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

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| **Coral Power, LLC** | **)** | **Docket No. EL03-151-000** |
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| **Coral Power, LLC** | **)** | **Docket No. EL03-186-000** |
| | **)** | **(Not Consolidated)** |

# COMMENTS OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION ON AGREEMENT AND STIPULATION

**To: Presiding Administrative Law Judge Carmen A. Cintron**
**Presiding Administrative Law Judge Isaac D. Benkin**

On November 14, 2003, Coral Power L.L.C. ("Coral") and the Federal Energy Regulatory Commission Trial Staff ("Staff") submitted an Agreement and Stipulation ("Agreement") to the Commission in full and final resolution of all issues related to Coral that were set for hearing on June 25, 2003 in *American Electric Power Service Corp., et al.*, 103 FERC ¶ 61,345 (2003) (the "Gaming Show Cause Order" or the "Gaming Order"), and in *Enron Power Marketing, Inc. and Enron Energy Services, Inc., et al.*, 103 FERC ¶ 61,346 (2003) (the "Partnership Show Cause Order" or the "Partnership Order"). Pursuant to Rule 602 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.602 (2003), the California Independent System Operator Corporation ("CAISO") timely submits these comments on the Agreement.

## I. Background

The Gaming Show Cause Order required Coral to show cause why it should not be found to have engaged in False Import, Circular Scheduling, Paper Trading, Cutting Non-Firm (Cut Schedules), Scheduling Counterflows on Out-of-Service Lines, and Load Shift, as those practices were described in the Order. The Partnership Show Cause Order required Coral to show cause why it should not be found to have acted in concert with the City of Glendale, California and Sempra Energy/Sempra Energy Resources to engage in activities that could have constituted Gaming Practices (as those practices were described in the Order). In these comments, the ISO addresses the issues of False Import, Circular Scheduling, Paper Trading, Cut Schedules, and Scheduling Counterflows on Out-of-Service Lines. The ISO takes no position on the Agreement with respect to the issues of Load Shift and any activities that Coral may have engaged in in connection with Glendale and Sempra.

## II. Discussion

### A. False Import

Staff asserts that "based on the Commission's definition of False Import transactions and review of the CAISO July 15, 2003 report, Staff determined that there is no basis upon which to proceed further with its investigation in False Import as it relates to Coral." Agreement at ¶ 3.2. The Agreement, in this respect, appears to rest on Staff's interpretation of the Gaming Show Cause Order. In Staff's view, a False Import transaction requires that a seller (i) engage

in a transaction involving export of energy from and re-import of energy into the State of California, (ii) involve a third party in the export-plus-import chain, and (iii) sell the allegedly imported power to the CAISO at a price above the then-applicable price cap in the CAISO's Real Time Market. Moreover, Staff's position is that the Commission made subject to the Gaming Show Cause Order only those False Imports that occurred between May 1, 2000 and October 2, 2000. The CAISO disagrees with this interpretation. In our Request for Rehearing and/or Clarification of the Gaming Order, filed on July 25, 2003, we asked the Commission to clarify that the investigation into potential False Import transactions would include all exports scheduled on a Day-Ahead or Hour-Ahead basis that could be associated with a subsequent sale of real time energy as an import, which is the screen the CAISO's Department of Market Analysis used to identify potential False Import transactions in the CAISO Report.[1] As we explained therein, limiting the scope of inquiry to only those transactions that involved an export from the State of California, a third party, and a sale to the CAISO above the then-applicable price cap would be inconsistent with the Commission's rationale for concluding that False Import transactions constitute a Gaming Practice in the first place. The rationale was that they involved a misrepresentation to the CAISO that the applicable power had been imported from outside the CAISO system when, in fact, the generation was California

[1] On July 11, 2003, the California Parties filed a motion for expedited clarification of the Order, in which they also requested that the Commission clarify that the investigation into potential False Import transactions would include all transactions where power was exported or claimed to be exported from the CAISO system via any market other than real-time, and then re-imported in real time. "California Parties' Motion for Expedited Clarification of Order to Show Cause Concerning Gaming and/or Anomalous Market Behavior," Docket Nos. EL03-137, *et al.* (filed July 11, 2003), at 5-13.

