California ISO
Your Link to Power

California Independent
System Operator Corporation

Memorandum

To: ISO Board of Governors

From: Nancy Saracino, Vice President, General Counsel and Corporate Secretary

Date: October 21, 2009

Re: **Regulatory Update**

This memorandum does not require Board action.

Federal Energy Regulatory Commission (FERC) matters and related decisions of the Court of Appeals

Tariff amendment filings and orders

- **Generator interconnection procedure amendments (ER08-1317 and ER09-1722)**

On September 17, 2009, FERC issued an order accepting the ISO's compliance filing for its generator interconnection procedure reform (GIPR) tariff amendment filed in docket ER08-1317. The GIPR modified the interconnection procedure from a queue approach, where projects are studied serially, to a cluster study approach, where groups of projects are studied together. The GIPR also put into place performance timelines, including requirements for interconnection customers to post financial security and certain development milestones. The ISO filed a tariff amendment on September 18, 2009 in docket number ER09-1722 to modify the financial security requirements. The amendment reduces the initial financial security requirement for generators in the queue and spreads the timeline for providing further financial security over the life of the project.

Responsible Attorney: Bill Di Capo

- **Real-time energy neutrality offset amendment (ER09-1781)**

On September 30, 2009, the ISO submitted a tariff amendment to exempt load and exports of load following metered subsystem operators from the allocation of the real-time imbalance energy neutrality offset adjustment. The ISO requested an effective date of October 1, 2009, and waiver of the sixty-day notice requirement. The real-time imbalance energy offset is a neutrality adjustment -- either a charge or a payment to demand -- based on whether the ISO has sufficient revenue from real-time demand market charges to compensate supply procured in the real-time market, which includes the hour ahead scheduling process (HASP). If revenues are insufficient, the ISO must charge demand. If revenues exceed the amount needed to pay supply, the ISO returns the excess to load serving entities based on their demand. Pending the development of a longer term approach on how to reduce the extent of the imbalance offset or to allocate the offset in a manner that better aligns with cost causation principles, the ISO identified the need to exempt MSS load following demand (including exports) from the offset adjustment.

Responsible Attorney: Anna McKenna

- **Modification of rule limiting supply bids in the integrated forward market (ER10-28)**

On October 2, 2009, the ISO filed a tariff amendment to eliminate the rule that limited the bids that could be considered in the integrated forward market. As originally filed, the tariff only permitted bids from resources that were committed through the local market power mitigation process to be considered by the integrated forward market. This rule reduced the availability of bids from resources, thereby resulting in market inefficiency and potentially higher costs, particularly when bid-in demand exceeds the ISO's demand forecast. This tariff amendment will allow the integrated forward market to consider all bids.

Responsible Attorney: Sidney Davies

- **Standard capacity product and ancillary services must offer obligation (ER09-1064)**

On September 16, the ISO filed an answer to the comments and protests on the standard capacity product compliance filing. In its answer, the ISO disagreed with suggestions to: 1) eliminate the monthly report requirement for hours in which a resource was prohibited from bidding on out-of-service transmission paths; 2) modify the tolerance band to provide availability incentive payments to resource adequacy imports and internal resource adequacy resources that either exceed the monthly availability standard by 2.5 percent or that are 100 percent available, whichever is less; and 3) eliminate part of the formula for calculating a resource's availability.

Responsible Attorneys: Beth Ann Burns, Anthony Ivancovich

- **Integrated Balancing Authority Area (IBAA) tariff amendment (ER08-1113)**

FERC's July 30, 2009 order on rehearing upheld the IBAA structure as a single hub as well as the default pricing proposal for imports and exports between IBAAs and the ISO. The order also affirmed the opportunity for parties to obtain alternative pricing if they share data under a market efficiency enhancement agreement to demonstrate the operation and location of their external resources supporting interchange transactions. On August 20, 2009, FERC held a technical conference to address the remaining compliance issues in this matter. The conference focused on the following issues: 1) the ISO's information requirements to model and calculate locational marginal prices under a market efficiency enhancement agreement; 2) the availability of that information; and 3) the ISO's procedures and information requirements to verify the location and operation of resources identified in a market efficiency enhancement agreement in order to determine applicable prices for interchange transactions subject to the agreement. The ISO and various parties submitted comments and reply comments regarding the issues discussed at the technical conference on

