

ISO MARKET SURVEILLANCE PROGRAM

A. COMMISSION'S ORDERS

In its October 30, 1997, Order Conditionally Authorizing Limited Operations of the ISO and PX ("October 30 Order"), the Commission approved in all its essential details the joint Market Power Monitoring Plan for the ISO and PX, filed as Appendix 7 to the ISO Tariff on March 31, 1997, as required in its December 18, 1996 Order¹ at 62,087. However, the Commission ordered that the joint "plan" for the ISO and PX monitoring programs be converted into separate, permanent monitoring programs for each of the ISO and PX to be in place and effective by the commencement of operations.² In anticipation of and in response to this requirement, each of the ISO and PX developed detailed market monitoring or surveillance protocols filed with the Commission along with the other ISO and PX protocols for informational purposes on October 31, 1997.³

In its October 30 Order, the Commission also required certain amendments or revisions to, and the inclusion of certain features in, each of the ISO and PX plans.⁴ These required changes were reflected in the ISO and PX protocols, as filed on October 31 and subsequently revised to reflect Commission-required changes and posted on the WEnet prior to the commencement of operations, as also required by the Commission.⁵ These required changes are addressed in this Compliance Filing.

By operations date, on March 31, 1998, both the ISO and PX had staffed their internal monitoring or compliance units, duly supported by external consulting and legal expertise, and had appointed their external market monitoring committees, all of which were operative in implementing the program required by the Commission.

In addition to the approval of and certain changes required in the monitoring plan filed by the ISO and PX, as implemented in these protocols, the Commission also added certain features to these programs that emanated from certain proposals of the Companies for the mitigation of market power in the transition periods pending the divestitures of generation units that they had undertaken and pending the end of the CTC recovery/retail rate freeze.⁶ These required additions are also addressed in this compliance filing.

¹ 77 FERC ¶ 61,265 at 62,0871.

² 81 FERC ¶ 61,122 at 61,552. The ISO describes the function as "market surveillance," to be carried out by a dedicated Market Surveillance Unit within the ISO organization. Similarly, the monitoring function of the PX is carried out by a dedicated internal Compliance Unit.

³ For the ISO, the Market Monitoring and Information Protocol ("MMIP").

⁴ 81 FERC at 61,522-54. As is self-evident, these "plans" are now replaced by operating protocols.

⁵ *Id.* at 61,552.

⁶ *Id.* at 61,537-48.

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B. STEADY STATE MONITORING PROGRAM: COMPLIANCE CHANGES

In the permanent or steady state monitoring program proposed by the ISO, and conditionally accepted by the Commission, the following changes or inclusions have been made or confirmed:

Changes Ordered

(All references are to Commission's
October 30 Order)

1. Include Protocol in tariffs. Order at 61,552.
2. Coordination between ISO and PX monitoring units. Order at 61,552.
3. ISO Market Surveillance Unit to monitor for and provide input to Commission on structural issues. Order at 61,552.
4. ISO to receive and pursue complaints. Order at 61,553.

Compliance

(All references are to MMIP)

1. MMIP is part of Appendix L to the ISO Tariff.
2. Broad ranging coordination and cooperation with PX Compliance Unit and Market Monitoring Committee authorized in MMIP Section 4.7. In implementation of this section, the monitoring units of each of the ISO and PX have attended Committee meetings of the other and joint meetings with the CPUC's market power team; and numerous exchanges of data and analysis have occurred.
3. MMIP 2.1.5 requires monitoring of and input to Commission on market structure flaws.
4. MMIP 3.3.5 authorizes receipt and pursuance of complaints by Market Surveillance Unit. In implementation, Market Surveillance Unit has established a confidential "hotline" on its web page for the receipt of complaints and has developed specific procedures for the systematic processing of complaints.

