The ISO is requesting that the Commission issue an order on that second petition by the close of business tomorrow, March 7. Thus, the second petition is intended to be a stop-gap remedy to address near-term adverse outcomes pending the issuance of a Commission order by March 19 granting this broader companion waiver petition.

I. Introduction and Summary of Filing

In both of the petitions being filed today, the ISO seeks temporary waiver of two ISO tariff provisions in order to ameliorate the impacts of any natural gas price spikes during the remaining winter and early spring period, which, based on price trends, is when the ISO believes they would most likely occur. An example of the type of event that this waiver is intended to address occurred on February 6, 2014. Per the ISO tariff, the day-ahead market for that day, which ran on the morning of February 5, utilized a gas price index calculated on the evening of February 4, derived from price data published on February 4, for gas delivered on February 5. However, between this calculation and the next publication of prices on the morning of February 5 for gas deliveries on February 6, natural gas prices increased to levels roughly 300 percent of what they had been, with the result that natural gas prices for the February 6 trading day greatly exceeded the tariff-based gas price index.

The ISO seeks temporary waiver of two sections of the ISO tariff to allow it to capture the impact of such gas price spikes in its day-ahead market on the day that they occur. First, the ISO seeks temporary waiver of the requirement in section 39.7.1.1.1.3 that the ISO determine natural gas cost inputs based on at least two natural gas price indices published the day prior to running the day-ahead market. This waiver will allow the ISO to instead use the only price index specified in the tariff that is available at approximately the same time as the day-ahead market is executed – the natural gas price index published by the Intercontinental Exchange ("ICE"). The ISO will use this single price index to calculate the applicable start-up and minimum load costs and cost-based ISO-generated energy bids for resources under a must-offer requirement in clearing and settling the ISO day-ahead market. The ISO will also use this additional flexibility to ensure that settlements of resources based on ISO-generated cost-based default energy bids utilize a default energy bid that more accurately reflects the price of natural gas for the applicable day-ahead market.

Second, the ISO is also proposing waiver of section 30.4.1.2. That section allows resources that elect to bid their start-up and minimum load costs based on a monthly gas price calculation, known as the registered cost option, to switch to a daily calculation, known as the proxy cost option, when the proxy cost exceeds their registered cost. Resources that select the registered cost option are required to remain under that option for a minimum of 30 days. Should resources switch from registered to proxy cost, that section requires resources to remain under the proxy cost option for the remainder of the applicable 30-day period when such elections are made. The ISO seeks waiver of that section so that it can allow resources that meet this criterion to be able to switch to the proxy cost option on those days on which the ISO must use the ICE price index to capture a price spike and return to the registered cost option when the proxy cost ceases to exceed the registered cost instead of having to remain under the proxy cost option.

The relief requested in this waiver is intended to address significant price spikes that may occur after the requested effective date of March 19 until April 30; the ISO does not intend to exercise the flexibility sought under this waiver on a daily basis. The ISO will exercise this flexibility only when there is a significant increase in the natural gas price, which the ISO plans to define initially as 150 percent or more of the gas prices based on a comparison of the index calculated on the prior evening and the ICE prices available the next day. On all other days, the ISO will continue to utilize the gas price calculated in accordance with the current tariff provision. The applicable threshold and procedures for executing this flexibility on any given day will be specified in the ISO's business practices manuals.

Good cause exists to grant this waiver because it is of limited scope, will remedy a concrete problem, and it will not have undesirable consequences. The waiver provides clear benefits because it will allow the day-ahead market to commit resources based on more accurate natural gas prices for the trading day in the event of a significant increase in gas prices. In addition, the more accurate natural gas price, which will be implemented through the ISO's existing tariff authority for recovery of bid costs and exceptional dispatch settlement, will help to ensure that market participants can recover their actual production costs when the gas prices increase significantly.

The ISO seeks this relief in two parts. With respect to the current waiver petition, the ISO respectfully requests that the Commission act expeditiously and shorten the comment period to no more than seven days so that it may issue an order on this petition by March 19, 2014. It is important that this waiver be in place as soon as possible because any further natural gas price spikes due to cold weather are most likely to occur in March and April. But because this waiver request, when triggered, will modify the manner in which the ISO calculates certain cost inputs utilized in the day-ahead market and therefore will impact the market results, the ISO requests that this waiver take effect only after the Commission issues an order approving it.

