



March 26, 2009

The Honorable Kimberly D. Bose
Secretary
Federal Energy Regulatory Commission
888 First Street, NE
Washington, DC 20426

**Re: California Independent System Operator Corporation
Docket No. ER08-73-____
Compliance Filing**

Dear Secretary Bose:

In compliance with the Commission order issued in this docket on February 24, 2009, 126 FERC ¶ 61,165 (2009) ("February 24 Order"), the California Independent System Operator Corporation ("ISO") respectfully submits for filing an original and five copies of the enclosed modifications to the CAISO Tariff.¹ The ISO is also tendering two copies of this filing to be time and date stamped and returned to our courier.

I. Background

On October 19, 2007, the ISO filed an amendment to its MRTU Tariff ("SU-ML Cap Amendment") to provide limits to Start-Up and Minimum Load Costs for suppliers that are eligible to recover such Costs in accordance with the Registered Cost option, as set forth in Section 30.4 of the MRTU Tariff. As the ISO explained in the transmittal letter accompanying the filing, it proposed adding these limits in order to protect against the potential exercise of market power by suppliers through the submission of extremely high Start-Up and Minimum Load Costs, particularly in resource-constrained areas of the ISO grid.

The ISO's proposal consisted of two levels of caps, based on whether a unit is located in a Local Capacity Area ("LCA"). For those units within LCAs, Start-Up and Minimum Load Costs under the Registered Cost option may not exceed 200 percent of the unit's projected Start-Up and Minimum Load Costs. For units outside of LCAs, Start-Up and Minimum Load Costs under the Registered Cost option may not exceed 400 percent of the unit's projected Start-Up and Minimum Load Costs. In the SU-ML Cap Amendment, the ISO explained

¹ Capitalized terms not otherwise defined herein have the meanings set forth in the CAISO Tariff, also referred to as the Market Redesign and Technology Upgrade ("MRTU") Tariff.

that it would determine gas prices used in calculating caps based on the highest price for monthly gas contracts at Henry Hub over a forward-looking six-month period. Also, in order to address concerns expressed by generators that caps under the Registered Cost option could increase the risk that price spikes in the spot market for gas could cause their actual Start-Up or Minimum Load Costs to exceed their Registered Costs, the ISO proposed that in the event that daily spot market gas prices increase to the point where a unit's Start-Up or Minimum Load Costs (calculated based on daily spot market gas prices) exceed the amount registered in the Master File under the Registered Cost option, units will have the option to switch to the Proxy Cost option. If a unit elects to switch, then it will remain under the Proxy Cost option for the remainder of the six-month period.

In an order issued in this proceeding on June 20, 2008,² the Commission accepted the SU-ML Cap Amendment, subject to two modifications. First, although the Commission accepted the ISO's proposal to develop the Projected Proxy Cost based on monthly gas contracts over a forward-looking six-month period at the time the bid is submitted, the Commission found that natural gas futures contracts with the delivery point at Henry Hub are not sufficiently representative of natural gas prices in California, and therefore directed the ISO to modify its proposal "to incorporate a more geographically appropriate index" for use in determining projected future gas prices to be used in applying caps under the Registered Cost option.³ Also, with respect to the definition of Projected Proxy Cost, the Commission found that the explanation and the methodology derivation need to be clear in the MRTU Tariff, and directed the ISO to revise the MRTU Tariff accordingly.⁴

On July 21, 2008, the ISO submitted a compliance filing along with a request for clarification or, in the alternative, rehearing of the June 20 Order. In its request for clarification/rehearing, the ISO explained that it was impossible to comply with what it understood to be the Commission's explicit directive to determine gas costs for the caps using a transparent gas futures index for California delivery points because, to the best of the ISO's knowledge, no such index exists. Therefore, the ISO requested that the Commission permit it to use Henry Hub gas prices to calculate the Start-Up and Minimum Load Cost caps, as proposed in its original filing and to which no party objected. However, the ISO also stated that if the Commission was not inclined to allow the ISO to determine gas costs as originally proposed, an alternative solution would be to incorporate into its methodology daily prices for "basis swaps," representing the differential between prices for monthly contracts at Henry Hub compared to final settlement prices for month-ahead gas contracts at various delivery points in California. The ISO noted that this was not its preferred approach because of concerns with

² *California Independent System Operator Corp.*, 123 FERC ¶ 61,288 (2008) ("June 20 Order").

