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Powerex appreciates the opportunity to comment on the CAISO's E-Tag requirements Initiative. Powerex believes this is an important topic and appreciates the CAISO's efforts to provide clarity to market participants.

1. What comments do you have relating to issues identify in the Issue Paper dated October 22, 2009, or other issues relating to determining physical Day Ahead schedules?

The NERC e-tagging process serves an important function in the interchange of energy by ensuring that schedules that are relied on by a Balancing Authority to serve load are feasible and accurately reflect a participant's capability of delivering on their physical obligations. The vast majority of schedules traded in the WECC on a pre-scheduled basis require a Day Ahead e-tag by 1500.

Powerex agrees with the issues and assessments of the ISO raised in the e-tagging Issue paper. Most importantly, Powerex believes that the current e-tagging timelines required by the CAISO under MRTU enables participants to engage in implicit virtual bidding, significantly increasing the risk of an unforeseeable load reliability event, as physical generation is displaced by virtual activities.

Powerex also notes that until recently there has been some ambiguity as to the e-tagging requirement in CAISO markets. Powerex believes this ambiguity makes the estimate provided by the CAISO that 95% of schedules are e-tagged a statistic of limited value going forward. This figure may go down very substantially in the future, now that the CAISO has clarified for all market participants that it does not require an e-tag until T-20.[1]

In Powerex's opinion, there are three categories of schedules bidding into the CAISO DA IFM at the interties.

1) Physical Energy Schedules submitted by participants that have energy and transmission procured and set aside in the pre-schedule time-frame; with corresponding e-tags submitted by the WECC business practice standard of 1500 Pacific Prevailing Time on the Day prior to the start of the transaction.
2) Physical Energy Schedules submitted by participants that have not procured all of the energy and transmission necessary within the Day Ahead time frame, but have a reasonable expectation of being able to do so. These participants expect to go

[1] Powerex assumes this 95% figure reflects a percentage of all IFM awards that are e-tagged. If this figure reflects final IFM obligations, after IFM virtual bids have been cleared, or "zeroed out", in the HASP, then the actual level of virtual bidding activity is likely substantially higher than 5% of all IFM awards.

out and procure the energy and/or transmission in the WECC real time energy markets and time frame.

3) Phantom schedules or Implicit Virtual Bids that have not yet procured the energy, nor transmission prior to bidding into the IFM and have no intention, and limited or no capability, of doing so. These schedules are financial in nature and they are attempting to arbitrage the price difference between the Day Ahead IFM and HASP prior to convergence bidding being formally introduced. After the participant is awarded a DA IFM, they place a high-priced buy back bid (or self-schedule) into the HASP to reverse the DA IFM award.

There can also be a combination of strategies 2 and 3 where the participant sells in the IFM and if prices are low enough in real-time in neighboring markets, they will deliver on the IFM schedule (as in 2 above). However, if the neighboring real-time markets are scarce or the prices are unattractive to the participant, the participant reverses the IFM schedule by buying it back in HASP (as in 3 above). This strategy can be equated to the participant getting a 'free option' from the CAISO to either serve their DA IFM award in real-time or buy it back in HASP. This is a free option, because the participant has not paid any of the costs associated with physical delivery (energy and/or transmission). In any event, the participant in this situation lacks a reasonable expectation of being able to deliver on the IFM award.

2. What comments do you have regarding maintaining the status quo (Option 1)?

Powerex believes that the status quo is not an option. Market participants and the CAISO should put in rules to prevent a reliability issue from occurring, and not waiting until after a reliability event, before taking action. Powerex notes that the current rules not only enable implicit virtual bidding, but they encourage this activity, as participants are able to avoid generation and transmission procurement costs associated with being able to deliver on their IFM awards. Aside from the current reliability issues, the current status quo is not viable in relation to future explicit convergence bidding rules. The CAISO must have a reliable way of differentiating actual physical schedules from purely financial bids so that convergence bidding rules and cost allocation methodologies can be accurately assessed.

3. What comments do you have regarding timing requirement with reporting (Option 2)?

Powerex believes any tagging timeline should be easy to administer and minimize discretion on the part of the CAISO or market participants. For this reason Powerex prefers option 3 or an alternative that includes preventative measures or an automatic financial reversal / penalty for failure to e-tag in accordance with the new timing requirement.

4. What comments do you have regarding timing requirement with financial implications (Option 3)?

Of the three options presented by the CAISO, this is Powerex' preferred option. If a market participant fails to submit an e-tag by the new deadline the CAISO should automatically reverse the DA IFM award (in the HASP) and bill the SC the higher of the HASP or DA IFM price. With this chargeback mechanism in place, the market participant cannot gain but may in some cases lose by failing to meet the tagging deadlines.

5. What other solutions would you recommend to resolve issues in number 1 above with no change to the E-Tag Timing Requirement (Option 4)?

Powerex recognizes that the CAISO, in an effort to ensure maximum *physical liquidity* in their IFM markets, may wish to enable participation of:

Category 1. Participants' bids that, if awarded, will result in an e-tag in the pre-schedule time frame (by 1500 PPT Day Ahead), reflecting physical energy and transmission that is procured pre-schedule.