The ISO is concerned, however, that another price spike could occur prior to March 19. Therefore, today the ISO is also filing a more limited version of this petition which requests waiver of the same tariff provisions but is limited to updating gas prices solely for use in financial settlements. The ISO is requesting that the Commission issue an order on that second petition by the close of business tomorrow, March 7, and is requesting immediate effectiveness of those measures as of the day the order in that proceeding is issued. Thus, the second petition is intended to be a stop-gap remedy to address near-term adverse outcomes pending the issuance of a Commission order by March 19 granting the broader waiver authority requested in this petition. Because the current filing requests waiver for both market and settlement purposes, any waiver granted for the companion settlement-only request will be automatically superseded by a Commission order approving the waiver requested in this petition. Finally, the ISO plans to commence a stakeholder process in April to address the issues raised by gas market conditions and to more comprehensively develop interim and permanent tariff solutions. To address the issues recently identified, the ISO has accelerated the stakeholder process it previously scheduled for this fall. The ISO expects that the stakeholder process will require at least several months to complete but is committed to developing an interim solution that can be implemented in the fall if such a solution does not require substantial system changes. The two waivers requested today will help the ISO and market participants bridge this gap during the period that price spikes are most likely to occur.

II. Background Regarding Need for Limited Tariff Waiver

A. Use of Gas Price Indices in the ISO Markets

1. Start-Up and Minimum Load Costs

In the day-ahead market, the ISO commits resources and publishes a financially binding day-ahead schedule. The costs that the market considers when making commitment decisions include the costs of starting up resources (start-up costs) and the costs of running resources at their minimum operating levels (minimum load costs).[2] On a 30-day basis, scheduling coordinators for resources may choose either the proxy cost option or the registered cost option for specifying their start-up costs or minimum load costs for the resources in the ISO markets.[3]

For resources under the proxy cost option, the ISO calculates start-up and minimum load costs using a natural gas price index.[4] Each day, the ISO calculates this price index between 7:00 p.m. and 10:00 p.m. Pacific time using up to four (but at least two) natural gas prices published that day from the following sources: Natural Gas Intelligence, SNL Energy/BTU's Daily Gas Wire, Platt's Gas Daily, and ICE. This gas price index is used in the next day's day-ahead market run for the following trading day as well as the real-time market for the following day.[5] Resources under the proxy cost option can submit bids for

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[2] *See* tariff section 31.3; tariff appendix A, definitions of "start-up cost" and "minimum load costs."

[3] Tariff section 30.4. A scheduling coordinator for a resource can choose the proxy cost option or the registered cost option for specifying either the start-up costs or the minimum load costs or both. *Id.* Thus, for a 30-day period, the scheduling coordinator could choose the proxy cost option for both the resource's start-up costs and minimum load costs, or could choose the proxy cost option for the resource's start-up costs and the registered cost option for the resource's minimum load costs, *etc.*

[4] Tariff section 39.7.1.1.1.3 specifies how the ISO calculates the natural gas price index. The natural gas price index is used for start-up and minimum load costs, variable cost default energy bids and generated bids. *See also* Business Practice Manual for Market Instruments at section C.1 ("The daily Gas Price Index (GPI) is the index that is used in the calculation of the Default Energy Bids, as well as the generated bids including Startup Costs, and Minimum Load Costs."). The business practice manual for market instruments is available on the ISO website at http://bpmcm.caiso.com/BPM%20Document%20Library/Market%20Instruments/BPM_for_Market_Instruments_v31_clean.doc.

[5] The result of this timing is that natural gas prices used in the day-ahead market for the applicable trading day are calculated based on prices published two days prior. An example of how this works in practice using the February 6 trading day is that natural gas prices are calculated between 7:00 and 10:00 pm on February 4, which are then utilized in the day-ahead market for the February 6 trading day, which closes at 10:00 am on February 5. The reason for using gas prices published on February 4 is that, except for ICE, all of the other price sources

their start-up and minimum load costs in the day-ahead market so long as those bids between zero and the calculated proxy cost.

