

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

**Removing Obstacles To Increased)
Electric Generation And Natural Gas) Docket No. EL01-47-001
Supply In The Western United States)**

**COMMENTS OF THE CALIFORNIA INDEPENDENT SYSTEM
OPERATOR CORPORATION CONCERNING ORDER REMOVING
OBSTACLES TO INCREASED ELECTRIC GENERATION AND
NATURAL GAS SUPPLY IN THE WESTERN UNITED STATES AND
REQUESTING COMMENTS ON FURTHER ACTIONS TO INCREASE
ENERGY SUPPLY AND DECREASE ENERGY CONSUMPTION**

I. INTRODUCTION AND SUMMARY

On March 14, 2001, the Commission issued, in the above-referenced docket, its Order Removing Obstacles to Increased Electric Generation and Natural Gas Supply In the Western United States and Requesting Comments On Further Actions to Increase Energy Supply and Decrease Energy Consumption.¹ The Commission stated that in light of the severe electric energy shortages facing California, it had examined all of its rate and facility certification authorities to determine how it can help increase the supply of electric energy. In proposing specific actions, the Commission recognized that the actions will not, by themselves, solve the electricity crisis in the West or prevent electricity blackouts this summer. However, the Commission wants to elicit whatever additional supply there is from existing resources.² The Commission also noted that in

¹ 94 FERC ¶ 61,272 ("March 14 Order"). Capitalized terms not otherwise defined herein are used in the sense given in the Master Definitions Supplement, Appendix A to the ISO Tariff.

² *Id.* at 61,967.

working on medium and longer term solutions to avert future supply shortages, its efforts can only address part of the supply picture and that “State regulators, not this Commission, have siting authority for electric generation and transmission facilities, as well as for natural gas local distribution facilities.”³

The Commission proposed, among other things, a number of actions within its authority to address the problems of transmission constraints, generation inadequacy, and inadequate demand-side response.⁴ Briefly, these actions include the following:

- Having the ISO and transmission owners in the Western Systems Coordinating Council (“WSCC”) prepare and file, for informational purposes, a list of projects that can be implemented in the shortest period of time. Such projects are those that do not present siting and acquisition of rights of way issues and could include, e.g., reconfiguring or reconductoring of existing transmission lines;
- Offering premiums on the return on equity and shorter depreciation periods for projects associated with new facility interconnections and other projects that can be implemented quickly;
- Extending temporary waivers of operating and efficiency standards for Qualifying Facilities (“QFs”) through December 31, 2001 throughout the WSCC;
- Adopting streamlined regulatory procedures and approvals to accommodate wholesale sales for businesses with on-site generation that is used primarily for back-up or self-generation;
- Allowing wholesale and retail customers, as permitted by state laws and regulations, to reduce consumption for the purpose of reselling their load reduction at wholesale; and
- Exploring the possibility of granting relief, consistent with environmental protection, from certain operating restraints at hydroelectric facilities throughout the WSCC.

³ March 14 Order at 61,967.

⁴ See *id.* at 61,968-73.

The California Independent System Operator Corporation (“ISO”) is to file its list of grid enhancements within 30 days of the issuance of the March 14 Order.⁵

In the March 14 Order, the Commission stated that it sought “the views of industry participants, organizations, and state regulatory authorities on the actions and proposals identified herein, and on what other measures the Commission and others could take to assist in improving the supply/demand balance in California and elsewhere in the West.”⁶ The ISO greatly appreciates the Commission’s concern regarding supply adequacy in the West and the initiatives proposed in the March 14 Order. Pursuant to the March 14 Order, the ISO hereby submits its comments on the matters described above.

II. TRANSMISSION

The ISO fully supports the Commission’s goal of expediting the development and construction of critical new transmission capacity in the West. As the Commission has long recognized, there is a necessary and appropriate delineation of responsibilities between the Commission and state authorities regarding the approval and siting of new transmission facilities. To date the Commission has appropriately focused on those measures it could take to create further incentives for new transmission, such as increased rates of return for transmission-owning entities and, in certain cases, market-based rates for specific transmission projects. We urge the Commission to continue to focus on such initiatives. At the state level, state authorities have and will continue to

⁵ *Id.* at 61,968-69.

oversee the siting of new transmission facilities. State authorities, consistent with their statutory obligations, focus on and must establish the “need” for a project and must address such issues as impact on the environment, impact on communities, routing, and other issues of particular concern to the citizens of the state. It is in this forum where a convergence of state and federal objectives first occurs.