generation that had never left the CAISO system. We also noted that the Commission compiled its list of entities that appear to have engaged in False Import based on those entities that were named in the ISO Report as possibly having engaged in Ricochet (i.e., False Import) transactions. We therefore urge the Commission, at this time, not to approve the Agreement with respect to the issue of False Import. Instead, we respectfully request that the Commission decline to rule on the portion of the Agreement concerning False Import until it renders a decision on the appropriate scope of the investigation into the practice of False Import in response to the requests for rehearing and/or motions for clarification of the Order that are currently pending before it.

### B. Circular Scheduling

The CAISO objects to approval of the Agreement with regard to the issue of Circular Scheduling. The Agreements states that Coral agrees to pay $809,253 to settle with respect to this issue. Agreement at ¶ 3.7. The Agreement notes that "the ISO's July 15 Data show that Coral received a total of $1,550,999 from potential Circular Schedules," but states that "Staff independently reviewed and verified the information and is satisfied that $741,746 of the revenue amount related to the Circular Schedules allegation were incorrectly identified by the ISO." *Id*.

Unfortunately, the Settlement does not identify or provide the information that was reviewed by Staff and formed the basis for Staff's conclusion that $741,746 of $1,550,999 in revenue identified by the CAISO as possibly

connected with the practice of Circular Scheduling was "incorrectly identified." The lack of said information makes it impossible for the ISO and other parties to evaluate and comment on the merits of Staff's conclusions. The ISO therefore objects to the Agreement's proposed settlement of this issue.

In response to Commission data requests concerning the various Gaming Practices, Coral denied engaging in any Circular Scheduling Activities.[2] However, in its September 2, 2003 response to the Show Cause Order ("Show Cause Response"), Coral admitted that many of the transactions identified by the ISO did, in fact, meet the Commission's definition of Circular Schedules.[3] Moreover, trading transcripts submitted by the California Parties in the 100-day Discovery proceeding (Docket Nos. EL00-95-075, *et al*.) demonstrate that Coral, on at least one occasion, did engage in the practice of Circular Scheduling by using the "Southwest Loop" identified in the CAISO Reports, by submitting a 9 MW import schedule into the CA ISO system at Four Corners, a 9 MW export schedule from the CAISO system at Palo Verde, with a connecting schedule between Palo Verde and Four Corners outside of the CA ISO system on Arizona Public Service Company transmission. Exh. CA-301. The ISO identified $1.2 million in transactions that were "Southwest Loops" similar to the one identified in

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[2] *See* Coral's May 22, 2002, Discovery Response to FERC's "admit or deny" data request. This response is certified by Beth A. Bowman, Senior Vice President of Coral Energy Management, L.L.C. Additionally, the May 21, 2002 response of Coral Power, L.C.C. is also certified by Beth A. Bowman, Senior Vice President of Coral Power, L.L.C. indicating that these two entities share at least some common management. In the May 22 response, Coral Energy Management, L.L.C. denies that Coral engaged in the practice of Circular Scheduling and no response was found for Coral Power, L.L.C. Due to the omission of a response from Coral Power, L.L.C. and the shared management, it is assumed that the denial of behavior certified by Beth A. Bowman on May 22 applies to all Coral entities that were required to respond to the data request issued in the PA02-2-000 docket.

[3] Testimony and Exhibits of Jeffrey Tranen on behalf of Coral Power, L.L.C, in Response to Order to Show Cause, Exh. COR-1 at 17:19-22.

Exhibit CA-301, $500,000 of which would not be explained by documents provided to Staff by Coral based on Staff's proposed settlement figure.