Of the four publications specified in the ISO tariff, ICE publishes gas prices the earliest in the day – by as early as 10:01 a.m., or by noon at the latest.[6] The ISO's experience has been that ICE almost always publishes the gas prices by 10:01 a.m. This timing converges with the timing of the ISO's day-ahead market, which normally closes (*i.e.*, the ISO no longer accepts bids for the following trading day) at 10:00 a.m. and the results of which are normally published for the following trading day at 1:00 p.m.[7] The ISO has the authority, however, to modify the normal timing of the day-ahead market in the event of a market disruption, to prevent a market disruption, to minimize the extent of a market disruption,[8] or to preserve system reliability, prevent an imminent or threatened system emergency, or to retain operational control over the ISO controlled grid during an actual system emergency.[9] This is relevant because, as explained below, when the ISO anticipates that natural gas prices will increase significantly, the ISO will use this authority to keep the day-ahead market open until the ICE prices for the applicable trading day are published.

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specified in the ISO tariff are published well after the close of the ISO's day-ahead market.

6 *See* business practice manual for market instruments at section C.3. The earliest that any of the other publications can provide gas prices is 4:00 p.m. *Id.*

7 Tariff section 30.5.1(a); tariff appendix A, definition of "market close."

8 Tariff section 7.7.15.1(a).

9 Tariff section 31.6.1(i).

The registered cost option, on the other hand, allows scheduling coordinators to register fixed start-up and minimum load cost values of their choosing for each resource they represent in the ISO's master file, subject to a cost cap set at 150 percent of the projected proxy cost, which is calculated on a monthly basis.[10] Per section 30.4.1.2 of the ISO tariff, scheduling coordinators must remain under either the proxy or registered cost option for a minimum of 30 days before they can switch. There is one exception: if the daily proxy cost calculation exceeds its registered costs, a scheduling coordinator can switch from the registered cost option to the proxy cost option for the remainder of the 30-day period.[11]

2. Variable-Cost Default Energy Bids

The ISO uses default energy bids to mitigate bids of resources subject to local market power mitigation.[12] When a resource's bid is mitigated, the mitigated bid, based on the default energy bid, is substituted for use in the market clearing process and is also used to determine the resource's bid cost recovery compensation.[13] Default energy bids are also used to settle exceptional

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10 Tariff sections 30.4.1.2, 39.6.1.6. Projected proxy cost is different from proxy cost and is determined using a different calculation.

11 *Id*.

12 *See* tariff section 39.7.1, *et seq.* Each scheduling coordinator can choose one of the following three options as its preferred option for calculating default energy bids: (1) the variable cost option, (2) the negotiated rate option, or (3) the locational marginal price option. Of these options, only variable-cost default energy bids, which are addressed in tariff section 39.7.1.1, are subject to this request for tariff waiver.

13 Tariff section 11.8.

dispatches and in the settlement of residual imbalance energy.[14] In determining default energy bids calculated using the variable cost option, the ISO is required to use the natural gas price index specified in section 39.7.1.1.1.3.[15] Therefore, a natural gas price spike can have a similar effect on variable-cost default energy bids calculated for the day-ahead market as it does on start-up and minimum load costs, *i.e*. variable-cost default energy bids can reflect gas prices that are significantly lower than the actual gas prices for the trading day.

3. Generated Bids

The ISO generates cost-based bids when a scheduling coordinator does not submit a bid for a resource that is subject to a must offer requirement under either a resource adequacy requirement or the scheduling and infrastructure bidding rules as set forth in the ISO tariff and applicable business practice manual.[16] As with start-up and minimum load costs, the ISO is required to use the indexes specified in section 39.7.1.1.1.3 to produce generated bids.[17]

B. Higher and More Volatile Natural Gas Prices Experienced in the West During Winter 2013-2014 and the Impacts Thereof

In December 2013 and the first two months of 2014, the ISO markets have been subjected to uncharacteristically higher and more volatile natural gas prices

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14 *See* ISO tariff sections 11.5.6 and 11.5.5, respectively.

15 *See supra* note 6.

16 *See* tariff sections 30.7.3.4, 40.6.8; tariff appendix A, definition of "generated bid".