The ISO’s determination of “need” for a transmission project, as established under the ISO Tariff, is often the basis for establishing “need” in the Certificate of Public Convenience and Necessity (“CPC&N”) proceedings of the California Public Utility Commission (“CPUC”) regarding proposed transmission projects. As the ISO, the Commission, and the state move forward to address the many and varied problems facing the California electricity market, the ISO believes that, collectively, all parties must identify new and innovative methodologies for supporting new transmission investment. The ISO is convinced that both the Commission and the State of California are of one mind on this matter.

Over the next several months, the ISO and Market Participants in California intend to examine and develop policies that will ensure that the ISO Controlled Grid is expanded in a manner to ensure access to low cost supplies for California consumers and to support competitive regional electricity markets. Specifically, the ISO and Market Participants will explore policies to expand the transmission system not only to satisfy reliability criteria, but also to ensure access to critical new supplies and markets and to, if necessary, mitigate the

⁶ *Id.* at 61,977.

exercise of locational market power in certain constrained areas of the ISO Controlled Grid. As explained further below, the CPUC has initiated a proceeding to begin exploring these methodologies and matters for purposes of establishing “need” in its own CPC&N proceedings. As the ISO and Market Participants develop and prepare to file proposed changes to the grid expansion and planning processes contained in the ISO Tariff, we urge the Commission to remain open to new methodologies for supporting grid expansion and to empower regional organizations with the ability to see that necessary transmission facilities get built.

A. There Are a Number of Efforts Underway In the State of California to Identify Priority Transmission Projects

The ISO will provide the Commission with the list of grid enhancements required by the March 14 Order. Additionally, the ISO will briefly outline the initiatives underway in California to identify and move forward expeditiously with priority transmission projects.

The ISO has worked extensively with the three largest investor-owned utilities (“IOUs”) in California, Pacific Gas and Electric Company (“PG&E”), Southern California Edison Company (“SCE”), and San Diego Gas & Electric Company (“SDG&E”), stakeholders, and California state agencies, including the Electricity Oversight Board (“EOB”), the California Energy Commission (“CEC”), and the CPUC, to identify priority transmission projects. Priority projects have been identified through the annual coordinated planning process, and associated efforts, facilitated by the ISO.

On August 10, 2000, the ISO consolidated information from the planning process and related activities to produce an Action Plan to Accelerate Generation, Transmission and Demand Response in California.⁷ The plan included a list of high priority transmission projects. Since then, the ISO has been working with the utilities, stakeholders, and the state agencies to track implementation of priority projects and to continually reassess and update the list of priority projects.

In addition, in September 2000, the Governor of California signed into law AB 970 which provides, in relevant part:

399.15 Notwithstanding any other provision of law, within 180 days of the effective date of this section, the [California Public Utilities Commission], in consultation with the Independent System Operator, shall take all of the following actions, and shall include the reasonable costs involved in taking those actions in the distribution revenue requirements of utilities regulated by the commission, as appropriate:

(a)(1) Identify and undertake those actions necessary to reduce or remove constraints on the state's existing electrical transmission and distribution system, including, but not limited to, reconductoring of transmission lines, the addition of capacitors to increase voltage, the reinforcement of existing transmission capacity, and the installation of new transformer banks. The commission shall, in consultation with the Independent System Operator, give first priority to those geographical regions where congestion reduces or impedes electrical transmission and supply.

On November 2, 2000, the CPUC initiated an investigation to carry out its mandate in AB 970 (docketed as I00-11-001). The investigation was bifurcated into two phases: phase one, the purpose of which is to focus on projects that could be in place by Summer 2001; and phase two, the purpose of which is to focus on longer term projects.