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| <p>5. ISO to develop through experience of operation a “detailed description of the monitoring standards and criteria.” Order at 61,552.</p> | <p>5. The detailed "criteria and standards" required by the Commission would provide the basis for defining offenses and taking action against Market Participants (whether by imposing some penalty, sanction or other disciplinary action; or by referring matters to the Commission, the Department of Justice or other pertinent regulatory or antitrust enforcement agency). In light of the serious use to which these criteria and standards will be put, they will need to be developed with great care and on the basis of considerably more experience in operating and monitoring the markets administered by the ISO than has been gained to date. Moreover, these criteria and standards cannot be meaningfully applied to Market Participants until the penalties and sanctions that will accompany the definition of offences have been developed and approved by the Commission. Again considerable care and attention is being paid to the development of penalties and sanctions in order to address potential concerns of the Commission and of stakeholders. The criteria and standards and the penalties and sanctions will be filed with the Commission as soon as sufficient operating experience is gained to develop them effectively.</p> |
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C. COMPANIES’ MITIGATION MEASURES FOR TRANSITION PERIODS

The Commission has defined the “mitigation measures” that the monitoring programs of the ISO and PX may need to undertake during the predivestiture and CTC recovery/retail rate freeze transitions addressed in the Companies’ Market-Based Rate Proposals.⁷

⁷ 81 FERC at 61,546-67.

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Mitigation Ordered

(All references are to Commission's October 30 Order)

1. ISO (and PX) to monitor for below-cost bidding to accelerate recovery of stranded costs through the CTC. Order at 61,547.

2. The ISO is directed "to file availability standards with the Commission as part of the mitigation proposal as soon as practicable." Order at 61,546. Further, the ISO is required "to develop *pro forma* availability standards applicable to all Market Participants as a necessary component of [its] sanctions proposal." Order at 61,554.

3. The ISO is directed to develop and file with the Commission *pro forma* bid caps "as soon as practicable." Order at 61,546.

Compliance

1. Since the principal market in which the below-cost bidding may occur is the Energy market administered by the PX, the monitoring function is to be carried out by the PX Compliance Unit. The ISO understands that the PX has developed, and is implementing, a reporting requirement for the Companies in order to carry out this monitoring function.

2. Considerable analysis has been undertaken on the development of effective availability standards. Meaningful availability standards designed to identify the strategic withholding of capacity to force prices to rise can only be developed after at least the experience of one summer peak season in which periods of high load and high prices and the incentive to abuse market power are most likely to occur. Hence, the ISO will develop availability standards to be used in monitoring and, as directed by the Commission, included as a necessary component of the ISO penalties and sanctions proposal when finalized, after sufficient experience of the 1998 summer seasonal peak.

3. The Commission imposed this requirement on the ISO and the PX explicitly in response to the Companies' proposed mitigation measures.

While the rationale for the Commission's general instruction to the ISO and PX to develop *pro forma* bid caps during the

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pre-divestiture transition is rapidly dissipating because of the Companies' divestitures, the ISO has in fact put in place specific price caps for each of the three markets that it administers for all generator participants – the Real Time Imbalance Energy Market, the Ancillary Service Capacity Markets and the Congestion Management Market.

The details of, and rationale for, these caps, are as follows:

Market	Price Cap	Rationale
Real Time Energy Market	\$250/MWh	A cap on the maximum energy bid to be used in the Imbalance Energy Market. Put in place to mitigate a problem in the real time dispatch software (BEEP). The current BEEP software can issue dispatch instructions for more units than operators can physically call in each 10 minute interval. Because the software calculates 10 minute prices based on bids called on by the operators, when extreme under-generation conditions exist, the software can set artificially high prices. The cap was put in place to mitigate this problem and will be removed once this aspect of the software is fixed.
Ancillary Service Capacity Markets	FERC Jurisdictional Caps (vary by IOU and Ancillary Service Type)	
Congestion Management	\$250/MW	A Default Usage Charge (DUC) used when the ISO has insufficient incremental and decremental adjustment bids and must make pro rata adjustments to relieve congestion.