17 *See supra* note 4. As with the tariff provisions discussed above regarding the recovery of start-up and minimum load costs under the proxy cost option, although the tariff provisions regarding generated bids do not directly reference section 39.7.1.1.1.3, the ISO interprets the provisions in section 39.7.1.1.1.3 to apply to the calculation of generated bids.

than the markets have experienced since the ISO's current market design went into effect in April 2009. In particular, in early February, California natural gas markets experienced an increase in prices to levels amounting to roughly 300 percent of the pre-increase levels within a span of less than twenty-four hours. On February 4, 2014 at 9:50 p.m., the natural gas index prices applicable to resources in the ISO markets ranged from $7.63/MMBtu to $8.62/MMBtu. But by February 5, 2014 at 10:01 a.m., those prices had increased to a range of $12.29/MMBtu to $23.53/MMBtu.

The higher natural gas prices experienced on February 5 were not reflected in the proxy cost calculation of start-up and minimum load costs for resources that were committed in the ISO's day-ahead market on February 5 for the February 6 trading day. Instead, per the calculation methodology set forth in section 39.7.1.1.1.3, the ISO's day-ahead market for the February 6 trading day utilized gas prices published on February 4 for gas deliveries for February 5. Likewise, these prices were not directly reflected in the costs of those resources utilizing the registered cost option on this date because such resources are limited to bidding commitment costs no greater than 150 percent of their projected proxy costs calculated on a monthly basis. As a result, a number of generators expressed concerns to the ISO regarding their ability to adequately recover their production costs as a result of the February natural gas spike. Some generators also expressed concern regarding the ISO's dispatches on February 6, which, due to a price differential between commitment costs and incremental energy bids, committed a number of resources to minimum load in lieu of dispatching them for incremental energy.

Under normal conditions, the risk of a recurrence of this type of spike in natural gas prices could be expected to decline as the winter season ends in California, which typically happens around April 1 each year. But this year unusual conditions currently present in the electricity and natural gas markets create a heightened possibility that such natural gas price spiking events may occur again even after April 1. Specifically, gas conditions in California are challenged by low storage inventory in California and an increase in demand in the west, the Midwest, and Canada due to the uncharacteristically cold weather being experienced in portions of the United States and Canada. These conditions have contributed to increased gas price volatility among the major companies that supply natural gas to California.

Given these conditions, the ISO believes there is a heightened risk that price spikes similar to the one in early February may recur until the end of the cold weather season in the United States and Canada, which may persist through March and to the end of April. Thus, the ISO is requesting that the waiver requested herein remain in effect until April 30, 2014.

III. Request for Limited Waiver of ISO Tariff Provisions

The Commission has previously granted requests for tariff waivers in situations where (1) the waiver is of limited scope, (2) a concrete problem needed to be remedied, and (3) the waiver did not have undesirable consequences, such as harming third parties.[18]

In this case, all three elements under Commission precedent for granting a tariff waiver are satisfied. Therefore, good cause exists to grant the ISO's request for waiver.

A. The Requested Waiver

The ISO requests waiver of certain provisions in sections 30.4.1.2 and 39.7.1.1.1.3 of the ISO tariff in order to allow the ISO to utilize the most recently available natural gas prices in the event of a significant price spike, and to allow resources more flexibility to structure their commitment cost bidding under these circumstances.

With respect to section 39.7.1.1.1.3, under normal conditions the ISO will continue to calculate the daily gas price index pursuant to the requirements of this section for use in the next day's day-ahead market run. However, the ISO will monitor gas prices and if, prior to the close of the day-ahead market at 10:00 a.m. on the day on which it executes the applicable day-ahead market, the ISO has reason to believe that the gas prices published by ICE that day will exceed a certain percentage of the price index calculated the night before, the ISO will hold open the day-ahead market until publication of the ICE prices. If the ICE prices published that day do not equal or exceed this threshold, then the gas

[18] *See, e.g.*, *New York Independent System Operator, Inc.*, 146 FERC ¶ 61,061, at P 19 (2014); *PJM Interconnection, L.L.C.*, 141 FERC ¶ 61,103, at P 8 (2012); *ISO New England Inc.*, 134 FERC ¶ 61,182, at P 8 (2011); *California Independent System Operator Corp.*, 132 FERC ¶ 61,004, at P 10 (2010).