⁷ See <[http:// www.caiso.com/docs/09003a6080/07/3f/09003a6080073f0f.pdf](http://www.caiso.com/docs/09003a6080/07/3f/09003a6080073f0f.pdf)>.

In compliance with the CPUC's directives, the ISO, PG&E, SCE, and SDG&E filed comments and information related to, among other things, transmission constraints and recommended transmission projects to relieve them. In particular, the ISO identified certain projects as "high priority" projects, and urged the CPUC to move ahead with their development. The CPUC Staff evaluated the filings and performed its own analysis.

On March 27, 2001, in these same proceedings, the CPUC issued a draft "Interim Opinion On Transmission Upgrades Needed for Summer 2001 (Phase 1)." The draft opinion identifies the transmission projects that can be put in place by Summer 2001 to relieve system constraints. In Phase 2, the CPUC intends to address longer term transmission planning issues.

B. The Commission Should Consider Remediating "Phantom Congestion"

The March 14 Order correctly recognizes that "eliminating bottlenecks which prevent maximum utilization of existing supply must be accomplished efficiently and expeditiously."⁸ The ISO concurs fully with this statement. There is one reform within the sole jurisdiction of the Commission that can enhance utilization of the transmission grid without the need for physical modifications: the mitigation or elimination of congestion caused by the ISO's requirement to honor, and reserve transmission capacity associated with, Existing Contracts under the ISO Tariff and previous Commission orders. Existing Contracts often contain scheduling timelines that are different from the ISO's Day-Ahead and Hour-Ahead scheduling timelines. In order to honor these Existing Contracts,

⁸ March 14 Order at 61,969.

transmission capacity is reserved in the ISO's Day-Ahead and Hour-Ahead scheduling processes but often is not used by existing rights-holders. These Existing Contract reservations cause paper or so-called "phantom" congestion. While the ISO can use in real time any transmission capacity that has not been scheduled by existing rights-holders in the Hour-Ahead scheduling process,⁹ the reserved and unused transmission capacity is not available for use by Market Participants in the ISO transmission markets (i.e., the Day-Ahead and Hour-Ahead scheduling processes).

In its Order concerning Amendment No. 27 to the ISO Tariff, the Commission described the problem of phantom congestion within the ISO Controlled Grid:

This term, as explained by the ISO, relates to the scheduling timelines afforded to current G[overnmental] E[ntitie]s under Existing Rights contracts which are different and not entirely compatible with the day-ahead and hour-ahead schedules that the ISO operates under. Because the Existing Rights contracts allow scheduling changes after the ISO scheduling deadlines, available transmission capacity remains unutilized. According to the ISO, an after-the-fact review of actual data from December 1998 to November 1999 indicates that in many days the congestion on contract paths was less than anticipated because the holders of Existing Rights did not fully utilize those rights, but that information was not available in real-time to the ISO to allow the market to respond. Thus, the ISO states that, if there were immediate conversion of Existing Rights to FTRs for new Participating TOs, this "Phantom Congestion" would be eliminated.

A number of GEs argue that: (1) "Phantom Congestion" is a valuable scheduling right of the GEs; (2) the ISO is at fault for failing to develop software to accommodate these rights nor recognize the operational realities of full service utilities; and (3) the requirement that Existing Rights be converted to F[irm] T[ransmission] R[ights] to alleviate the purported "Phantom Congestion" is a step backwards inasmuch as the ISO currently

⁹ See ISO Tariff, Section 2.4.4.5.1.6.

allows a five year conversion period during which time a party to an Existing Contract can become a new Participating TO and continue to exercise their contract rights. Additionally, some GEs have suggested that the appropriate place to deal with this issue may be the stakeholder process now under way in the ISO congestion management program.

