UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	**)** **)**	**Docket No. ER06-615-000**

ANSWER OF THE
CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION
TO COMMENTS ON DECEMBER 20, 2006 COMPLIANCE FILING

Pursuant to Rules 212 and 213 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §§ 385.212 and 385.213 (2006), the California Independent System Operator Corporation ("CAISO") respectfully submits this Answer to comments addressing the CAISO's compliance filing made on December 20, 2006 ("December 20 Compliance Filing") in accordance with the Commission's order of September 21, 2006 conditionally accepting the CAISO's Market Redesign and Technology Upgrade Tariff Filing ("MRTU Tariff Filing"), [1] and the Commission's "Notice of Extension of Time" issued in this docket on November 27, 2006. Two parties, Powerex and Williams, submitted comments on the December 20 Compliance Filing. The CAISO responds to their concerns herein.

I. BACKGROUND

On February 9, 2006, the CAISO filed with the Commission its complete MRTU Tariff proposal ("February 9 MRTU Tariff Filing"). This filing consisted of

[1] *California Independent System Operator Corp*., 116 FERC ¶ 61,274 (2006) ("September 21 Order").

all of the proposed modifications to the CAISO Tariff reflecting the numerous changes to the CAISO's market structure included in the MRTU initiative, as well as hundreds of pages of testimony from numerous witnesses explaining these changes, and a comprehensive transmittal letter and attachments describing the changes and the MRTU process in detail.

On September 21, 2006, the Commission accepted for filing the MRTU Tariff to become effective on the proposed effective date of November 1, 2007,[2] subject to a number of modifications, as detailed in the September 21 Order. In addition to tariff changes, the Commission also directed the CAISO to take various other actions, including providing additional details concerning several of its proposals, filing with the Commission status reports on specific issues, and making certain information available to Market Participants. The Commission provided several timeframes for the CAISO to comply with these various requirements.

On November 20, 2006, the CAISO filed with the Commission a compliance filing that included most of the items that the Commission ordered the CAISO to address within 60 days of the September 21 Order ("November 20 Compliance Filing"). On that same date, the CAISO also filed a motion for extension of time to comply with several of the 60-day compliance items. On November 27, 2006, the Commission issued an order approving the CAISO's motion for extension of time, with one modification.

[2] As the CAISO has previously informed the Commission, on December 19, 2006, the CAISO Board of Governors approved a revision to the scope, schedule and budget of MRTU, modifying the implementation date for Release 1 of MRTU from November 2007 to January 31, 2008 (for Trading Day February 1, 2008).

On December 20, 2006, the CAISO submitted a compliance filing consisting of three items from the September 21 Order for which the CAISO requested and was granted a 30-day extension of time within which to comply. On January 10, 2007, two parties, Powerex and Williams, filed comments addressing the December 20 Compliance Filing.

II. ANSWER

A. Negotiated Option for Default Energy Bid Issues

In the September 21 Order, the Commission directed the CAISO to clarify the procedures a Market Participant must follow and the type of information it must provide to take advantage of the Negotiated Rate Option for Default Energy Bids.[3] The CAISO was also directed to file procedures for dispute resolution in the event that the market participant and the CAISO cannot agree on a negotiated price.[4] In the December 20 Compliance Filing, the CAISO proposed a specific set of procedures for determining Negotiated Rates for Default Energy Bids. In its comments, Williams raises several issues with respect to the CAISO's proposed procedures.

[3] September 21 Order at P 1059.

[4] *Id*. In the September 21 Order, the Commission also directed the CAISO to modify the MRTU Tariff to require that an agreed-upon negotiated price for Default Energy Bids be filed at FERC. In its Request for Clarification and Rehearing of the September 21 Order, the CAISO requested that the Commission clarify that this directive will be satisfied by a monthly informational filing, and that Commission review and approval of the negotiated Default Energy Bids will not be required prior to those Bids taking effect.

