Memorandum

To: ISO Board of Governors

From: Nancy Saracino, Vice President, General Counsel & Chief Administrative Officer

Date: May 9, 2012

Re: **Regulatory Update**

This memorandum does not require Board action.

Regulatory Highlights

- **Order 755 - Compensation for regulation services (ER12- 1630)**

On April 27, 2012, the ISO filed a tariff amendment to comply with FERC's Order 755 directive to compensate regulation resources based on the actual service provided, including both a capacity payment that reflects the marginal unit's opportunity costs and a performance payment that reflects the quantity of regulation service actually provided in response to dispatch signals. These tariff changes are expected to provide additional compensation to resources that are more responsive than other resources. Resources that respond with greater accuracy will also receive higher payments. The Board approved this tariff amendment at its March 2012 meeting. Consistent with the Board's decision, the ISO's filing includes a request to implement Order 755 in the spring of 2013 rather than the fall of 2012.

Responsible attorney: Andrew Ulmer

- **Transmission reliability margin (ER12-1468)**

On April 10, 2012, the ISO filed a tariff amendment seeking approval to revise the sections of its tariff governing the calculation of available transfer capability on ISO intertie scheduling paths in order to allow the ISO to use a transmission reliability margin in certain narrowly defined circumstances. When used, a transmission reliability margin reduces the available transfer capacity for the affected scheduling path by the amount of the transmission reliability margin. The tariff amendment is designed to address operational difficulties that arise, both for the ISO and market participants, when certain conditions cause the transfer capacity of an ISO intertie scheduling path to be reduced after energy schedules have already been awarded in the ISO's hour ahead scheduling process, resulting in cuts to awarded schedules shortly before dispatch. The tariff amendment will address this problem by allowing the ISO to establish, during the hour before the hour-ahead market closes, a transmission reliability margin value that reserves transfer capacity to account for those expected conditions and thereby prevents the award of hour-ahead schedules that are likely to be cut shortly thereafter. The ISO Board approved this proposal at its March 2012 meeting.

Responsible attorney: Burt Gross

ISO complaint to amend the transmission control agreement (EL11-40)

On February 29, 2012, the ISO filed a complaint with FERC to amend the transmission control agreement. The filing of a complaint was necessary since the parties ultimately reached an impasse with respect to the ISO's proposal to revise the standard for a determination of liability or indemnity from an ordinary negligence standard to a gross negligence standard as had been previously approved by FERC with respect to the standard set forth in the tariff. As expected, the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (collectively, the "Six Cities") who had opposed the change in the indemnity standard during the negotiations protested these changes at FERC. The ISO requested an effective date of July 1, 2012 but has asked FERC to issue an order by April 30 to provide greater certainty for Citizens Sunrise Transmission as a new participating transmission owner with respect to its interest in the Sunrise Powerlink transmission expansion project.

Responsible attorney: John Anders

Federal Energy Regulatory Commission and related Court of Appeals matters

Tariff amendments and orders

- **Reliability demand response resource tariff amendment (ER11-3616)**

On February 16, 2012, FERC issued an order rejecting the ISO's proposed tariff amendment to allow reliability demand response resources to participate in the ISO markets. Reliability demand response resources include utility emergency-triggered demand response programs, interruptible, air conditioning, and pumping load programs. The ISO filed a request for rehearing of this order in support of its position on FERC's March 15, 2011 final rule (Order 745) attempting to establish a standardized approach for compensation and cost allocation for certain demand resources in ISO and RTO markets. The ISO's approach to reliability demand response resource participation included application of the same default load adjustment mechanism that FERC had found was not consistent with Order 745. The purpose of the ISO's default load adjustment is to ensure that the ISO does not pay both the load serving entity and the demand response provider for the same curtailment. Separately, the ISO has sought rehearing of FERC's order regarding the ISO's filing in response to Order 745 on January 17, 2012. In addition, the ISO filed a petition with the Court of Appeals for the District of Columbia Circuit on December 27, 2011 of FERC's Order 745 and Order 745-A. Consistent with the ISO position in these other proceedings, the ISO sought rehearing of FERC's order in this proceeding.

Responsible attorneys: John Anders and Sidney Davies

Multi-stage generating resource modeling (ER12-992-000)

On February 3, 2012, the ISO filed a tariff amendment to implement five enhancements to the multi-stage generating unit functionality. Multi-stage generating units include combined cycle generating units and other resources that have multiple operating or regulating ranges. These resources have constraints when transitioning between ranges. The ISO's multi-stage generating unit functionality, which was first implemented in December 2010, allows the ISO to model the distinct operating modes, or configurations, of these generating units. The enhancements in the February proposal include: (1) increasing the number of configurations that a multi-stage unit can bid into real-time from three to six (but continue to allow all registered configurations [up to ten] to be bid in to the day-ahead market) and limiting the number of transition paths for resources that have registered more than six configurations; (2) requiring multi-stage units to bid their entire capacity from the plant level minimum up to the maximum; (3) allowing multi-stage units to specify two ramp rates per configuration; (4) permitting multi-stage units to self-schedule in real-time in a different configuration from the day-ahead; and (5) crediting a multi-stage unit with the lower of the minimum load costs of its metered and committed configurations. On March 27, FERC issued a letter order approving the proposed amendment in its entirety.