September 15 and 22, respectively. Additionally, on September 30, the ISO submitted a filing to comply with the directives in the June 30 order regarding the losses adjustments for certain import and export schedules. Finally, the following parties filed petitions for review of FERC's July 30, 2009 and September 19, 2008 orders in the United States Court of Appeals for the District of Columbia Circuit: Sacramento Municipal Utility District, Modesto Irrigation District, Turlock Irrigation District, the Transmission Agency of Northern California, the City of Redding and the City of Santa Clara.

Responsible Attorneys: Anna McKenna, Andrew Ulmer

- **Exceptional dispatch tariff amendment (ER08-1178)**

On September 2, 2009, FERC issued an order accepting the ISO's pending compliance filing subject to modification. The subject of that compliance filing related to the ISO's exceptional dispatch reporting requirements relating primarily to the details required in the ISO's monthly reports. Although it accepted the ISO's prior reports, FERC directed that, on a prospective basis, the ISO file specific details for each exceptional dispatch in a given reporting period on two different charts, the latter to include settlement data, and to ensure that the second chart identified the same exceptional dispatches identified on the first chart by reference number. The September 2 order also required the ISO to continue to file reports every 120 days that summarize the ISO's efforts to reduce reliance on exceptional dispatch including potential software and market product enhancements developed through discussions with stakeholders. On September 14, 2009, the ISO filed a motion for extension of time for the September monthly exceptional dispatch report and a motion for clarification regarding the monthly reporting requirements. With respect to the latter motion, the ISO requested clarification that details required for the first chart that would not be available in time to be included could be included on the second chart. In addition the ISO sought clarification that the reporting period could be changed to be consistent with ISO settlements, *i.e.* on a calendar month basis rather than on a 30 day period beginning on the 16th of every month. On October 2, 2009, the ISO made two additional filings—a filing in compliance with the September 2 order and a request for clarification or, in the alternative, rehearing. The latter filing requested rehearing of the clarifications issues raised in the ISO's September 14 motion as well as clarification or rehearing that the exceptional dispatch information posted on OASIS is consistent with the exceptional dispatch information included in the monthly reports.

Responsible Attorney: Sidney Davies

- **Market parameters tariff amendment (ER09-240**

On March 17, 2009, the California Department of Water Resources State Water Project filed a request for rehearing of FERC's February 19, 2009 order conditionally accepting the ISO's proposed tariff revisions to relax the extent to which the ISO's market clearing software must literally exhaust all economic bids before engaging in any adjustments to submitted self-schedules. The State Water Project had argued that the February 19 order fails to ensure accurate day-ahead ISO schedules and is otherwise procedurally and substantively erroneous. In its September 17, 2009 order, FERC rejected the State Water Project's arguments and denied its request for rehearing.

Responsible Attorney: Anna McKenna

- **New market issues tariff amendments (ER09-1529)**

On July 31, 2009, the ISO filed tariff revisions to implement changes regarding: 1) recovery of start-up and minimum load costs; 2) financial settlements of congestion revenue rights; and 3) the locational marginal price of an electrically disconnected pricing node. The ISO filed these clarifications to align operational outcomes with actual costs and to avoid the market or settlement distortions that became apparent under the ISO's new market design. On September 29, 2009, FERC issued an order accepting these changes effective as of August 1, 2009.