³ *Id.* at P 37.

⁴ *Id.* at P 38.

respect to the robustness and liquidity of the basis swap markets, as well as the public availability of such data.

In the February 24 Order, the Commission recognized that there is no physical futures product for western delivery points of natural gas equivalent to Henry Hub, but nevertheless found that it would be unjust and unreasonable to use the unmodified Henry Hub gas prices to calculate the Start-Up and Minimum Load Cost caps, and directed the ISO to submit a revised proposal for determining a geographically appropriate proxy cost for gas. The Commission also analyzed the ISO's basis-swap alternative, and determined that the basis swap market in California, used in conjunction with Henry Hub futures contract prices, was representative of natural gas prices in California and sufficiently liquid and transparent for use in calculating Start-Up and Minimum Load Cost caps. Although the Commission indicated that it was not endorsing a specific approach or mandating that the ISO calculate gas costs using basis swap data, the Commission stated that it saw "merit in a methodology that derives a projected proxy cost of gas using basis swaps to obtain a more geographically indicative benchmark."⁵

II. Tariff Revisions to Comply with the February 24 Order

Consistent with the Commission's directives in the February 24 Order, the ISO has developed a revised proposal for determining a "geographically appropriate" proxy cost of gas used in calculating Start-Up and Minimum Load Cost bid caps for suppliers that are eligible to recover such Costs in accordance with the Registered Cost option in Section 30.4 of the MRTU Tariff. The ISO's proposal follows the format of the basis swap alternative that it laid out in its July 21, 2008 request for clarification/rehearing and which the Commission found to have merit in the February 24 Order.

Specifically, the ISO is proposing the following revised methodology to determine proxy gas costs for use in calculating Start-Up and Minimum Load Cost caps for resources receiving such costs under the Registered Cost option. As with the original proposal, the ISO will calculate a gas price to be used in establishing maximum Start-Up Costs and Minimum Load Costs after the twenty-first day of each month. The relevant posted price will be the posted price at the time of a Scheduling Coordinator's election to utilize the Registered Cost option.⁶

⁵ February 24 Order at P 34.

⁶ The result of this timeframe is that the specific gas prices used in calculating Start-Up and Minimum Load Cost caps for resources electing the Registered Cost option will be dependent on when a resource makes such an election. If a resource makes this election on or prior to the twenty-first day of each month, then the proxy gas cost will be based on gas prices from the previous month, whereas if the election is made after the twenty-first day of the month, then the proxy gas cost will be based on gas prices from the current month.

First, the daily closing prices for monthly New York Mercantile Exchange (“NYMEX”) Natural Gas Futures contracts at Henry Hub for each of the next six monthly contracts will be averaged over the first twenty-one days of the month, resulting in a separate average for each of the six monthly contracts. This portion of the process is unchanged from the ISO’s original proposal.

Second, daily prices for NYMEX futures contracts for basis swaps at identified geographically appropriate California delivery points will be averaged over the first twenty-one days of the month, resulting in separate averages for each of the six monthly contracts for those geographically appropriate delivery points as set forth in a Business Practice Manual (“BPM”).⁷ These daily prices are expressed as the differential between prices for monthly contracts at Henry Hub compared to final settlement prices for month-ahead gas contracts at the identified California delivery points. The ISO chose to utilize NYMEX basis swap data for California instead of data from Intercontinental Exchange (“ICE”) because NYMEX data are publically available on the Internet, while a special contractual arrangement would be necessary to obtain the ICE data.⁸ Given the Commission’s finding that the NYMEX data is sufficiently liquid for use in determining the proxy gas cost for Start-Up and Minimum Load Cost bid caps, the ISO believes that the additional transparency associated with the NYMEX data makes it the better choice.

