

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Duke Energy Trading and Marketing Co.) Docket No. EL03-152-000

**PETITION FOR REHEARING OF THE
CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

Pursuant to Rule 713 of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission (“Commission”), 18 C.F.R. § 385.713 (2004) and Section 313(a) of the Federal Power Act, 16 U.S.C. § 825I (a), the California Independent System Operator Corporation (“CAISO”) hereby requests rehearing of the Order Approving Contested Settlement issued in this proceeding on September 21, 2004, 108 FERC ¶¶ 61,259 (2004). The Settlement Agreement approved in the September 21 Order resolved issues related to Duke Energy Trading and Marketing Company that were set for hearing in the Commission’s Order to Show Cause Concerning Gaming and/or Anomalous Market Behavior in this docket, 103 FERC ¶¶ 61,345 (2003), *reh’g denied*, 106 FERC ¶¶ 61,020 (2004) (the “Gaming Show Cause Order”). However, the Settlement Agreement left for Commission resolution one issue – whether the ISO Tariff requires that the amount of capacity sold as Replacement Reserve remain unloaded at all times except when dispatched by the CAISO. 108 FERC ¶¶ 61,259 at P 3. The Commission found that the CAISO Tariff does not require that capacity sold as Replacement Reserve remain unloaded at all times except when dispatched by the CAISO. *Id.* at P 12. The CAISO respectfully requests

rehearing of this determination because it misinterprets the CAISO Tariff and is contrary to Commission precedent.

I. Specifications of Error

The Commission erred in determining that the CAISO Tariff does not require Replacement Reserve to remain unloaded at all times except when dispatched by the CAISO.

II. Argument

A. Contrary to the Commission's Finding, the CAISO Tariff Requires Replacement Reserve to Remain Unloaded at All Times Except When Dispatched By the CAISO.

The CAISO Tariff clearly provides that a Scheduling Coordinator must ensure that Replacement Reserve remain unloaded until dispatched by the CAISO. Section 2.5.26.2.1 of the CAISO Tariff provides:

If the ISO determines that a Scheduling Coordinator has supplied Uninstructed Imbalance Energy to the ISO during a Settlement Period from the capacity of a Generating Unit or System Resource that is obligated to supply Spinning Reserve, Non-Spinning Reserve, or Replacement Reserve to the ISO during such Settlement Period, payments to the Scheduling Coordinator representing the Generating Unit or System Resource for the Ancillary Service capacity used to supply Uninstructed Imbalance Energy and for Energy supplied from such capacity shall be eliminated to the extent of the deficiency, except to the extent (i) the deficiency in the availability of Ancillary Service capacity from the Generating Unit or System Resource is attributable to control exercised by the ISO in that Settlement Period through AGC operation, an RMR Dispatch Notice, or dispatch to avoid an intervention in Market operations or to prevent a System Emergency; or (ii) a penalty is imposed under Section 2.5.26.1 with respect to the deficiency.

In other words, a unit cannot sell any Ancillary Service, including Replacement Reserve unless the capacity remains unloaded.¹ The reliability rationale for this position is clear. The CAISO operators must be able to count on Replacement Reserve as being in the mix of available resources in the event of an emergency. If instead, that capacity is already loaded and simply converting from a bilateral sale to providing the contracted for reserves, the operators will not receive the expected injection of additional Energy into the grid, which could cause a decrease in Operating Reserve Margin.²

¹ In addition, the CAISO Tariff defines Ancillary Services to include Replacement Reserve. See Master Definition Supplement, Appendix A to the ISO Tariff. Ancillary Services are defined as”

Regulation, Spinning Reserve, Non-Spinning Reserve, *Replacement Reserve*, Voltage Support, and Black Start together with such other interconnected services as the ISO may develop in cooperation with Market Participants to support the transmission of Energy from Generation resources to Loads while maintaining reliable operation of the ISO Controlled Grid in accordance with Good Utility Practice.