prices calculated the night before will be utilized per the normal process set forth in Section 39.7.1.1.1.3.[19]

However, if the ICE prices equal or exceed the threshold for any of the gas price regions used in the ISO markets, the ISO will exercise the flexibility provided under the requested waiver and will not calculate the gas price index utilizing at least two price sources based on prices published the day prior to the running of the day-ahead market (*i.e*. two days prior to the applicable trading date).[20] Instead, the ISO will re-calculate the gas price index using just the ICE prices published on the same day that the day-ahead market is executed and utilize these updated prices in determining resources' start-up and minimum load costs, as well as any ISO-generated bids used for resource adequacy resources and as required by the scheduling and infrastructure bidding rules. This means that the day-ahead market, for these purposes, will utilize gas price data that pertains to the same trading day for which the day-ahead market creates schedules.[21] The reason for relying solely on ICE when gas prices exceed the threshold is that ICE's index is the only price index of those listed in Section 39.7.1.1.1.3 that is published around the time that the day-ahead market closes (10:00 a.m.). Utilizing the ICE prices in these circumstances is appropriate

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[19] ICE publishes gas price data for several regions in California. The ISO proposes that the special waiver procedures discussed herein will be triggered if a price increase in any of these regions exceeds the threshold.

[20] The ISO is not proposing, as a component of this waiver petition, a particular percentage threshold that would trigger the recalculation of the natural gas index. As explained below, the ISO plans to define the threshold in the business practice manual for market instruments.

[21] The ISO will include these special procedures in a business practice manual.

because when a significant spike in gas prices occurs, market efficiency and cost recovery are better served by relying on data that reflects the differential in prices for the applicable trading day, even if this means using the only available source for up-to-date gas prices.

During a gas spike triggering event, the ISO will notify the market that an event has been triggered and will hold the day-ahead market open for up to two and one-half hours beyond the normal 10:00 a.m. market close in order to incorporate this updated price data as well as to allow scheduling coordinators to resubmit bids reflecting the updated gas price calculations.[22]

In addition, in order to permit resources subject to the registered cost option to have the same opportunity as resources subject to the proxy cost option to receive higher start-up and minimum load costs when the threshold is triggered, the ISO requests a waiver of the provision in section 30.4.1.2 that requires a resource under the registered cost option that switches to the proxy cost option to remain under the proxy cost option for the remainder of the 30-day period. The ISO requests waiver of this provision so that if a scheduling coordinator elects to exercise the proxy cost option under conditions where the price increase threshold is triggered, it will revert to the registered cost option effective as of the next day that gas prices decline to a level such that the proxy

[22] The expected significant increase in natural gas prices will constitute a market disruption that permits the ISO, under existing tariff authority, to hold the day-ahead market open for this longer time, as well as to allow the resubmission of bids. *See* tariff section 7.7.15. Such events will be reported to the Commission consistent with the requirements of section 7.7.15.

cost no longer exceeds its registered cost.[23] If scheduling coordinators wish to switch for the remainder of their 30-day period, they will be required to follow the existing tariff provisions for such transfers. During the term that this waiver is in effect, the ISO would endeavor to implement such transfers to and from the proxy cost option under the existing tariff requirements as quickly as practical.

The ISO will implement this procedure by giving all scheduling coordinators representing resources under the registered cost option the choice to include them in a list to be compiled by the ISO of resources that will automatically be switched to the proxy cost option in the event that: (1) the gas price indices exceed the threshold; and (2) the updated proxy costs (*i.e.*, those based on the more current ICE gas price index) for the listed resource exceed the resource's registered cost values. When the threshold is triggered, resources subject to the registered cost option and included on this list will have their start-up and minimum load costs determined based on the daily proxy cost calculation using the ICE price, as described above. The reason for creating this advance list is that the ISO cannot, practically speaking, switch resources between the registered cost and proxy cost option in the short amount of time between recalculating gas costs and execution of the day-ahead market. A resource will continue to have its start-up and minimum load costs determined in this manner until gas prices decline to the point where the resource's proxy cost no longer

[23] A scheduling coordinator's proxy or registered cost election is reflected in the ISO master file for resources. The ISO cannot mechanically change this election in the master file in the time between the recalculation of gas prices and the close of the day-ahead market. Therefore, scheduling coordinators electing in advance to "switch" to the proxy cost option when a gas spike occurs will technically still be considered to be under the registered cost option, but will be calculated and settled using the proxy cost during this period.

exceeds its registered cost. When this occurs, the resource's commitment costs will revert to being determined based on the normal registered cost rules.