We do not agree with the position taken by the GEs. Software that perpetuates the non-conforming schedules will not fix this problem of "Phantom Congestion." We believe that this approach simply suggests an iterative scheduling process that will not allow sufficient time for the market to respond and will leave the ISO with insufficient time to manage the grid reliably. Furthermore, while GEs contend that their scheduling flexibility is a valuable asset, it results in overall market inefficiencies due to scheduling time lines that do not conform to the time lines of the overall markets. It is difficult to justify the scheduling flexibility advantage in light of the congestion these rights cause the ISO.¹⁰

The Commission recognized that phantom congestion was "a market inefficiency that must be addressed and rectified as quickly as possible" and stated that, if the issue was not resolved in the overall settlement negotiations concerning that ISO's transmission Access Charge, the Commission would "address it in a separate proceeding."¹¹

The ISO recognizes the importance the Commission has placed on honoring Existing Contracts and that contract reformation is not to be undertaken absent the most compelling public interest. But, as the Commission properly recognizes, there is an "electricity crisis facing California and the other areas of the West" and the problems in these areas arise, in part, from transmission constraints.¹²

¹⁰ *California Independent System Operator Corporation*, 91 FERC ¶ 61,205 at 61,727 (2000).

¹¹ *Id.*

¹² See March 14 Order at 61,967-68.

Accordingly, the ISO offers the following two options for the Commission's consideration. Under Option 1, the Commission would reform the scheduling timelines of the Existing Contracts of the Participating Transmission Owners so that any service under these agreements would be scheduled with the ISO on a Day-Ahead basis. Thus, any capacity left unscheduled in the Day-Ahead Market would be available to the Hour-Ahead Market.¹³

Option 2 involves the provision of Firm Transmission Rights ("FTRs"). In accordance with Article 9 of the ISO Tariff, the ISO makes FTRs available through periodic auctions. FTRs enable Market Participants to hedge their exposure to Inter-Zonal Congestion costs imposed through Usage Charges. FTRs entitle the holder to receive a share of the Usage charge revenues paid to the ISO. Transmission capacity represented by FTRs that is not scheduled on a Day-Ahead basis is released to the market. Under Option 2, the holders of Existing Contracts would be given FTRs for Inter-Zonal Interfaces commensurate with their pre-existing capacity reservations. These FTRs would entail the same rights and obligations as those previously auctioned by the ISO and could be sold in a secondary market. Thus, the FTR holder would have a scheduling priority in the Day-Ahead scheduling process and would be entitled to receive a commensurate share of congestion revenues.¹⁴ The Commission found a similar

¹³ If the Existing Contracts were reformed such that an existing rights-holder had an ability to exercise its rights in the Hour-Ahead scheduling process (i.e., not schedule in the Day-Ahead process, but exercise its rights in the Hour-Ahead process), provisions would have to be developed to implement the recallable aspect of the transmission capacity made available in the Day-Ahead process.

¹⁴ See Sections 9.7 and 9.6 of the ISO Tariff, respectively.

proposal for FTRs reasonable in the context of the ISO's transmission Access Charge.¹⁵

The purpose behind both of these options is to resolve the phantom congestion problem, at least on an interim basis, in order to maximize the efficient use of scarce transmission capacity. The ISO has explored the possibility of other means to make this capacity available, such as a non-firm "recallable" transmission service. However, the software modifications necessary to initiate such a service would not be available for many months.

III. SUPPLY INITIATIVES

In the March 14 Order, the Commission stated that it wished "to elicit whatever additional electric supply there is from existing resources and, equally important, to identify and work constructively on medium and longer term solutions, including new infrastructure that can help avert future recurrences of the current electric supply shortage in the West."¹⁶ The ISO shares the Commission's concern. For this reason, the ISO has proposed and/or implemented the following supply initiatives.

A. The ISO Summer Reliability Generation Program for Summer 2001

Since Spring 2000, the ISO has recognized the need to engage in a Summer Reliability Generation Program (also known as a "peaker" program) for Summer 2001. The ISO issued a Request for Proposal on August 24, 2000. The ISO contracted with ten developers of 30 projects to provide 1,324 MW of

¹⁵ See *California Independent System Operator Corporation*, 91 FERC at 61,726-27.

¹⁶ *Id.* at 61,967.

additional generation during Summer 2001.¹⁷ The program provides a capacity payment to ensure that the capacity is developed. The program does not contract for energy. The California Department of Water Resources (“CDWR”) plans to assume responsibility for these contracts and negotiate for the energy output of the projects to serve the citizens of California.