Responsible Attorneys: Anna McKenna and Sidney Davies

- **Tariff clarifications regarding regulatory must-take generation and enforcement of transmission constraints (ER09-1542)**

On October 2, 2009, FERC issued an order conditionally accepting tariff revisions to clarify: 1) that generating units located outside the ISO's balancing authority area can be treated as regulatory must-take generation under the tariff; and 2) the relationship between the full network model and the enforcement of transmission constraints. The order also requires the ISO to conduct a stakeholder process to consider what additional visibility can be provided with respect to the ISO's transmission constraint enforcement and operator practices to account for system conditions in managing the limits of the transmission system. In this stakeholder process, the ISO will consider ways in which it can provide more information on constraint enforcement and will develop guidelines for its constraint management process. FERC directed the ISO to file tariff sheets setting forth those principles that significantly affect rates, terms or conditions within 90 days.

Responsible Attorneys: Anna McKenna and Sidney Davies

- **Reference Bus Tariff Amendment (ER09-240)**

On August 4, 2009, FERC issued an order accepting tariff revisions, subject to modification, that allow the ISO the flexibility to use a distributed generation reference bus in calculating the marginal cost of energy in cases where the integrated forward market cannot clear using a distributed load reference bus. In addition, the order also requires the ISO to add specific language to its tariff that will require the ISO to notify market participants when a distributed reference bus is utilized. The order also requires the ISO to post on its website an informational report detailing the nodal pricing ramifications whenever a distributed generation reference bus is utilized. On September 3, 2009, the ISO submitted its compliance filing. Also on September 2, 2009, the ISO filed a request for clarification or in the alternative rehearing regarding these reporting requirements. While the ISO does not object to posting the requested comparative cost information to the extent that the ISO actually is able to obtain such information, the August 4 order appears to presume that ISO will always be able to obtain the comparative cost information when the integrated forward market fails using the distributed load reference bus. This presumption is not correct because the integrated forward market may fail using the distributed load reference bus for reasons not immediately obvious, or that may never be known. The ISO requests clarification that in the event that the ISO cannot successfully re-run the integrated forward market using the distributed load reference bus within ninety days it is not required to post comparative cost data.

Responsible Attorney: Anna McKenna

- **Miscellaneous tariff clarifications-simplified ramping (ER09-556 et al)**

FERC accepted the ISO's motion to modify the effective date of tariff revisions to implement simplified ramping from October 1, 2009 to November 5, 2009. Simplified ramping will allow the ISO to utilize the operational ramp rate rather than the regulation ramp rate when dispatching resources. On October 15, 2009, the ISO filed a status report indicating that it was on track to implement simplified ramping on November 5, 2009.

Responsible Attorney: Sidney Davies

- **Access to ISO non-public operating procedures (ER06-615; ER08-367)**

On August 7, 2009, FERC issued an order on compliance conditionally accepting the ISO's proposed tariff language addressing access to ISO non-public operating procedures. The ISO had proposed to limit access to entities that are operationally affected by the ISO non-public operating procedure subject to agreed-upon controls. The order affirms that the ISO may restrict access to non-public operating procedures if the requesting entity is only economically or financially impacted by the procedure. On October 15, 2009, FERC accepted the tariff language submitted by the ISO in compliance with the August 7, 2009 order.

Responsible Attorneys: Andrew Ulmer

- **Payment acceleration tariff amendment (ER09-1247 and ER09-1744)**

On September 17, FERC issued an order in docket number ER09-1247 that found the ISO's proposed payment acceleration program to be just reasonable. FERC based its decision on the ground that the payment acceleration program should lower the market's credit exposure and reduce the financial security requirements that market participants must meet. The order approved all major features of the ISO's proposal effective as of November 1 subject to certain modifications specifically to: 1) explain the process for determining metered demand if a scheduling coordinator doesn't submit meter data by the specified deadline; 2) extend the application of interest to the end of the 36-month settlement process; 3) provide a timeline to resolve settlement statement disputes; and 4) make other minor clarifications. On October 19, 2009, the ISO submitted a compliance filing to implement these changes. On September 25, the ISO filed a further tariff amendment in docket number ER09-1744 to modify the payment acceleration program to resolve a settlement imbalance issue discovered during the dry run namely that charges for congestion revenue rights and the participating intermittent resource program that have historically had a monthly settlement netting element would not settle on a neutral basis due to the switch from monthly to semi-monthly invoicing. The filing proposed modifications so that these charges will be calculated on a daily basis and then reconciled on a monthly basis in order to assure neutrality. The ISO requested that FERC accept these modifications effective as of November 1.