Responsible attorney: David Zlotlow

- **Operations and maintenance cost adder (ER12-806)**

On January 13, 2012, the ISO filed a tariff amendment to update the default operations and maintenance adders that are used to calculate minimum load costs and default energy bids. Currently, the tariff provides two default values; $4.00 per MWh for combustion turbines and $2.00 per MWh for all other resources. The tariff proposes to replace the two default values with 10 default values to capture differences in costs by technology as well as fuel type. The new values range from $0 (for wind, for example) up to $5.00 per MWh for biomass. No adverse comments were filed in response to this tariff amendment filing. On March 15, 2012, FERC issued a letter order accepting the tariff changes as filed.

Responsible attorney: Sidney Davies

Regulatory contracts

- **Desert Star Energy Center large generator interconnection agreement (ER12-988 and ER12-989)**

On February 3, 2012, the ISO and the San Diego Gas and Electric Company filed a large generator interconnection agreement with respect to the Desert Star Energy Center generating facility owned by SDG&E (formerly owned by Sempra Generation and known as the Eldorado Combined Cycle generating facility). The ISO and SDG&E filed this conforming LGIA to seek FERC confirmation that the Merchant substation facilities should be characterized as integrated network transmission facilities following the reconfiguration of the Merchant substation that will transition the facilities from the Nevada Power Company balancing authority area to the ISO balancing authority area. FERC issued an order on April 3, 2012 agreeing that the facilities could appropriately be considered integrated network facilities under the ISO's operational control. FERC noted that SDG&E cost recovery for the facilities pursuant to the ISO transmission access charge would be dependent upon the final configuration following the transition. It is currently anticipated the Merchant substation will transition into the ISO balancing authority area in June in accordance with an amendment to the ISO and Nevada Power Company interconnection agreement, which is expected to be filed with FERC prior to the transition.

Responsible attorney: John Anders

- **Nevada Hydro large generator interconnection agreements (ER12-1312 and ER12-1305)**

Nevada Hydro proposes to interconnect its proposed Lake Elsinore Advanced Pumped Storage (LEAPs) hydroelectric pumped storage generating plant to both the SDG&E and SCE transmission systems via a generation tie line. Nevada Hydro submitted its interconnection request to the ISO in 2005, which generated separate interconnection procedures with SDG&E and SCE. On March 21, 2012, the ISO filed a notice of termination of the large generator interconnection agreement (LGIA) between Nevada Hydro, SDG&E and the ISO. The termination is based upon Nevada Hydro's failure to meet contractual milestones to advance the development of the pumped storage facility and because it is not possible to complete the project within the remaining three-year window provided in the applicable generator interconnection process even with revised milestones. Key factual support includes the fact that after seven years in the interconnection queue, Nevada Hydro was required in 2012 to reapply for a pumped storage license at FERC and the fact that the water district whose water facility was integral to the generating facility upon which the interconnection request was founded is no longer involved with the project. On April 11, Nevada Hydro filed a protest in response to the ISO's termination notice arguing that it has the right to continue to postpone milestone the dates.

With respect to the SCE proposed interconnection, the ISO filed the unexecuted SCE LGIA with FERC on March 21, 2012, simultaneously with ISO's filing of the notice of termination of the San Diego LGIA. The ISO did so because Nevada Hydro exercised its right under the serial LGIP to require that the LGIA be submitted to FERC when the parties are at an impasse as to the final LGIA terms. On April 11 Nevada Hydro filed its protest arguing that the dispute over final terms between SCE, ISO and Nevada Hydro results from the "dual nature" of the generation line interconnection with both SDG&E and SCE to interconnect the LEAPS project and to develop transmission line to loop SCE and SDG&E's transmission systems. Nevada Hydro seeks to structure the LGIA to first accomplish construction of the tie line and then accomplish interconnection of the LEAPS generation facility, arguing that the transmission line can be completed within the ten year window. In its answer to protest, the ISO argued that Nevada Hydro is inappropriately attempting to substitute its transmission project for the LEAPS project. For the same reasons discussed above with respect to the SDG&E LGIA, the ISO is also urging FERC to reject the LGIA in its entirety as the LEAPS project clearly cannot be completed within the ten year window.