1. The CAISO has included an appropriate level of detail concerning the Negotiated Rate Option for Default Energy Bids in the MRTU Tariff

Williams argues that the CAISO's proposal inappropriately defers to a Business Practice Manual ("BPM") details concerning the information that Scheduling Coordinators must submit to the CAISO as part of the Negotiated Rate Option process.[5] Specifically, Williams takes issue with the following proposed tariff language: "Scheduling Coordinators that elect the Negotiated Rate Option for the Default Energy Bid shall submit a proposed Default Energy Bid along with supporting information and documentation as described in a BPM."[6]

The CAISO submits that including in a BPM, rather than its Tariff, details concerning the supporting documentation to be submitted by Scheduling Coordinators as part of the Default Energy Bid process is consistent with the Commission's standard, which requires that only those provisions "*significantly* affecting rates, terms and conditions of service" must be included in a Commission-approved Tariff.[7] The type of information submitted by Scheduling Coordinators as part of the Default Energy Bid process does not significantly affect rates, terms and conditions of service. Although this information will assist the CAISO (or Independent Entity) in reviewing the Scheduling Coordinator's proposed Default Energy Bid, it does not actually affect the rate itself, because

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[5] Williams Comments at 3.

[6] MRTU Tariff, Section 39.7.1.3.1

[7] *See City of Cleveland v. FERC*, 733 F.2d 1368, 1376 (D.C. Cir. 1985) ("[T]here is an infinitude of practices affecting rates and service. The statutory directive must reasonably be read to require the recitation of only those practices that affect rates and service significantly, that are realistically susceptible of specification, and that are not so generally understood in any contractual arrangement as to make recitation superfluous.").

the rate is determined based on negotiations between the CAISO (or an Independent Entity) and the Scheduling Coordinator. If the CAISO (or Independent Entity) does not agree with the Scheduling Coordinator's proposed Default Energy Bid, then the Scheduling Coordinator has the option of establishing a temporary Default Energy Bid pursuant to any of the other options set forth in Section 39.7, pending negotiations or Commission review.

Moreover, although the information requirements for Default Energy Bid submissions will not be included in the Tariff, the CAISO developed these requirements through an ongoing stakeholder process. On January 19, 2007, the CAISO made available to stakeholders a draft BPM containing details regarding the types of information that Scheduling Coordinators should submit as part of their Default Energy Bid proposals. The CAISO will work with stakeholders over the coming months to refine this language as necessary.

Finally, the CAISO notes that, as a practical matter, the Tariff and BPMs must provide some flexibility in terms of the specific type of supporting documentation to be submitted by Scheduling Coordinators as part of the Default Energy Bid process, in order to accommodate the wide range of resources and situations for which Default Energy Bids may need to be established under the Negotiated Rate Option. For example, this option is likely to be applied in many cases due to the existence of special circumstances or resource characteristics that may make the other Default Energy Bid options inappropriate or infeasible. Because the precise nature of these special circumstances or resource characteristics can never be fully anticipated, flexibility is needed in terms of

specifying the relevant type of supporting documentation that Scheduling Coordinators may be required to submit as part of the Default Energy Bid process. Requiring the specifics of such information requirements to be "hard coded" into the Tariff would defeat the purpose of this option, which is to provide Scheduling Coordinators and the CAISO with increased flexibility in order to better establish suitable Default Energy Bids. For these reasons, the CAISO requests that the Commission reject Williams' argument that the CAISO must include in its Tariff details concerning the specific supporting information that Scheduling Coordinators must submit along with their proposed Default Energy Bids.

2. The CAISO's proposal to calculate and establish temporary Default Energy Bids under certain well-defined circumstances is just and reasonable

Under the CAISO's proposed Default Energy Bid procedures, when the CAISO and a Scheduling Coordinator fail to agree upon a Default Energy Bid, the CAISO will be able to establish a temporary Default Energy Bid under two scenarios: (1) when the Scheduling Coordinator does not choose to exercise one of the other options available under Section 39.7 for which data are available; or (2) sufficient data do not exist to calculate a Default Energy Bid on the basis of any of the other available options. Williams contends that the CAISO should not be given the authority to establish temporary Default Energy Bids under these circumstances for several reasons. None of the reasons provided by Williams is convincing.