Responsible Attorney: Beth Ann Burns

- **Reduction in unsecured credit limit (ER09-1681)**

As part of the payment acceleration program, the ISO committed to a further reduction in unsecured credit from $150 million to $50 million. On September 4, 2009, the ISO filed the necessary tariff language to reduce the maximum unsecured credit limit to $50 million effective as of January 5, 2010, the last day of cash clearing under the prior payment schedule. The ISO filed an answer to comments and protests on October 13, 2009 arguing that the unsecured limit should not remain at $150 million due to higher credit requirements that may be imposed for congestion revenue rights auctions.

Responsible Attorney: Sidney Davies

Regulatory contracts filings and orders

- **SMUD Interconnected Control Area Operating Agreement (ICAOA) amendment no. 5 and California-Oregon Intertie (COI) Control Area Operating Agreement amendment no. 1 (ER09-1577; ER09-1578)**

On October 13, 2009, FERC issued an order accepting the ISO's filings of amendment no. 5 to its ICAOA with SMUD and amendment no. 1 to its COI Control Area Operating Agreement with SMUD. The ISO had originally filed these amendments on August 12, 2009 and had filed revisions to these amendments on September 3, 2009. The revisions to these amendments implemented a minor modification agreed upon by the ISO and SMUD to their percentage obligations for power flow reduction measures that may be required by the path operator for the COI and any sanctions that may be imposed on the path operator for the COI for operation of the COI.

Responsible Attorney: Mike Dozier

Report filings

- **Market Disruption reports (ER06-615)**

On September 15, and October 15, 2009 the ISO submitted its monthly market disruption reports. A market disruption is an action or event that causes a failure of an ISO market, related to system operation issues or System Emergencies. Section 7.7.15 of the tariff authorizes the ISO to take one or more of a number of specified actions in the event of a market disruption, to prevent a market disruption, or to minimize the extent of a market disruption. In the October report, the ISO reported that for the time period of August 15 to September 15, 2009, there were a total of 44 market disruptions, which was slightly higher than the 40 market disruptions listed in the September 2009 Report. The ISO also reported that no reportable events occurred in the day-ahead market and that the ISO did not remove any bids (including self-schedules) during the reporting period. The ISO reported that, compared to the September 2009 report, the number of hour ahead scheduling process failures increased by three. The number of real-time dispatch failures decreased slightly from 24 to 18. On average, there was less than one real time dispatch (RTD) failure per day. Most of the RTD failures were due to software variance, bid processing issues, or the software application timing out.

Responsible Attorney: Anna McKenna

- **Exceptional dispatch reports (ER08-1178)**

On September 29, and October 15, 2009, the ISO submitted its monthly exceptional dispatch reports. Pursuant to the September 14 motion for extension of time and clarification, the September 29, and October, 15 report provided details concerning exceptional dispatches occurring during the months of July and August 2009, respectively. Details include data, incremental and decremental MW volume, duration, local reliability area (if applicable), and reason for exceptional dispatches.

Responsible Attorney: Sidney Davies

- **120-Day Exceptional dispatch report (ER08-1178)**

As directed by FERC in its September 2 order, the ISO filed its second 120 day report summarizing its efforts to reduce reliance on exceptional dispatch. The ISO has substantially reduced the frequency of exceptional dispatches issued prior to the day-ahead market by enforcing certain capacity based nomograms in the residual unit commitment process. Another recent operational enhancement is the development of a more automated approach for dealing with compensating injections. The ISO believes that this will reduce frequency of real-time exceptional dispatches. The ISO also believes that future operational enhancements, such as simplified ramping, multi-stage generator modeling, incorporation of additional constraints in the day-ahead market, reduction in market disruptions (such as failures of the hour ahead scheduling process and real-time dispatch), will further reduce frequency of exceptional dispatch. For the long term, the ISO believes that transmission upgrades and the development of a multi-day commitment will further reduce exceptional dispatch. The ISO has conducted two exceptional dispatch workshops and will schedule more in the future. These workshops will allow the ISO and stakeholders to discuss operational issues and the potential need for new products to reduce exceptional dispatch. To date, the ISO has not identified a particular product that would be needed and believes that full year of data is needed so that all seasonal issues can be identified and planned operational improvements can be implemented before determining whether a new product is necessary.