Emphasis added. See also *San Diego Gas & Elec. Co. v. Sellers of Energy etc.*, 105 FERC ¶ 61,066 at P 49 (2003) (“Replacement Reserves are an ancillary service involving capacity that is dedicated to the CAISO.”). Section 2.5.21 of the CAISO Tariff provides that Ancillary Service Schedules “represent binding commitments made in the markets between the ISO and the Scheduling Coordinator concerned.” Moreover, the CAISO Scheduling Protocol provides that the CAISO will make payment only for capacity that is “made available.” CAISO Scheduling Protocol, Sections 9.6.2, 9.7.2, 9.8.2.

² If Replacement Reserve is loaded without instruction, the CAISO will need to reduce output at other facilities to balance the system. While output from units on Automatic Generation Control (“AGC”) that are providing Regulation service can be reduced for short intervals, the CAISO would need to promptly instruct other resources to reduce output so that the regulating range of resources on AGC can be maintained. If the CAISO were required to instruct a combustion turbine to shut down, or to move a steam unit to its lower operating range, then it may take longer than 60 minutes (the response time for Replacement Reserve) for these units to return to their original operating levels. This is because operating constraints such as minimum shut down time or the time required to add a boiler feed water pump may exceed 60 minutes. The CAISO may then be faced with dispatching Spinning or Non-Spinning Reserve to meet the Energy requirement that cannot be fulfilled by units that are constrained off or constrained down. The end result may be the CAISO has a lower Operating Reserve margin as a direct result of the uninstructed deviation on Replacement Reserve capacity.

In the September 21 Order, the Commission concluded that the CAISO Tariff does not require Replacement Reserve to remain unloaded based on a comparison of the Tariff's definition of Replacement Reserve with the definition of Spinning Reserves. In that regard, the Commission stated that “[w]hile the CAISO Tariff requires that Spinning Reserves be unloaded and capable of being immediately responsive to CAISO dispatch, the definition of Replacement Reserve does not state that this capacity must be unloaded.” 108 FERC ¶ 61,259 at P 14. The Commission erroneously concluded that the CAISO intended that Spinning Reserves and Replacement Reserve be treated differently under the CAISO Tariff with respect to the obligation to remain unloaded because the word “unloaded” is not used in the Replacement Reserve definition. The lack of the mere word “unloaded” in the definition of Replacement Reserve definition does not justify this interpretation. Although the definition of Replacement Reserve does not specifically require that such reserves must remain unloaded until they are dispatched by the CAISO, Section 2.5.26.2.1 of the ISO Tariff (quoted above) -- which applies to Replacement Reserve -- confirms that Replacement Reserve is required to remain unloaded.

B. The Commission's Conclusion Also Is Contrary To Prior Commission Rulings

The Commission's ruling that Replacement Reserve does not have to remain unloaded also is contrary to prior Commission rulings. It is axiomatic that an agency must conform to its prior practice, policy and decisions or explain the reasons for its departure from such precedent. See *United Municipal Distributors Group v. FERC*, 732 F.2d 202, 210 (D.C. Cir. 1984); *Greater Boston Television Corporation v. FCC*, 444 F.2d 841, 852 (D.C. Cir.), *cert. denied*, 403 U.S. 923 (1971) (agency must give reasoned

analysis for departures from prior agency practice). The Commission has failed to conform to this mandate.

In its February 9, 1999 order accepting the CAISO's Amendment No. 13, the Commission affirmed the obligation of Scheduling Coordinators to hold capacity sold as Ancillary Services in reserve. *California Independent System Operator Corp.*, 86 FERC ¶ 61,122 (1999). In that order, the Commission explained that:

Currently, when Ancillary Service providers are selected by the ISO, they are paid a capacity charge for holding their generating resource in reserve and an energy charge to the extent the ISO directs them to produce energy, e.g., when operating reserves are called upon. The ISO states that Ancillary Service providers currently have incentives to violate their obligation to hold their generating resource in reserve and, instead, produce energy. Under the ISO Tariff, unscheduled generation that is delivered to the ISO is compensated at the market clearing price for imbalances. When the imbalance energy involves the output of an Ancillary Service provider, the generator is paid twice (the Ancillary Service capacity charge and the energy imbalance energy charge) and *the ISO is exposed to reliability risks because it expected the generating resources to be held in reserve*. According to the ISO, if a generator produces energy using capacity already committed to the ISO as reserves for Ancillary Services, such capacity is not available for dispatch by the ISO. The ISO contends that this behavior can cause operational difficulties, can raise costs, and can cause a violation of WSCC and NERC policies.