Category 2. Participants' bids that, if awarded, will result in an e-tag in the real-time time frame (by T-20) reflecting physical energy and transmission that will be procured pre-schedule *and/or* real-time. In other words, the participant has a reasonable expectation of being able to perform on their DA IFM bids, by T-20, *independent of* any HASP reductions.

While Day-Ahead bilateral markets in the WECC generally limit participation to schedules with Category (1) above to ensure reliability[2], the inclusion of schedules from Category (2), would enable the CAISO to benefit from increased liquidity in the DA IFM markets.

Powerex believes that participant's bids that are awarded in the DA IFM and reduced in the HASP without a corresponding e-tag may reflect virtual bidding activity; and that implicit bidding activity provides *false physical liquidity,* providing no real benefit to the CAISO or its market participants.

With this in mind, Powerex believes that another option that should be explored which is designed to prevent implicit virtual bidding, with no change required to the current E-tagging timeline, is outlined below.[3]

The new rule would be as follows:

Only DA IFM awards that have been e-tagged by the WECC pre-schedule timeline of 1500 can be decreased in the HASP.

[2] The predominant product traded in the bilateral markets in WECC is WSPP Schedule C. This agreement requires an e-tag in the pre-schedule time frame.

[3] Powerex defers to the CAISO to determine the feasibility of this option with respect to any automation and/or system modifications that may be required.

This alternative would still allow those market participants that rely on procuring energy or transmission that becomes available after the DA markets close, to participate in the DA IFM market, provided they have a reasonable expectation of being successful in their procurements:

1. If a participant's IFM award on a respective Resource ID is fully e-tagged by the 1500 WECC timeline, then the participant will be deemed to have demonstrated a physical capability to deliver, and will be eligible to reduce the respective Resource ID in the HASP.
2. If a participant's IFM award on a respective Resource ID is NOT fully e-tagged by the 1500 WECC timeline, then the participant will be deemed to have NOT demonstrated a physical capability to deliver, and will be prevented from reducing their respective Resource ID in the HASP.

Therefore, a participant has a choice – either demonstrate your physical capability in the Day Ahead time frame, or do so by up to T-20.

Since the CAISO has a current penalty mechanism for declines of HASP awards (Tariff Section 11.31), this mechanism would automatically apply to IFM failures to E-tag by up to T-20 (since the HASP award amount could not be less than the IFM award amount for Resource IDs that weren't E-tagged Day Ahead, a failure to deliver on the IFM award would result in the HASP penalty mechanism being applied).

This method:

- Ensures that a participant cannot avoid demonstrating their physical capability, by reducing an award in the IFM in the HASP, without ever E-tagging it.
- Enables participants to procure energy and/or transmission up to the existing T-20 timeline to meet IFM awards, increasing physical liquidity in the CAISO IFM markets.
- Utilizes the existing HASP penalty mechanism.

Powerex believes this option is preferable to Option 1, 2 and 3; however some modifications to this option may be further preferable, including:

1. If prevention of HASP reductions is difficult to achieve by the CAISO technically (and/or in a timely manner), the CAISO could allow HASP reductions, but have the existing HASP penalty mechanism apply to both:
   a. Failures to deliver on HASP awards, and
   b. HASP reductions that were not e-tagged in the Day Ahead time frame.

Or alternatively:

2. If prevention of HASP reductions is difficult to achieve by the CAISO technically (and/or in a timely manner), the CAISO could allow HASP reductions, but have a new penalty mechanism for HASP reductions whereby HASP reductions that were not E-tagged in the Day Ahead time frame are settled:

    a. At the higher of the IFM, HASP and RT price for reductions to IFM imports[4]; or
    b. At the lower of the IFM, HASP and RT price for reductions to IFM exports[5].

Powerex believe this option (and corollaries) would encourage market participants to e-tag most of their IFM awards by the 1500 Day Ahead timeline in order to be eligible to make changes to the schedule in HASP. It clearly identifies which schedules are physical and removes the incentive to engage in 'implicit virtual bidding'. This option also allows the CAISO to properly allocate and administer convergence bidding costs once those market rules become effective.

This option would also address any 'liquidity' concerns associated with earlier E-tagging timelines since all *physical* market participants that have a reasonable expectation of delivering, can still participate in the IFM.

It should be noted that this option also allows all market participants to continue participating in the HASP market. Those not e-tagging their IFM Resource IDs by 1500 in the DA time frame, can still participate in the HASP, on either the import or export side, and avoid financial penalties, by putting in a new bid on a new resource id (they are just prohibited/discouraged from changing the DA IFM resource ID that did not get e-tagged).

6. What comments do you have with the stakeholder timeline?

Powerex appreciates the CAISO initiating this stakeholder process to provide clarity on this issue. While Powerex believes this issue was a significant gap since MRTU go-live, we feel the current timeline for stakeholder engagement is now adequate to move this issue forward.

7. Others?

Powerex has no other comments at this time.

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[4] The logic here is that the CAISO has to go out and make up that supply in their markets so the market participant should be on the hook for the highest priced supply the CAISO had to procure in order to make up the shortage (following cost causation principles).

[5] The logic here is that the CAISO has to go out and sell that excess supply in their markets so the market participant should be on the hook for the lowest priced sale the CAISO had to make in order to (following cost causation principles).