Responsible Attorney: Sidney Davies

- **Negotiated default energy bid report (ER06-615)**

On October 7, 2009, the ISO filed, on a confidential basis, default energy bids that went in to effect or were modified in the prior month. Specifically, there were 11 new, and eight modified, negotiated default energy bids that went into effect in September 2009. Default energy bids are used in the local market power mitigation process.

Responsible Attorney: Sidney Davies

Complaint proceedings

- **Default Loss Rule Complaint (EL09-62)**

On September 23, 2009, FERC issued an order in response to the June 30, 2009 complaint filed by certain sellers of electricity in the ISO markets contending that Section 11.29.17.1 of the ISO tariff -- the default loss allocation rule -- is unjust and unreasonable. The default loss rule allocates losses from defaults on payments due the ISO to net creditors in a given settlement period. The complainants requested that FERC adopt a rule which allocates the default risk among all market participants that benefit from the ISO's markets on a strict absolute value basis. The September 23 order found that the ISO's default loss allocation tariff provisions were not just and reasonable but that sellers had not demonstrated that their alternative approach was just and reasonable. Accordingly, FERC set the matter for hearing pending settlement judge procedures. The ISO participated in the first settlement conference held on October 14, 2009.

Responsible Attorney: Sidney Davies

Rulemakings and policy statements

- **Request for comments on transmission planning (AD09-8-000)**

FERC issued a request for comments on October 8, 2009 concerning its Order 890 transmission planning process that builds upon the three regional technical conferences held in September 2009. The ISO actively participated on panels at the technical conference in Phoenix. FERC is requesting comments on two general topics: 1) enhancing regional transmission planning processes; and 2) allocating the cost of transmission. The ISO will file its comments on November 9, 2009.

Responsible Attorney: Judi Sanders

- **Green Energy Express Incentive Rate Filing (EL09-74)**

On September 6, Green Energy Express, LLC filed a petition for a declaratory order requesting FERC approval of certain rate incentives for the proposed Green Energy Express Transmission Line. On October 6, the ISO filed comments on the incentive rate filing. The ISO requested that FERC either wait to act on the petition until after the ISO has completed all applicable actions under its transmission planning process or confirm that the FERC's grant of some or all of the incentives requested in the petition does not, in any way, pre-judge the outcomes of the ISO planning process. The ISO also requested that FERC clarify that the costs to develop proposed transmission projects that are not constructed because they are not approved in the ISO planning process should not be entitled to "abandoned plant" cost recovery if the reason the project is not constructed is because the ISO found the project is not needed.

Responsible Attorney: Anthony Ivancovich

Other proceedings

- **Petition for limited waiver of tariff provision (ER10-32)**

On October 5, 2009, the ISO filed a limited waiver of tariff provisions that impose "penalty" points on metered subsystem operators when their day-ahead schedules are below the ISO demand forecast or their own metered demand data. The Cities of Riverside and Vernon accrued 11 and 10 points, respectively in April, 2009, the first month of the ISO's new market design. Once a metered subsystem operator accrues 20 points in any 12 month period, it will be subject to residual unit commitment cost allocation. Both cities provided substantial and credible evidence that the penalty points accrued in April should be waived. Accordingly, the ISO filed the waiver request.