Next, the average Henry Hub prices will be combined with the average basis swap prices, resulting in an amalgamated price for the identified California delivery points for each of the six monthly contracts. The maximum of these combined averages will then be selected and will represent the baseline gas prices applicable for calculating the Start-Up and Minimum Load Cost caps for resources electing the Registered Cost option, and the most geographically appropriate proxy gas cost will apply to a particular resource. The calculation of separate gas prices for the identified California delivery points will allow for a proxy price that more accurately accounts for geographic variation. This approach is also consistent with the process used by Potomac Economics to determine the Gas Price Index that is used in calculating daily gas prices used in

⁷ As explained in an issue paper the ISO posted on its website on March 13, 2009, which is available at <http://www.caiso.com/2370/23708027307b0.pdf>, the ISO is proposing to utilize two California delivery points as of day one of MRTU: SoCal Border and PG&E Citygate. These are the same delivery points utilized by the ISO and Potomac Economics, Ltd. (“Potomac Economics”) for calculating Default Energy Bids. If the ISO later determines that it is geographically appropriate to designate another California delivery point for use in calculating Start-Up and Minimum Load Cost caps, the ISO will modify the BPM to include the additional delivery point, pursuant to the process contained in the BPM for BPM Change Management.

⁸ The ISO is following up on a comment submitted by Pacific Gas and Electric Company that additional permissions from NYMEX may be required to utilize the NYMEX data as proposed in this filing. The ISO will obtain the necessary permissions and will promptly advise the Commission and parties if it encounters any problems that would require the ISO to modify its proposal.

Default Energy Bids and Generated Bids, as well as Start-Up and Minimum Load Costs for units under the Proxy Cost option.

Finally, the ISO will add the applicable intra-state gas transportation charge to the baseline gas price for each resource that elects the Registered Cost option in order to arrive at a final gas price for calculating the Start-Up and Minimum Load Cost caps for each such resource.⁹ The adders for intra-state gas transportation will set forth in the Business Practice Manual.

Because this new methodology for calculating proxy gas costs is more detailed than the one the ISO originally proposed, the ISO has placed the details regarding this methodology in a new Section 39.6.1.6.1 of the MRTU Tariff rather than in the definition of Projected Proxy Cost. This involves moving some language that, although relating to the calculation of gas proxy costs, was not implicated in the Commission's February 24 Order and therefore has not been substantively modified.¹⁰ The ISO believes that this arrangement is superior from a tariff-organizational standpoint and will make it easier for readers of the MRTU Tariff to follow.

III. Stakeholder Process

Consistent with the Commission's directive in the February 24 Order to consult with stakeholders,¹¹ the ISO has conducted a short stakeholder process in order to give Market Participants the opportunity to review and comment on the ISO's proposed new methodology for determining the gas proxy component of Start-Up and Minimum Load Cost caps for resources under the Registered Cost option. On March 13, 2009, the ISO posted on its website an issue paper describing the new methodology.¹² On March 24, 2009, the ISO conducted a conference call with stakeholders to discuss the proposal. Few stakeholders had comments on the new methodology and no one opposed the approach. Those stakeholders that commented did not raise any concerns about the methodology but instead only asked questions regarding certain implementation details. Therefore, the new methodology seems to have broad support among stakeholders.

⁹ For the SoCal Border and PG&E Citygate, the ISO utilizes the intra-state gas transportation charges set forth in the Southern California Gas Company's and PG&E's respective tariffs.

¹⁰ The ISO has moved the following existing language from the definition of Projected Proxy Cost to new Section 39.6.1.6.1: "For non-gas fired resources, the Projected Proxy Costs for Start-Up Costs and Minimum Load Costs will be calculated using the information in the Master File used for calculating the Proxy Cost as set forth in the Business Practice Manual." The ISO is, therefore, not proposing any changes or offering this language on compliance.

¹¹ February 24 Order at P 35.

¹² See *supra* note 7.