With respect to the variable-cost default energy bids used in the ISO's local power market mitigation process, the ISO is requesting a more limited waiver of section 39.7.1.1.1.3. Unlike start-up and minimum load costs and generated bids, it is not feasible to recalculate those default energy bids prior to running the day-ahead market. This is because the variable-cost default energy bids are produced by an independent entity and are delivered each day to the ISO to be used in the day-ahead market. It would not be feasible for the ISO to reconstruct the variable-cost default energy bids on any given day using the updated index after they have already been delivered by the independent entity in time to include them in the day-ahead market run. However, the ISO proposes to exercise additional flexibility if the Commission grants the requested waiver of section 39.7.1.1.1.3 when the price increase threshold is met for purposes of settling those resources that were subject to variable-cost default energy bids in the day-ahead market (*i.e.*, subject to local market power mitigation). The ISO proposes to settle these transactions based on the variable-cost default energy bids sent by the independent entity for the following day, which will reflect the increased gas prices as calculated based on the methodology set forth in section 39.7.1.1.1.3.

The ISO will include the applicable price increase threshold that must be met to trigger the additional flexibility under the requested waiver in the ISO's business practice manual for market instruments. The ISO proposes to commence with a price increase threshold that will trigger if the ICE prices published at or about10:00 a.m. equal or exceed 150 percent of the price index calculated the previous evening under the normal tariff methodology.[24] The ISO believes this amount of a price increase represents a reasonable initial trigger as it is analogous to the cost of fuel exceeding the maximum start-up and minimum load cost values that can be registered in the master file for a resource that has elected the registered cost option, *i.e.*, 150 percent of the projected proxy cost.

In normal circumstances, the ISO will go through a stakeholder process in order to modify the threshold to be set forth in the business practice manual.[25] However, if emergency circumstances require it, the ISO may promptly and unilaterally revise the threshold. Any revisions the ISO may make to the business practice manual in such circumstances will promptly be announced in a market notice and be subject to stakeholder review either beforehand or subsequently.[26]

B. The Waiver Will Be of Limited Scope

While the ISO requests general waiver of the provisions in sections 30.4.1.2 and 39.7.1.1.1.3, the ISO will apply the additional flexibility granted by the waiver only in the limited circumstances when the daily gas prices published by ICE exceed by a significant margin the gas price index calculated the night before. Also, this waiver will be for a discrete period, through April 30, 2014, in

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[24] *See supra* note 10 and accompanying text.

[25] *See* tariff sections 22.4.3, 22.11.

[26] See tariff sections 22.4.3, 22.11.1.7; business practice manual for business practice manual change management at section 2.6.

order to provide the ISO and stakeholders sufficient safeguards during the balance of the winter and early spring when there is a greater risk of gas price spikes.

The ISO plans to commence a stakeholder process in April to address the issues raised by the gas market conditions and to more comprehensively develop interim and permanent tariff solutions.[27] The ISO expects that the stakeholder process will require at least several months to complete but is committed to developing an interim solution that can be implemented in the fall if such solutions do not require substantial system changes. While the ISO does not have any preconceived ideas about what permanent solution may finally be reached, the ISO anticipates that stakeholders may propose a variety of solutions and such potential solutions may have different components.[28] Any solution resulting from the stakeholder process will be submitted to the ISO Governing Board for approval, and then the ISO will file any tariff revisions required to implement that solution for Commission acceptance.

C. The Waiver Will Address a Concrete Problem that Needs to Be Remedied

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[27] The ISO originally contemplated beginning the stakeholder process in the fall but now believes it should start sooner.