Williams first argues that there are no circumstances under which the CAISO would not have sufficient information to calculate a Default Energy Bid under one of the options set forth in Section 39.7.[8] Williams bases this argument on Section 4.6.4 of the MRTU Tariff, which states that Participating Generators must provide, upon the CAISO's request, information regarding the capacity and operating characteristics of their Units. Williams reasons that because this section would presumably include heat rate data, which would be needed in order to calculate the Variable Cost Option under Section 39.7.1.1, if a Participating Generator fails to submit heat rate data to the CAISO, the CAISO should obtain this data from the Generator rather than calculating and imposing a temporary Default Energy Bid.

Williams' argument is flawed, because it assumes that the CAISO's ability to obtain data pursuant to Section 4.6.4 will allow the CAISO to calculate a Default Energy Bid under the Variable Cost Option in all cases. This assumption is wrong for two reasons. First, the Generator may not have provided sufficient heat rate data, or other information, to allow calculation of a Default Energy Bid under any of the available options under Section 39.7. The CAISO will make appropriate efforts to obtain such information. However, until such time as such data is available, it is reasonable that the CAISO have the ability to establish a Default Energy Bid in the interim. In particular, Williams overlooks situations in which the operating characteristics of a Unit might change quickly, and the CAISO would need to establish promptly a temporary Default Energy Bid despite the fact that it does not have the data necessary to calculate a Default Energy

[8] Williams Comments at 5-7.

Bid under one of the options set forth in Section 39.7. Second, Williams overlooks the fact that many resources may not have heat rates or equivalent data upon which very standard, formulaic calculations may be used to derive Default Energy Bids.

The CAISO concedes that these situations are likely to be rare, but believes it prudent and beneficial to the market as a whole to have in place tariff language that provides the CAISO with the ability to establish Default Energy Bids under such circumstances. Under the MRTU market rules for Local Market Power Mitigation, Default Energy Bids are used to determine which units are dispatched to meet local reliability needs, and which units' bids require mitigation. Consequently, the CAISO believes it is imperative to have a "safety net" to insure that appropriate temporary Default Energy Bids can be used in these types of situations.

Finally, Williams fails to take account of the possibility that even if the CAISO has the heat rate data necessary to calculate a temporary Default Energy Bid under the Variable Cost Option, the Scheduling Coordinator may not wish its temporary Default Energy Bid to reflect the Variable Cost Option. By not electing one of the options available under Section 39.7, the Scheduling Coordinator has the flexibility, as explained below, to allow the CAISO to calculate a Default Energy Bid that will better reflect current market conditions. Accordingly, the CAISO's proposal provides maximum flexibility to Scheduling Coordinators to choose the option that it believes is most appropriate for its circumstances.

Williams' second argument concerning the CAISO's authority to establish temporary Default Energy Bids is that if a Scheduling Coordinator fails to elect one of the options set forth under Section 39.7, that the CAISO should use the Variable Cost Option, rather than calculating a Default Energy Bid.[9] Williams contends that there is no reason for the CAISO to calculate a Default Energy Bid in this situation. Williams is incorrect. In the transmittal letter accompanying the December 20 Compliance, the CAISO stated why it chose this approach. Therein, the CAISO explained that because this provision only applies in cases where a Scheduling Coordinator opts not to use a Default Energy Bid, it would likely only be invoked in cases when a Scheduling Coordinator feels that any of the options available under Section 39.7 would result in an unreasonably low Default Energy Bid, such as when system or market conditions may warrant a sudden increase in a unit's Default Energy Bid on an expedited basis. In such cases, this provision would provide the CAISO with the flexibility to implement a temporary Default Energy Bid that reflects such conditions, even though a valid Default Energy Bid may exist under any of the other options. For these reasons, the CAISO's proposal to calculate a Default Energy Bid in situations when a Scheduling Coordinator does not elect one of the options available under Section 39.7 is reasonable, and Williams' argument should be rejected.