Because Staff and Coral have provided no information to support the conclusion that $741,746 of the potential revenue related to the practice of Circular Scheduling was misidentified by the ISO, and Coral has admitted to engaging in this practice, after it had previously denied doing so, the Commission should reject the proposed settlement on this issue, and require that this issue be subject to evidentiary hearing procedures in order to adduce material facts concerning Coral's participation in the practice of Circular Scheduling, especially the "Southwest Loop" schedules. Additional evidence that can and should be produced by Coral in the context of such a hearing would include "e-tags" submitted by Coral to different control areas for these schedules, and purchases of transmission outside the ISO control area which may be used to link the import/export schedules identified by the ISO into a circular loop of schedules.

### C. Paper Trading

In the Agreement, Coral agrees to settle the issue of Paper Trading for a payment of $6,798,412. Agreement at ¶ 3.6. The CAISO does not object to the Agreement's proposed settlement of this issue.

### D. Cutting Non-Firm

With respect to the issue of Cutting Non-Firm (Cut Schedules), the Agreement states that Staff, based on an independent review of information

provided by Coral, is satisfied that the transactions flagged by the CAISO as potentially Cut Schedules were incorrectly identified by the CAISO. Therefore, the Agreement concludes that there is no basis to proceed with its investigation into Cutting Non-Firm, and proposes to settle this issue for no money. The CAISO objects to approval of the Agreement as to this issue.

First, Staff is mistaken in its conclusion that schedules must be categorized as "Non-Firm" in order to qualify as gaming practices. Agreement at ¶ 3.4. The crucial element that characterizes this Gaming Practice, and other congestion-type practices, according to the Commission, is the submission of a schedule that the Market Participant never intended to deliver or knew it would not be able to deliver. Show Cause Gaming order at P. 46 ("Each of the four Congestion-Related practices violated the MMIP because the market participants submitted false schedules to the ISO."). This crucial characteristic of Cut Schedules is reflected in all of the CAISO's reports and analysis, and has been clearly explained by the CAISO in previous discussion with Staff. Specifically, the CAISO Report explains [with respect to cut non-firm schedules]:

> Enron successfully used this strategy to earn a total of $54,000 in congestion payments on three separate days between June 14 and July 20, 2000. The next day, on July 21, 2000, this practice was proscribed by the ISO under a Market notice issued under the MMIP, and this practice has not occurred since a market notice was issued. No other SCs appear to have successfully used this strategy prior to the incidents with Enron in June-July 2000 with the possible exception of Duke.[4]

[4] "Analysis of Trading and Scheduling Strategies Described in Enron Memos," Department of Market Analysis, October 4, 2002, at 7.

A subsequent portion of the CAISO Report states that the universe of Cut Schedules identified in that report included only a few non-firm schedules, and were primarily comprised of other types of schedules (firm or wheeling) that were cut after earning counterflow congestion payments. As the CAISO Report stated:

> A more general type of scheduling practice described in the Enron memos is where SCs submit schedules in the Day-Ahead and/or Hour-Ahead Congestion Markets, providing counter-flows on a congested path. These Schedules receive Congestion charges, which are ultimately paid by SCs with Schedules in the congested direction, as counter-flow revenue in the Day-Ahead and/or Hour-Ahead Congestion Markets. Under current ISO scheduling and Settlement practices, SCs may subsequently cut the counter-flow Schedules just prior to real-time, but still receive the counter-flow revenues for Schedules submitted in the Day-Ahead and/or Hour-Ahead Congestion Markets.
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> This creates a gaming opportunity, in that SCs may earn Congestion revenues for counterflow schedules in the Day-Ahead and Hour-Ahead Markets, and then cancel these Schedules prior to real time. The practice of cutting non-firm Schedules was proscribed by the ISO on July 21, 2000 in accordance with the Market Monitoring and Information Protocol Section of the ISO Tariff and does not appear to have occurred since that time. However, a similar gaming opportunity continued to exist insofar as the same basic strategy could be employed by cutting wheel-through Schedules and/or firm Energy Schedules.[5]

Thus, the CAISO analysis of this practice, as provided to the Commission, was not limited to the cutting of "non-firm" schedules. Moreover, the Commission required all entities identified in the ISO Report as possibly having engaged in this practice to show cause why they had not, even though the ISO clearly explained that its analysis was not limited to "non-firm" schedules.[6] Thus, it is unreasonable for Staff to conclude that the Commission intended for the Show

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[5] "Supplemental Analysis Trading and Scheduling Strategies Described in Enron Memos," Department of Market Analysis, June, 2003 ("Supplemental Analysis") at 26.