[28] For example, some stakeholders may wish to suggest that the permanent solution include tariff provisions to allow resources to recover penalty costs for violating natural gas pipeline balancing orders and costs of emissions of nitrogen oxide (NOx) and sulfur oxide (SOx) as part of the bid cost recovery mechanism under the tariff. The ISO originally proposed to include such tariff provisions in its 2013 tariff amendment to include additional categories of costs eligible for inclusion in proxy cost calculations for start-up and minimum load, generated bids, and variable cost default energy bids, but the ISO subsequently deferred that proposal because it required further consideration and development. *See* transmittal letter for ISO tariff amendment, Docket No. ER13-2296-000, at 4-5 (Aug. 30, 2013).

As discussed above, the approximately 300 percent spike in natural gas prices in early February caused certain disparities in resource commitment which led to the possible under-recovery of natural gas-related costs by resources participating in the ISO markets. Cost recovery is a fundamental principle of the ISO market. Granting the requested waiver will enable the ISO to take necessary measures to reflect more accurate fuel costs in its dispatch and compensate resources accordingly in the event of a significant increase in near-term natural gas prices.

In a comparable recent situation, the Commission found that good cause existed to grant requests for waiver filed by the New York Independent System Operator, Inc. ("NYISO") and PJM Interconnection ("PJM") of their tariff provisions setting a bid cap of $1,000/MWh.[29] In response to spikes in natural gas costs caused by recent extreme cold weather in the northeast, the NYISO and PJM requested that the Commission grant a temporary waiver to allow generators to recover demonstrated costs that they actually incur to operate, should those costs exceed the $1,000/MWh bid restriction.[30] The Commission explained that granting the NYISO's request for waiver "addresses the concrete problem that generators might be required to provide service to support reliability but without being able to recoup the incremental operating costs that they incur, which would discourage generators from offering service at a time when they are

[29] *New York Independent System Operator, Inc.*, 146 FERC ¶ 61,061 ("*NYISO*"); *PJM Interconnection, LLC*, 146 ¶ 61,041 (2014) ("*PJM*").

[30] *NYISO* at P 1; *PJM* at P 3.

needed."[31] Similarly, in *PJM*, the Commission explained that waiver was necessary in order to "address the reliability concerns posed by the extreme weather currently being experienced in the PJM Region and maintain confidence in market operations."[32] Likewise, granting the ISO's request for waiver will enhance the ability of generators to recoup their start-up and minimum load costs and thus will encourage generators to offer service into the ISO market. In addition, by helping to prevent market inefficiencies caused by natural gas price spikes, this waiver will increase confidence in ISO market operations.

D. The Waiver Will Not Have Undesirable Consequences

No undesirable consequences will result from approving this waiver petition. The ISO recognizes that the temporary solution proposed herein may result in increased payments to generators for bid cost recovery when natural gas prices spike, which may ultimately increase the costs paid by load. However, it is appropriate that generators are compensated for their production and marginal costs based on the most up-to-date gas prices during atypical events, and doing so will help to ensure continued reliable electric service in the ISO market. In the NYISO waiver order discussed above, the Commission found that, "although granting waiver may result in increased costs to load and increased cost to certain market participants if generators incur verifiable actual energy production costs above $1,000/MWh, we find that it is appropriate to

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31 *NYISO* at P 20.

32 *PJM* at P 5.

allow generators to recover such costs in this exigent circumstance."[33] Similarly, the Commission should find that possible increases in start-up and minimum load costs and energy costs are not an undesirable consequence that should preclude granting this ISO request for waiver.

The waiver also does not require the adoption of additional rates, terms and conditions because the settlement impact of the use of the updated indices will flow through the ISO's existing settlement authority for bid cost recovery, exceptional dispatch and residual imbalance energy.[34]

IV. Stakeholder Process for Limited Waiver Request

On February 20, 2014, the ISO issued a market notice announcing that it would issue a technical bulletin and hold a stakeholder conference call regarding these issues and the ISO's request for limited tariff waiver. The technical bulletin was issued on February 21. It describes the ISO proposal set forth in this filing.

On the stakeholder conference call held on February 27, while a number of stakeholders expressed concerns that the proposed waiver did not go far enough to address all their concerns with the ISO's current market structure for incorporating such costs, the vast majority of stakeholders represented that they did not oppose the ISO seeking this waiver. Stakeholders also requested that the ISO consider certain modifications to its original proposal, which the ISO will adopt if the present waiver is granted.

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[33] *New York Independent System Operator, Inc.*, 146 FERC ¶ 61,061, at P 20.