Williams's third argument relating to the CAISO's Default Energy Bid proposal is that proposed Section 39.7.1.5 provides the CAISO with too much discretion because it provides the CAISO with a "banquet of options" for

[9] *Id*. at 7-8.

calculating a temporary Default Energy Bid.[10] The CAISO concedes that Section 39.7.1.5 provides the CAISO with flexibility to establish a Default Energy Bid based on a variety of data. Contrary to Williams' assertion, however, such flexibility is a positive feature because, as explained above, it will allow the CAISO to establish the Default Energy Bid that best reflects current market conditions. Moreover, it should be understood that the CAISO will have the authority to calculate Default Energy Bids under Section 39.7.1.5 only in cases where the CAISO and the Scheduling Coordinator have not been able to agree on a Default Energy Bid, *and* where the Scheduling Coordinator foregoes its opportunity to elect one of the Default Energy Bid options available under Section 39.7 for which there is data available.

Finally, Williams argues that proposed Tariff Section 39.7.1.5 is outside the scope of the directives contained in the September 21 Order because the Commission therein "did not direct or authorize the CAISO to develop a process in which the CAISO may unilaterally calculate and impose a temporary Default Energy Bid."[11] The Commission did, however, note that the MRTU Tariff lacked "specific procedures to address negotiation and resolve disputes relating to the default energy bid" and directed the CAISO to "clarify[] the procedures a market participant must follow to exercise [the Negotiated Rate Option for Default Energy Bids."[12] Section 39.7.1.5 is consistent with the Commission's directive to establish such procedures, because it addresses situations that may occur during the Default Energy Bid negotiation process. Specifically, instances in

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10 *Id*. at 8.

11 *Id*. at 8-9.

12 September 21 Order at P 1059.

which the CAISO and Scheduling Coordinator cannot reach agreement on a Default Energy Bid, and the Scheduling Coordinator either fails to elect one of the options available under Section 39.7 on a temporary basis, or has not provided sufficient data to permit calculation of a temporary Default Energy Bid. Williams' implicit assertion that the CAISO's proposal is outside the scope of the September 21 Order merely because the Commission did not explicitly address these specific scenarios and order the CAISO to adopt tariff language similar to what it proposed in Section 39.7.1.5 strains credibility, and should be rejected.

B. The CAISO Gave Full and Meaningful Consideration to the Appropriateness of the 80 Percent Threshold for Frequently Mitigated Units

In the September 21 Order, based on concerns regarding resource adequacy and bidding incentives, the Commission directed the CAISO to consider whether the 80 percent mitigation frequency threshold is appropriate, and whether units mitigated less than 80 percent of the time should also receive a bid adder, and to report its conclusions.[13] In the transmittal letter accompanying the December 20 Compliance Filing, the CAISO noted that it had conducted a stakeholder process addressing this issue in which it prepared and circulated a whitepaper, solicited stakeholder feedback on that whitepaper, and held a meeting with stakeholders to discuss this issue. The CAISO went on explain that in light of the diversity of comments and further discussion with stakeholders, and on careful reflection, the CAISO determined that no changes to the Frequently Mitigated Unit ("FMU") tariff language in the MRTU Tariff are

[13] September 21 Order at P 1063.

warranted at this time. The CAISO also specifically discussed the two concerns raised by the Commission in the September 21 Order.

Williams argues that the CAISO has not complied with the September 21 Order on this issue because the CAISO "did not perform any quantitative analysis to identify units that might be eligible for the FMU Bid Adder under the 80 percent threshold and the frequency with which those units would be mitigated."[14] Concerns about this issue expressed during the stakeholder process appeared to be derived from the misperception that the CAISAO could perform such an analysis based upon the frequency and units the CAISO intended to mitigate in order to resolve transmission constraints. However, In the December 20 Compliance Filing transmittal letter the CAISO specifically addressed this argument, explaining that such an analysis could not be done in any meaningful way at this time, because it would require making a series of assumptions about market conditions and behavior under MRTU from a virtually unlimited set of scenarios and permutations of different assumptions. As noted in the December 20 Compliance Filing specifically, such analysis would need to be based on assumptions about the specific scheduling and bidding of every resource in the CAISO system, as well as which units were under Resource Adequacy contracts. Moreover, such analysis would presumably need to be performed for an entire year and would need to examine various scenarios representing a virtually unlimited set of transmission and plant outages that could also effect the need to mitigate bids for non-RA units. Furthermore, in order to address issues of revenue adequacy for specific units that were assumed not to

[14] Williams Comments at 9-11.

be under RA contracts, another series of assumptions and analysis would be needed to assess each unit's overall cost and revenues under the various market or system scenarios examined. Finally, as a practical matter, the CAISO notes that the CAISO's ability to perform such analysis at this time is limited by the market simulation tools and staff resources available for use in modeling and analyzing performance of the CAISO system under a nodal market design.