Responsible Attorney: Sidney Davies

- **New Market Design Appeals (Court of Appeals, Case No. 07-1208)**

On October 2, 2009, the ISO filed a brief supporting FERC concerning appeals of FERC orders approving the ISO's new market redesign. Four petitioners – Sacramento Municipal Utility District, San Diego Gas & Electric Company, the City and County of San Francisco, and the Imperial Irrigation District – challenged FERC's approval of certain features of the new market. The challenged features include marginal losses, the assessment of losses to holders of Transmission Ownership Rights, the use of load aggregation points, the amount of credit for the use of contractual transmission rights to satisfy local capacity requirements, the historical reference period for the allocation of congestion revenue rights (CRRs), and the issuance of only "obligation" type CRRs without also offering "option" type CRRs. The ISO's brief was also signed by Pacific Gas & Electric Company, Southern California Edison, several NRG affiliates, and D.C. Energy. The petitioners' reply briefs are due November 2. The Court is expected to hear the matter early next year, although no date has yet been set for oral argument.

Responsible Attorneys: Roger Collanton and Dan Shonkwiler

<u>California Public Utilities Commission (CPUC) matters</u>

Rulemaking relating to the safety of electric utility facilities (R.08-11-005)

The CPUC has initiated phase 2 of its rulemaking addressing the issue of whether to revise and clarify regulations relating to the safety of electric utility and communications infrastructure provider facilities. Among other issues under consideration is whether the CPUC should extend inspection and maintenance rules for distribution facilities to transmission facilities under the ISO's operational control. The ISO attended the CPUC's prehearing conference in this matter held on October 9, 2009, and intends to participate as a party in the proceeding.

Responsible Attorney: Andrew Ulmer

Southern California Edison Company's certificate of public convenience and necessity for Devers-Palo Verde No. 2 transmission project (A.05-04-015)

On September 28, 2009, the CPUC administrative law judge issued a proposed decision that would approve Southern California Edison's construction of the California-only portion of this project, subject to certain conditions, including the ISO's further approval of that construction. On October 19, 2009, the ISO submitted comments describing the conditions that would have to be satisfied in order for the ISO to approve the construction of specified components of the California portion of the project and requested a clarification of the proposed decision regarding the ISO's approval process for the California-only portion of the project. The ISO's comments and request for clarification were based on the revised description of the project set forth in Southern California Edison Company's amended petition for modification filed on September 2, 2008, as revised pursuant to its letter to the CPUC dated May 15, 2009.

Responsible Attorney: Mike Dozier

Ruling on smart grid and the Energy Independence and Security Act of 2007 (R.08-12-009)

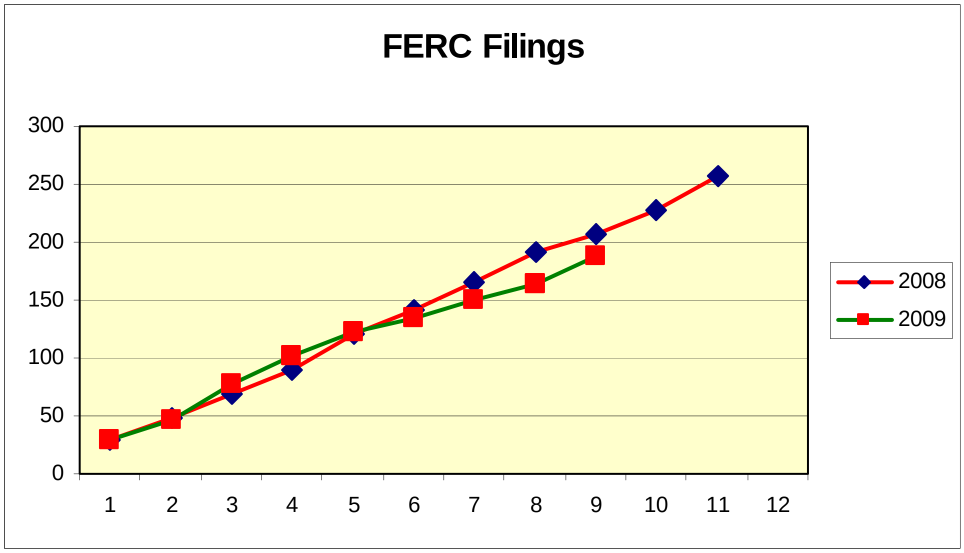
On September 28, 2009, the CPUC released a proposed ruling in its smart grid proceeding addressing issues raised by the Energy Independence and Security Act of 2007 (EISA). The proposed ruling addresses five issues the CPUC believes it is required to consider under EISA. The five issues are whether a utility:

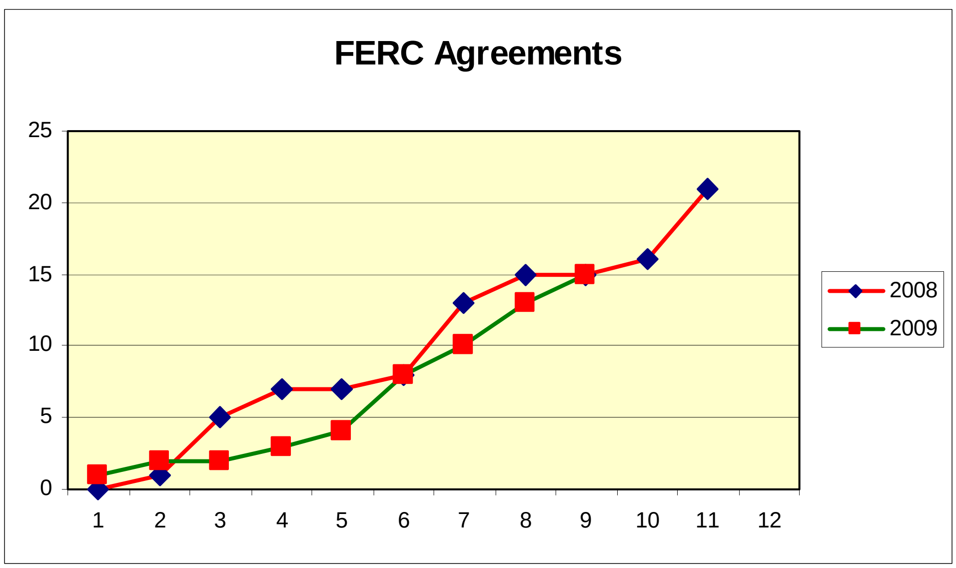
1. should be required to demonstrate that it considered a smart grid investment before it makes any grid investment.
2. should be allowed to recover any costs (including a reasonable rate of return) relating to the deployment of a qualified smart grid system.
3. that deploys a qualified smart grid system should recover the book value of equipment rendered obsolete by the deployment of that smart grid system.
4. should be required to provide customers with daily information regarding their energy usage (including retail and wholesale prices) and with annual information concerning the utility's sources of generation and associated greenhouse gas emissions.
5. must provide customers with access to their information at any time through the Internet and must provide any interested person aggregated usage information.

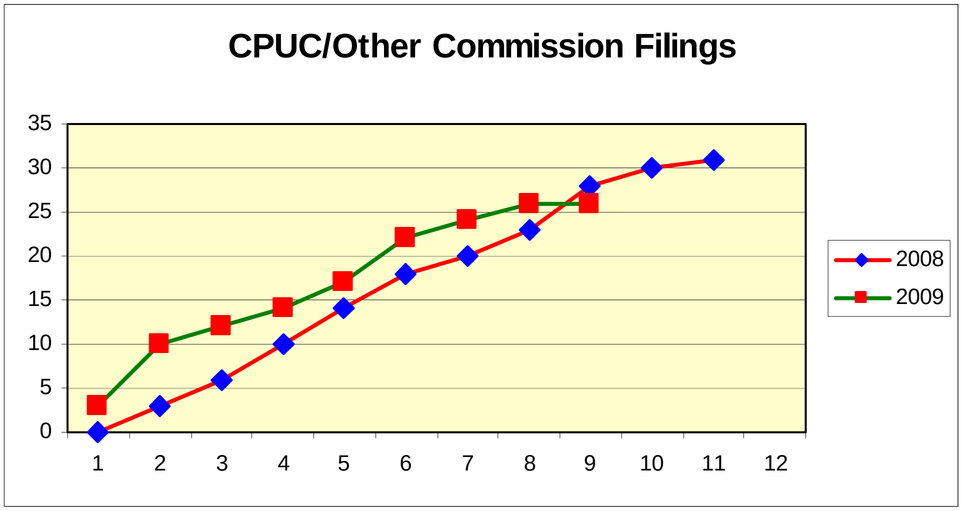
The proposed ruling answers all five questions in the negative, either because the proposed standard could be counter-productive or because there are better ways to address the issue.