[34] *See* tariff sections 11.8, 11.5.6, and 11.5.5, respectively.

First, the stakeholders requested that the ISO should permit resources to be able to remain subject to the registered cost option even if they are able to switch to the proxy cost option on a day that the ISO observes a natural gas price spike and implements its procedures to use the more up-to-date index in calculating the gas prices. To accommodate this change, the ISO modified its proposal to include the voluntary list of resources that will switch from the registered cost option to the proxy cost option and switch back if the circumstances discussed above arise.

Second, stakeholders requested a firm commitment to commence a stakeholder process to develop more permanent solutions to the issues posed by the gas price spikes. The ISO agreed and in response commits to commencing the stakeholder process in April with the expectation that it will be able to develop a more complete solution by the fall of this year. Further, the winter season will end in April. Consequently, the ISO is only asking for the waiver to apply until April 30. The ISO expects that any changes that require significant software enhancements, however, will not be able to be implemented until later in 2015.

One stakeholder suggested that the procedures discussed herein should be triggered not only when gas prices increase by a significant percentage, but also when they decline by the same amount. It is not necessary, however, to have in place similar mechanisms to address sudden price declines because the ISO tariff allows customers to bid in commitment costs, so long as those costs do not exceed the applicable cap (based on the proxy cost or registered cost option). Therefore, resources already have the ability to reflect downward price adjustments in their commitment costs.

V. Request for Shortened Comment Period and Expedited Commission Action by March 19, 2014

The ISO respectfully requests that the Commission act expeditiously and issue an order no later than March 19, 2014 that prospectively grants this waiver petition effective as of the date of the order. To permit the timely issuance of the order, the ISO also requests that the Commission shorten the comment period on this filing to no more than 7 calendar days. As explained above, the ISO is also requesting that the Commission issue an order granting the limited companion waiver by tomorrow, March 7.

Commission action within this time frame will allow the ISO to implement in a timely manner the special procedures discussed above for ensuring adequate cost recovery and preventing future market inefficiencies similar to those that occurred in December and the first two months of 2014. The risk of a recurrence of these conditions is most significant during the winter/spring season that ends in April. Commission action as soon as possible prior to March 19 is necessary to minimize this risk. In addition, shortening the time for filing comments on this petition is also appropriate because interested parties have already had the opportunity, through the ISO's stakeholder process described above, to review and provide input on the ISO's proposal.

VI. Service

The ISO has served copies of this filing upon the California Public Utilities Commission and all parties with effective scheduling coordinator service agreements under the ISO tariff. In addition, the ISO has posted this filing on its website.

VII. Correspondence

The ISO requests that all correspondence, pleadings and other communications concerning this filing be served upon the following:

Roger E. Collanton
General Counsel
Anna McKenna
Assistant General Counsel
Sidney Davies
Assistant General Counsel

California Independent System
Operator Corporation
250 Outcropping Way
Folsom, CA 95630
Tel: (916) 351-4400
Fax: (916) 351-4436
E-mail: amckenna@caiso.com
sdavies@caiso.com

Michael Kunselman
Bradley R. Miliauskas
Alston & Bird LLP
The Atlantic Building
950 F Street, NW
Washington, DC 20004
Tel: (202) 239-3300
Fax: (202) 239-3333
E-mail:
michael.kunselman@alston.com
bradley.miliauskas@alston.com

VIII. Conclusion

The ISO respectfully requests that the Commission grant a limited waiver until April 30, 2014 of provisions in tariff sections 30.4.1.2 and 39.7.1.1.1.3, as discussed above. The ISO also respectfully requests that the Commission shorten to the greatest extent possible any comment period on this petition, so that it may issue an order by March 19, 2014 that prospectively grants the requested waiver from the date of the order.

Respectfully submitted,

Roger E. Collanton
General Counsel

Anna A. McKenna
Assistant General Counsel
Sidney Davies
Assistant General Counsel
California Independent System
Operator Corporation
250 Outcropping Way
Folsom, CA 95630

Michael Kunselman
Bradley R. Miliauskas
Alston & Bird LLP
The Atlantic Building
950 F Street, NW
Washington, DC 20004

Counsel for the California Independent System Operator Corporation

Dated: March 6, 2014