The CAISO also stated in the transmittal letter accompanying the December 20 Compliance Filing that it will be closely monitoring and analyzing the Mitigation Frequency as MRTU is implemented, and that should that analysis indicate that modifications to the FMU Bid Adder are necessary, the CAISO will determine the appropriate changes through a stakeholder process and make a filing with the Commission.

Williams does not contest the CAISO's assertion that it cannot, at this time, meaningfully perform the type of quantitive analysis that Williams believes is necessary to comply with the September 21 Order. Nevertheless, employing a "Catch-22" type logic, Williams contends that until the CAISO has performed such an analysis, it cannot be said to have complied with the September 21 Order. Williams provides no suggestions as to how the CAISO might bridge this impasse, simply reiterating that the Commission should direct the CAISO to engage in the "meaningful analysis" required by the September 21 Order. The CAISO has performed as extensive an analysis as is currently possible of the 80 percent FMU threshold. If the CAISO were to undertake the sort of quantitative analysis demanded by Williams at this time, the results would be, at best,

suspect, and therefore virtually useless in meaningfully answering the concerns raised by the Commission. The CAISO maintains that the analysis that it has conducted to date, as explained in the transmittal letter accompanying the December 20 Filing, along with its commitment to monitor and analyze the Mitigation Frequency as MRTU is implemented, and to make any necessary modifications to the FMU Bid Adder indicated by such analysis, sufficiently satisfies the Commission's directives in Paragraph 1063 of the September 21 Order. Williams' meritless argument to the contrary should be rejected.

C. Interruptible Import Issues

In the September 21 Order, the Commission directed the CAISO to explain how it will handle sales of Interruptible Imports in the Day-Ahead Market. This question arises because Scheduling Coordinators are responsible for an Operating Reserve Obligation equal to 100% of Interruptible Imports. Unless the Interruptible Import is a Self-Schedule, however, the CAISO will not know how much additional Operating Reserves to procure to cover the Interruptible Import prior to the simultaneous optimization of the Energy and Ancillary Services markets. In the December 20 Compliance Filing, the CAISO proposed modifications to the MRTU Tariff to address the treatment of Interruptible Imports in the Day-Ahead Market. In its comments on the December 20 Compliance Filing, Powerex raises several concerns regarding the CAISO's proposed tariff language.

First, Powerex suggests that the CAISO remove the term "non-firm" from the definition of Interruptible Imports, reasoning that it is redundant, and may

cause confusion because the MRTU Tariff does not define “non-firm,” and the Commission is considering including a definition of “non-firm” to its pro forma Open Access Transmission Tariff (“OATT”).[15] The CAISO agrees to make this change in any further compliance filing ordered by the Commission, with the clarification that the CAISO uses the term “Non-Firm,” rather than “Interruptible,” in its scheduling template, and therefore, Market Participants will still see the term “Non-Firm” used when submitting Self-Schedules under MRTU.

Second, Powerex stated that the CAISO is not consistent in its description of the requirement that all Interruptible Imports be submitted as Self-Schedules. Specifically, Powerex points out that MRTU Tariff Section 30.5.2.4 states that Interruptible Imports “*can only* be submitted through Self-Schedules in the Day-Ahead Market.” However, elsewhere the Tariff states that Interruptible Imports “*must be* submitted through Self-Schedules in the Day-Ahead Market.”[16] Powerex suggests that the appropriate solution is for the CAISO to design its software so that when a Scheduling Coordinator schedules an Interruptible Import it can – under the CAISO's software – only do so by selecting a Self-Schedule, and consistent with this, the CAISO should revise other references to Interruptible Imports to match the language in section 30.5.2.4, by providing that Interruptible Imports “can only be submitted through Self-Schedules in the Day-Ahead Market."[17] In response, the CAISO notes that its software will be designed consistent with the "can only be” rather than “must be" approach. An Interruptible Import will only be accepted if it is submitted as a Self-Schedule in