Id. at 61,418 (emphasis added).

The Commission went on to conclude:

We believe that the ISO's proposal to withhold both payments when an Ancillary Service provider fails to honor its commitment to remain unloaded until directed by the ISO is reasonable. Withholding the energy imbalance payment removes the economic incentive for Ancillary Service providers to violate their obligations, while removing the compensation for Ancillary Services that were not provided as promised, creates a strong incentive for generators to honor their obligations.

Id. Thus, the Commission eliminated both the capacity payment and the energy payment when Ancillary Services are loaded with uninstructed deviations. The Commission adopted this position because Ancillary Services suppliers should honor their obligations. Because Replacement Reserve is an Ancillary Service, the Commission necessarily recognized in its order on Amendment 13 that Replacement Reserve must remain unloaded in order for the seller to be compensated.

In the Gaming Show Cause Order, the Commission also confirmed the requirement that Replacement Reserve must remain unloaded until dispatched by the CAISO. In its comments on the Duke settlement, the CAISO made the Commission aware of that fact. Specifically, in the Gaming Show Cause Order, the Commission defined Double Selling of Ancillary Services as “selling ancillary services in the day-ahead market from resources that were initially available, but later selling those same resources as energy in the hour-ahead or real-time markets.” Gaming Show Cause Order at P 50. The Commission explained that “the market participant misled the CAISO by selling capacity that it had already committed to reserve as ancillary services, thus making that capacity no longer available in real time if the CAISO were to call upon that resource to provide ancillary services.” *Id.* at P 51. The Commission also found that the practice of Double Selling violated Section 2.5.22.11 of the CAISO Tariff which requires that resources that have been committed to provide ancillary services for a given period must be available and capable of providing the services for the full duration of the period. *Id.* The Commission did not carve out an exception for Replacement Reserve or any other type of Ancillary Service. The September 21 Order does not explain the departure from past orders for treating Replacement Reserve different than

all of the other Ancillary Services in this respect. Given that Replacement Reserve is an Ancillary Service under the CAISO Tariff, the provisions of Section 2.5.22.11 necessarily must apply to Replacement Reserve.

Neither the CAISO Tariff nor any Commission order carves out an exception to the obligation to keep capacity unloaded with respect to Replacement Reserve. As with all other types of Ancillary Services, the CAISO has full authority and discretion in determining how the capacity that the CAISO has purchased shall be dispatched. As the Commission stated in the Amendment No. 13 Order, the failure of suppliers to hold the capacity committed in reserve exposes the CAISO to reliability risks because the CAISO expects that this capacity will be available when needed. This is no less true for capacity committed as Replacement Reserve. For this reason, the Commission must grant rehearing and reverse its finding that the CAISO Tariff does not require that Replacement Reserve remain unloaded at all times except when dispatched by the CAISO.

III. Conclusion

For the foregoing reasons, the CAISO respectfully requests that the Commission grant rehearing with respect to the conclusion in the September 21 Order that the CAISO Tariff does not require that Replacement Reserve remain unloaded at all times except when dispatched by the CAISO.

Respectfully submitted,

/s Anthony J. Ivancovich

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Dated: October 21, 2004

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the service list compiled by the Secretary in this proceeding.

Dated at Folsom, CA this 21st day of October, 2004.

Is Anthony J. Ivancovich
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October 21, 2004

The Honorable Magalie Roman Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, DC 20426

**Re: Duke Energy Trading and Marketing Co.
Docket Nos. EL03-152-000**

Dear Secretary Salas:

Enclosed please find an electronic filing of the Petition for Rehearing of the California Independent System Operator Corporation. Thank you for your attention to this filing.

Respectfully submitted,

/s/ Anthony J. Ivancovich
Anthony J. Ivancovich

Counsel for the California Independent
System Operator Corporation