IV. Contents of Filing

In addition to this transmittal letter, the instant compliance filing includes the following attachments:

Attachment A	Clean MRTU Tariff sheets
Attachment B	MRTU Tariff sheets red-lined against provisions of the MRTU Tariff as filed with the Commission in this docket on July 21, 2008

V. Communications

Correspondence and other communications regarding this filing should be directed to the following:

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VI. Effective Date

In the original SU-ML Cap Amendment filing and in the July 21, 2008 compliance filing, the ISO requested waiver of the requirements of the Commission's Order No. 614 in order to make the associated tariff modifications effective as of the date of MRTU implementation. As of the dates it submitted those filings, the ISO was not certain of the date of MRTU implementation, and therefore the ISO did not indicate an effective date on the tariff sheets it filed. In the February 24 Order, the Commission granted the ISO's waiver requests, and directed the ISO to make an informational filing specifying an effective date prior to the implementation of MRTU.¹³ The implementation date of MRTU is now set for March 31, 2009. Therefore, the ISO is requesting an effective date of March 31 for the tariff sheets included in the instant filing. The ISO will also make the required informational filing prior to that date.

¹³ February 24 Order at P 36 n.39.

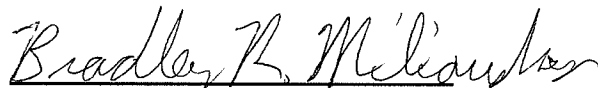
VII. Service

The ISO has served copies of this filing on all parties on the parties listed on the official service list compiled by the Secretary in the above-captioned proceeding, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure.¹⁴

VIII. Conclusion

For the reasons set forth above, the ISO respectfully requests that the Commission accept the instant filing as compliant with the February 24 Order.

Respectfully submitted,



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¹⁴ 18 C.F.R. § 385.2010.

Attachment A – Clean Sheets

Bid Caps for Start-Up Costs and Minimum Load Costs Compliance Filing

4th Replacement MRTU Tariff

March 26, 2009

39.6.1.6.1 Gas Price Component of Projected Proxy Cost

For natural gas fired resources, the CAISO will calculate a gas price to be used in establishing maximum Start-Up Costs and Minimum Load Costs after the twenty-first day of each month and post it on the CAISO Website by the end of each calendar month. The price will be applicable for Scheduling Coordinators electing the Registered Cost option until a new gas price is calculated and posted on the CAISO Website. The gas price will be calculated as follows:

- (1) Daily closing prices for monthly NYMEX Natural Gas Futures contracts at Henry Hub for each of the next six monthly contracts are averaged over the first twenty-one (21) days of the month, resulting in a separate average for each of the six (6) monthly contracts.
- (2) Daily prices for NYMEX futures contracts for basis swaps at identified California delivery points, are averaged over the first twenty-one (21) days of the month, resulting in separate averages for each of the six (6) monthly contracts for the identified California delivery points as set forth in the Business Practice Manual.
- (3) For each of the six (6) monthly contracts, for any California delivery point, the average Henry Hub and basis swap prices are combined.
- (4) The maximum of these combined averages are selected and will be used as the baseline gas price applicable for calculating the caps for Start-Up and Minimum Load costs for resources electing the Registered Cost option. The most geographically appropriate will apply to a particular resource.
- (5) The applicable intra-state gas transportation charge as set forth in the Business Practice Manual will be added to the baseline gas price for each resource that elects the Registered Cost option to create a final gas price for calculating the caps for Start-Up and Minimum Load Costs for each such resource.

For non-gas fired resources, the Projected Proxy Costs for Start-Up Costs and Minimum Load Costs will be calculated using the information contained in the Master File used for calculating the Proxy Cost, as set forth in the Business Practice Manual.