Responsible Attorney: David Zlotlow

Regulatory Filings
September 2009 Charts






CPUC/Other Commission Filings
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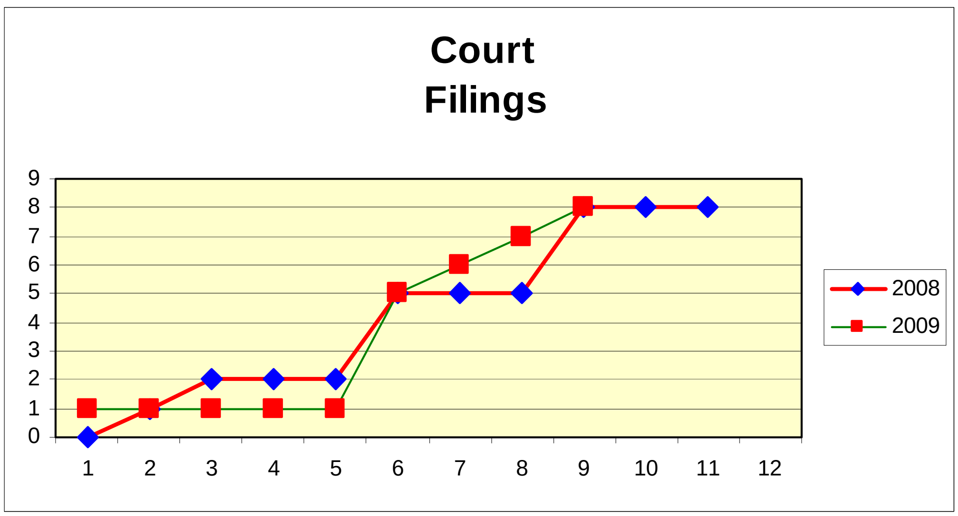
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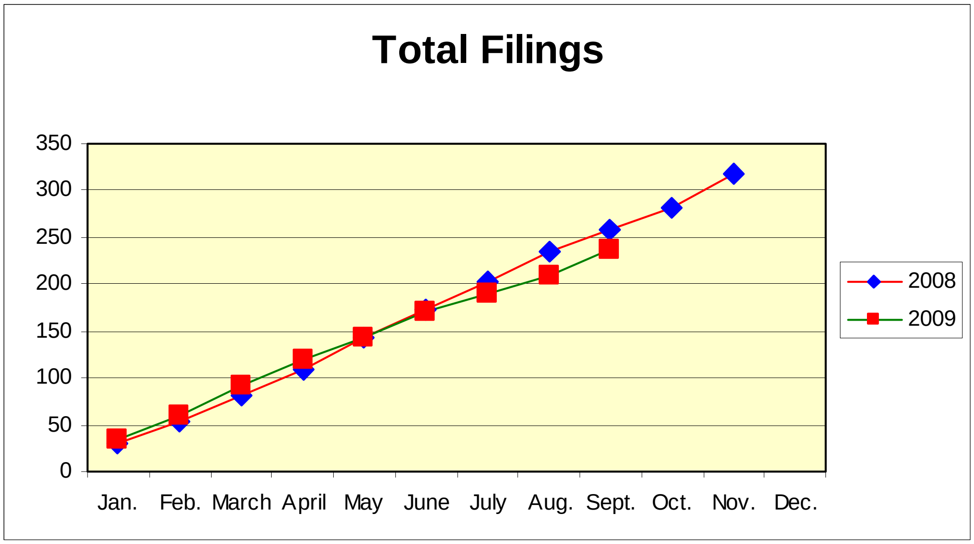
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