B. Distributed Generation Changes

In Amendment No. 35 to the ISO Tariff, submitted on December 29, 2000, the ISO proposed the following changes to the ISO Tariff to permit small distributed generation to participate in the ISO’s markets:

- clarification that a distribution-level Generating Unit of under 1 MW that does not participate in the ISO’s Ancillary Services and/or Imbalance Energy markets is not a “Participating Generator” and is not required to be an ISO Metered Entity;
- reduction of the minimum rated capacity threshold for Generating Units to participate in the ISO’s Ancillary Services markets from 10 MW to 1 MW, and provision of flexibility to undertake programs for aggregation of Generating Units of under 1 MW to participate in such markets;
- clarification that a distribution-level Generating Unit of under 10 MW that does not participate in the ISO’s Ancillary Services and/or Imbalance Energy markets is not required to install ISO telemetry; and

¹⁷ See Memorandum Concerning Summer Reliability Generation – Update and Cost Recovery, available at <<http://www.caiso.com/docs/09003a6080/0c/4e/09003a60800c4eb5.pdf>>; Memorandum Concerning Summer 2001 Preparedness Update and Demand Response Programs, available at <<http://www.caiso.com/docs/09003a6080/0c/4e/09003a60800c4e8e.pdf>>.

- addition of provisions to allow net metering arrangements for distribution-level Generating Units of under 1 MW.

On March 14, 2001, the Commission accepted each of these changes, except that it declined to set the ISO's net metering requirements proposal for hearing in the Amendment No. 35 proceeding, as that issue is presently being litigated in other dockets. The Commission granted the ISO's request that the approved changes go into effect on January 1, 2001.¹⁸ The ISO intends to continue to focus on ways to facilitate the participation of all generation in the ISO's markets.

C. BEEP Split

On March 20, 2001, in Docket No. ER01-1579-000, the ISO filed Amendment No. 38 to the ISO Tariff. Among other things, Amendment No. 38 would modify the Imbalance Energy market to allow Energy from Contingency-only Operating Reserves to be separated (or "ordered") in real-time Energy procurement from Operating Reserve Energy that can be used for real-time imbalances in the real-time Imbalance Energy market (or "BEEP") stack. This would give Market Participants with resources selected to provide Operating Reserves the ability to indicate whether the dispatch of these resources should, or should not, be limited to Contingencies or System Emergencies. Market Participants would be able to indicate their preference on an hourly basis. The flexibility to restrict the dispatch of Operating Reserves from energy-limited resources and would increase the available supply of Operating Reserves and

¹⁸ See *California Independent System Operator Corporation*, 94 FERC ¶ 61,266, at 61,921-23.

would assist the ISO in preserving those reserves for Contingency and System Emergency use. Since many energy-limited resources are hydroelectric facilities, Amendment No. 38 supports the Commission's goal of increasing the flexibility of hydroelectric resources to meet power demands in the West. The Commission has not yet acted on Amendment No. 38.

D. New Generator Interconnections

The ISO yesterday filed Amendment No. 39 to the ISO Tariff. Amendment No. 39 proposes enhanced procedures for interconnecting new Generation to the ISO Controlled Grid. The objective of the ISO's proposed New Facility Interconnection Policy ("NFIP") is to establish a clear and consistent policy for interconnecting to the ISO Controlled Grid. The existing ISO Tariff is silent on interconnection procedures and defers such matters to each of the Participating Transmission Owners, thus creating the possibility that new entrants could be treated differently depending upon where they choose to interconnect to the ISO Controlled Grid. The ISO hopes that by filing the NFIP, the ISO will establish one policy applicable to all interconnections to the ISO Controlled Grid, thus facilitating *new* interconnections and eliminating the potential for disparate treatment of new facilities. Moreover, under the NFIP, the procedural and cost responsibilities of new facilities are structured in a manner to reduce barriers to entry for new Generation and accord with Commission precedent. The ISO urges the Commission to expeditiously consider and approve the ISO's proposed NFIP. The ISO believes that the NFIP will further development of critical new generating capacity in California.