Prior Period Change Worksheet	A worksheet prepared by the RMR Owner and submitted to the CAISO following discovery of a necessary change to an RMR Invoice after the Revised Adjusted RMR Invoice for the billing month has been issued.
Projected Proxy Cost	A calculation of a resource's Start-Up Costs and Minimum Load Costs for a prospective six-month period used to determine the maximum Registered Cost for the resource. Projected Proxy Costs will be calculated whenever a Scheduling Coordinator elects the Registered Cost option. For natural gas fired resources, the CAISO will calculate a gas price to be used in calculating maximum Start-Up Costs and Minimum Load Costs as set forth in Section 39.6.1.6.1.
Project Sponsor	A Market Participant, group of Market Participants, a Participating TO or a project developer who is not a Market Participant or Participating TO that proposes the construction of a transmission addition or upgrade in accordance with Section 24.
Proposal for Installation	A written proposal submitted by a CAISO Metered Entity to the CAISO describing a proposal for the installation of additional Metering Facilities.

Attachment B – Blacklines

Bid Caps for Start-Up Costs and Minimum Load Costs Compliance Filing

4th Replacement MRTU Tariff

March 26, 2009

39.6.1.6.1 Fuel Cost Component of Projected Proxy Cost.

For natural gas fired resources, the CAISO will calculate a gas price to be used in establishing maximum Start-Up Costs and Minimum Load Costs after the twenty-first day of each month and post it on the CAISO Website by the end of each calendar month. The price will be applicable for Scheduling Coordinators electing the Registered Cost option until a new gas price is calculated and posted on the CAISO Website. The gas price will be calculated as follows:

- (1) Daily closing prices for monthly NYMEX Natural Gas Futures contracts at Henry Hub for each of the next six monthly contracts are averaged over the first twenty-one (21) days of the month, resulting in a separate average for each of the six (6) monthly contracts.
- (2) Daily prices for NYMEX futures contracts for basis swaps at identified geographically appropriate California delivery points are averaged over the first twenty-one (21) days of the month, resulting in separate averages for each of the six (6) monthly contracts for the identified geographically appropriate California delivery points as set forth in the Business Practice Manual.
- (3) For each of the six (6) monthly contracts, for any identified geographically appropriate California delivery point, the average Henry Hub and basis swap prices are combined.
- (4) The maximum of these combined averages are selected and will be used as the baseline gas price applicable for calculating the caps for Start-Up and Minimum Load costs for resources electing the Registered Cost option. The most geographically appropriate will apply to a particular resource.
- (5) The applicable intra-state gas transportation charge as set forth in the Business Practice Manual will be added to the baseline gas price for each resource that elects the Registered Cost option to create a final gas price for calculating the caps for Start-Up and Minimum Load Costs for each such resource.

For non-gas fired resources, the Projected Proxy Costs for Start-Up Costs and Minimum Load Costs will be calculated using the information contained in the Master File used for calculating the Proxy Cost, as set forth in the Business Practice Manual.

* * *

CAISO Tariff Appendix A

Master Definitions Supplement

Projected Proxy Cost

A calculation of a resource's Start-Up Costs and Minimum Load Costs for a prospective six-month period used to determine the maximum Registered Cost for the resource. Projected Proxy Costs will be calculated whenever a Scheduling Coordinator elects the Registered Cost option. For natural gas fired resources, the CAISO will calculate a gas price to be used in calculating maximum Start-Up Costs and Minimum Load Costs as set forth in Section 39.6.1.6.1, ~~after the twenty-first day of each month and post it on the CAISO Website by the end of each calendar month. The price will be applicable for the following month until a new gas price is calculated and posted on the CAISO Website. The gas price will be calculated as follows. First, daily closing prices for monthly NYMEX Natural Gas Futures contracts at Henry Hub for each of the next six monthly contracts are averaged over the first twenty one days of the month. A separate average is calculated for each of the six monthly contracts, based on the average closing price of the contract over the first twenty one days. Second, the maximum of the six monthly averages will be calculated and be used as the gas price applicable for calculating Start-Up Bid and Minimum Load Bid caps. For non-gas fired resources, the Projected Proxy Costs for Start-Up Costs and Minimum Load Costs will be calculated using the information contained in the Master File used for calculating the Proxy Cost, as set forth in the Business Practice Manual.~~