15 Powerex Comments at 2-3.
16 *Id*. at 3-4.
17 *Id*. at 4.

the Day-Ahead Market. The CAISO commits to make changes to the MRTU Tariff to replace references to “must be” with “can only be” in any further compliance filing ordered by the Commission to the extent that phrase is used to describe the scheduling process for Interruptible Imports.

Third, Powerex notes the language that the CAISO proposed to add to Section 11.10.3.2 of the MRTU Tariff in the December 20 Compliance Filing in order to clarify the submission of Interruptible Imports should, for the sake of consistency, also be added to the identical sentence Section 11.10.4.2.[18] The CAISO agrees and commits to make this change in any further compliance filing ordered by the Commission.

Fourth, Powerex points out that the CAISO agreed to clarify in the MRTU Tariff that it is the Scheduling Coordinator scheduling the Interruptible Import who will be allocated the cost of the Operating Reserve associated with Interruptible Imports, regardless of whether that Scheduling Coordinator is a Load-Serving Entity ("LSE") or a non-LSE, but that the CAISO did not include this clarification in the tariff text of the December 20 Compliance Filing.[19] The CAISO agrees and commits to modify the MRTU Tariff in any further compliance filing directed by the Commission in order to clarify that the Scheduling Coordinator scheduling an Interruptible Import will be responsible for Operating Reserves associated with the Interruptible Import, regardless of whether the Scheduling coordinator is an LSE or non-LSE.

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[18] *Id*. at 4-5.

[19] *Id*. at 5.

Fifth, Powerex suggests that although the CAISO's restriction of sales of Interruptible Imports to the Day-Ahead Market may be a reasonable accommodation for the initial implementation of MRTU, the CAISO may wish to consider also allowing Interruptible Import sales in the HASP, as this would be consistent with policy objectives of inducing additional energy imports to California when needed to meet load.[20] The CAISO notes that it would not be possible for it to fully analyze and stakeholder this issue as well as make the necessary software changes in order to allow sales of Interruptible Imports in HASP as of MRTU Release 1. The CAISO, however, agrees with Powerex insofar as the CAISO believes that it is appropriate to consider allowing the sale of Interruptible Imports in HASP as a post-MRTU Release 1 enhancement. The CAISO will also consider this change in conjunction with its commitment to explore the implementation of a full hour-ahead market in the post-Release 1 timeframe.

Finally, Powerex notes that the CAISO's proposal to require Self-Schedules for all Interruptible Imports may lead to unintended consequences with respect to Economic Bids. Specifically, Powerex states that Self-Scheduled Interruptible Imports could be given a higher scheduling priority than Economic Bids for Imported Energy that is not Interruptible. Powerex requests that the CAISO clarify whether it intends Interruptible Imports to receive a higher priority than Economic Bids for Imported Energy, and describe how it intends to evaluate these proposed transactions.[21] In response, the CAISO states that it does,

[20] Powerex Comments at 5-6.
[21] Powerex Comments at 6.

indeed, intend that Interruptible Imports receive a higher priority than Economic Bids. The CAISO believes that this outcome is appropriate because the CAISO will procure, and Scheduling Coordinators submitting Self-Schedules for Interruptible Imports will be responsible for, Operating Reserves equal to 100 percent of the quantity of Interruptible Imports.

III. CONCLUSION

Wherefore, for all the reasons stated above, the CAISO respectfully requests that the Commission accept the December 20 Compliance Filing with the clarifications and revisions that the CAISO agrees to make the instant filling.

Respectfully submitted,

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Dated: January 25, 2007

Certificate of Service

I hereby certify that I have this day served a copy of this document upon all parties listed on the official service list compiled by the Secretary in the above-captioned proceedings, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated this 25th day of January, 2007 at Folsom in the State of California.

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