E. Qualifying Facility Issues

QF capacity is a critical element of the supply portfolio for the State of California. In fact, absent production from these facilities, particularly in Northern California, the ISO would be required to conduct rolling blackouts on a regular, if not a daily, basis. Obviously, since most of the QF capacity is under long-term Power Purchase Agreements (“PPAs”) with the state’s IOUs, resolution of the IOUs’ financial situation is of paramount importance if these resources are to operate. The State is currently addressing that matter.¹⁹ Moreover, the ISO approves of the Commission’s extension, in the March 14 Order, of the fuel-requirements waiver it granted to all QFs in California in the December 15, 2000 Order Directing Remedies for the California Wholesale Electric Markets.²⁰ The ISO believes, however, that there are a number of additional measures the Commission could take to ensure continued production from these facilities. To the extent that QFs in California are released from their existing PPAs and wish to sell their output into the ISO’s markets, we urge the Commission to clarify that the facilities’ existing Interconnection Agreements (“IAs”) should continued to be honored. In addition, if existing QFs are capable of selling additional capacity to the ISO (above and beyond that specified in their PPAs) and the ISO determines that introduction of that additional capacity onto the ISO Controlled Grid will not have an adverse impact on grid reliability, the ISO urges the Commission to

¹⁹ See <<http://www.cpuc.ca.gov/static/announcements>>.

²⁰ See March 14 Order at 61,970-71 (extending waiver through December 31, 2001 and applying it to the entire Western Systems Coordinating Council); *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Services Into Markets Operated by the California Independent System Operator and the California Power Exchange, et al.*, 93 FERC ¶ 61,294, at 62,018.

permit such deliveries under the terms of their existing IAs.²¹ The ISO believes that such measures are necessary to ensure the availability of all QF capacity for the critical summer season.

IV. DEMAND INITIATIVES

In the March 14 Order, the Commission expressed its support for initiatives to reduce demand, and proposed certain initiatives within its authority.²² The ISO is also a proponent of demand initiatives.

As the ISO recently explained in its Comments On Staff's Recommendation On Prospective Market Monitoring and Mitigation for the California Wholesale Electric Power Market, the ISO has undertaken several demand-side initiatives to encourage demand response. These fall into three areas: (1) price-responsive demand (e.g., the ISO Participating Load Ancillary Services Program and ISO Discretionary Load Curtailment Program), (2) conservation campaigns (e.g., public announcements and the PowerWatch communications initiative), and (3) demand curtailments under emergency conditions (e.g., the ISO Demand Relief Program). The ISO also explained that the requirements of load-serving entities must be coordinated with state demand reduction efforts (e.g., the contemplated installation of interval meters to facilitate

²¹ As specified in the proposed modification to Section 5.7 of the ISO Tariff contained in Amendment No. 39, new facilities covered by the ISO's interconnection procedures include: (1) each Generating Unit that seeks to interconnect to the ISO Controlled Grid; (2) each existing Generating Unit that has been re-powered and increased the total capability of the power plant; and (3) each existing Generating Unit that has been re-powered without increasing the total capability of the power plant but has changed the electrical characteristics of the power plant such that its re-energization may violate Applicable Reliability Criteria. Thus, existing facilities such as QFs with existing interconnection arrangements would not be required to go through the new facility interconnection process when their existing PPAs expire.

²² See March 14 Order at 61,967-68, 61,972-73.

implementation of real-time pricing and thus true demand responsiveness).²³

These programs are further detailed in documents available on the ISO Home Page.²⁴

V. CONCLUSION

The ISO requests that the Commission accept for consideration the comments presented above.

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²³ See Comments of the California Independent System Operator Corporation On Staff's Recommendation on Prospective Market Monitoring and Mitigation for the California Wholesale Electric Power Market, Docket No. EL00-95-012 (Mar. 22, 2001), at 22-26.

²⁴ See Memorandum Concerning Summer 2001 Preparedness Update and Demand Response Programs, available at <<http://www.caiso.com/docs/09003a6080/0c/4e/09003a60800c4e8e.pdf>>; Demand Response Programs and Summer 2001 Preparedness Presentation, available at <<http://www.caiso.com/docs/09003a6080/0c/6e/09003a60800c6e4f.pdf>>.