[6] *Id.* at 26-28.

Cause proceeding to be limited to those transactions that involved the cutting of non-firm schedules.

Therefore, for the reasons stated above, the CAISO believes that Coral's potential participation in the practice of Cut Schedules should be subjected to further review, which will allow collection of actual evidence relating to whether any of the schedules identified by the CAISO involve schedules which, as claimed by Coral, Coral never intended to deliver or Coral knew it would not be able to deliver.

### E. Scheduling Counterflows on Out-of-Service Lines

Staff states that it is satisfied that there is no basis upon which to proceed further with its investigation into the allegations that Coral engaged in Scheduling Counterflows on Out-of-Service Lines ("Wheel Out"), on the grounds that the Commission's definition of this practice is limited to situations in which the same Market Participant first creates and then relieves congestion on a line this is known to be out-of-service. Agreement at ¶ 3.5. The CAISO objects to this result. Staff's interpretation is entirely inconsistent with the "Wheel Out" strategy as described in the initial Enron memos, as well as in the CAISO Reports upon which the Show Cause Orders were based. Again, as the Commission stated in the Show Cause Gaming Order, the essential element of this practice, as with the other congestion practices, is that it involved the submission of false schedules to the ISO. Show Cause Gaming Order at P. 46. In fact, under Staff's overly restrictive reading, even Enron would be found never to have employed

the "Wheel Out" strategy described in the Enron Memos.[7] As stated in the Enron Memos, the crucial element of the "Wheel Out" strategy is that when a tie-line is known to be out of service, traders submit schedules in a direction that is counter to potential congestion, knowing that they may be able to earn congestion revenues for schedules they know they will not have to provide.[8]

In its Show Cause Response, Coral argues that since the counterflow revenues it received from scheduling on out-of-service lines were the result of the ISO congestion management procedure utilizing adjustment bids submitted by Coral, that Coral did not intentionally submit the schedule itself and is not responsible for the resulting schedule. Exh. COR-1 at 22:1-18. However, Coral is responsible for submitting the adjustment bids that resulted in the final schedules that were paid to relieve congestion on the out-of-service tie-lines. In practice, it makes no difference if an entity submits an initial energy schedule, or submits adjustment bids which may result in an energy schedule in the counterflow direction if accepted by the CAISO's congestion management software. In both cases, an entity may be submitting a schedule to the CAISO for energy that it never intended to deliver or knew it would not be able to deliver. In practice, the only difference between these two scheduling mechanisms is that by submitting adjustment bids, rather than directly scheduling energy, an entity can remove any risk associated with the Wheel Out strategy by ensuring that it

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[7] In fact, under a situation that fits the interpretation used by Staff, no gaming opportunity would even exist, since a participant who first created congestion by scheduling in one direction on an open tie would incur congestion charges that would at least off set (and could even exceed) any congestion credits received for any counterflow schedules submitted by that same participant.

[8] *See* Enron Memo dated December 6, 2000, at 6.

can only benefit from congestion, since its adjustment bids will only be accepted if there is congestion in the opposite direction for which the entity will receive a counterflow payment.

## III. Conclusion

For the reasons stated herein, the CAISO opposes the Agreement between Coral and Commission Staff with respect to the issues of False Import, Circular Scheduling, Scheduling Counterflows on Out-of-Service Lines, and Cutting Non-Firm. The ISO respectfully requests that the Commission reject the Agreement with respect to these issues.

Respectfully submitted,

*/s/ J. Phillip Jordan*

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Dated: December 4, 2003

## CERTIFICATE OF SERVICE

In accordance with the order issued by the Presiding Administrative Law Judge I hereby certify that I have this day served the foregoing document by posting an electronic copy on the Listserv for this proceeding, as maintained by the Commission.

Dated at Washington, DC, on this 20th day of November, 2003.

*/s/ Michael Kunselman*
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