Responsible attorney: Bill Di Capo

- **Dynamic transfer agreements with the Balancing Authority Area of Northern California (ER12-1636 and ER12-1637)**

On April 27, 2012, the ISO filed two agreements that will replace the pilot pseudo-tie contractual arrangements that were previously agreed to and accepted by FERC. A pseudo-tie resource is a physical resource located outside the ISO's balancing authority area that participates as if it were in the ISO's balancing authority area. The replacement agreements include the umbrella Dynamic Transfer Balancing Authority Operating Agreement between the ISO and the Balancing Authority of Northern California ("BANC") and the resource specific Pseudo-Tie Agreement among the ISO, BANC, Western Area Power Administration – Sierra Nevada Region ("Western"), and PG&E. These agreements are necessary for continuation of the pseudo-ties between the ISO and BANC consistent with the dynamic transfer provisions of the tariff approved by FERC in the fall of 2011. The umbrella agreement addresses both dynamically scheduled resources and pseudo-tie resources. At this time there are two pseudo-ties between the ISO and BANC, one from the ISO to BANC with respect to Western's New Melones hydroelectric generating facility and one from BANC to the ISO with respect to Calpine's Sutter Energy Center. There are no dynamically scheduled resources between the ISO and BANC at this time. Additional pseudo-tie resources or dynamically scheduled resources could be supported with agreement of the ISO and BANC. The companion resource specific agreement for the New Melones hydroelectric generating facility references pseudo-tie requirements in the tariff and has been agreed to by the ISO, Western, BANC, and PG&E.

Responsible attorney: John Anders

Rulemakings

Order 760 --Electricity market surveillance and analysis (RM11-17-000)

In October of last year, FERC released a notice of proposed rulemaking to require all independent system operators and regional transmission operators (ISOs/RTOs) to provide FERC with a continuous stream of essentially all market data. This ongoing obligation would replace periodic ad hoc data requests. FERC intends to use the market data for monitoring and surveillance of the individual ISO/RTO markets. FERC would also use the information to monitor issues occurring at the seams between different ISO/RTO markets and between an ISO/RTO market and non-ISO/RTO market. On April 19, 2012, FERC issued Order 765, which adopts most of the major proposals published in the notice of proposed rulemaking. Order 765 requirements will be phased-in. Starting in early August, all ISOs/RTOs will have to begin providing FERC with all supply offers. Other data streaming obligations will be phased in over the following months. By late January of 2013, ISOs/RTOs would be responsible for full compliance, streaming essentially all market data.

Responsible attorney: David Zlotlow

Report filings

- **Interconnection Queue Quarterly Progress Report; Q1 2012 (ER08-1317; ER11-2830)**

On April 30, 2012, the ISO submitted its Q1 2012 quarterly report on progress in processing the generator interconnection queue. In its report, the ISO noted that the second financial security posting deadliness for cluster 1 and 2 customers came due in Q1, and that 6 projects withdrew, leaving 37 projects. In addition, the ISO noted that the first financial posting deadline came due for cluster 3 customers in Q1, causing 69 projects to withdraw and leaving 99 interconnection customers. The application window for cluster 5 was March 1-31. The ISO is in the process of reviewing these interconnection request applications.

Responsible attorney: Bill Di Capo

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

A market disruption is an action or event that causes a failure of an ISO market, related to system operation issues or system emergencies. The ISO reports these market disruptions to FERC on a monthly basis. On March 15, 2012, the ISO submitted its monthly report of market disruptions that occurred from January 16, 2012 through February 15, 2012. On April 16, 2012, the ISO submitted its monthly report of market disruptions that occurred from February 16, 2012 through March 15, 2012. 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.

Responsible attorney: Anna McKenna

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

The ISO submits two types of monthly exceptional dispatch reports to FERC. On March 15 and April 13, 2012, the ISO submitted transactional data including incremental and decremental MW volume, duration and location for exceptional dispatches occurring during the months of January and February, 2012, respectively. On March 30 and April 30, 2012, the ISO submitted MW hour data and cost data for exceptional dispatches occurring during the months of December, 2011 and January 2012, respectively. An exceptional dispatch is a dispatch or a commitment issued by the ISO to a resource outside of the operation of the ISO market to address operational needs that cannot be address by the ISO market.

Responsible attorney: Sidney Davies

Other FERC matters

- **Capacity procurement mechanism waiver for Sutter Plant (ER12-897)**

As described in greater detail in the March 15, 2012 regulatory report, on January 25, 2012, the ISO submitted a petition requesting that FERC waive applicable tariff provisions to prevent the retirement in 2012 of the Sutter Energy Center, an existing flexible, combined cycle facility owned by Calpine Corporation. On April 26, 2012, FERC issued an order granting the ISO's motion to hold FERC action on the waiver petition in abeyance. FERC found that a March 22, 2012 CPUC resolution initiated a process whereby the investor-owned utilities will negotiate with Calpine with the goal of securing a contract that will keep the Sutter plant in operation during 2012. FERC acknowledged that the CPUC resolution does not guarantee that Calpine will successfully negotiate a contract with the investor-owned utilities, but found that it was appropriate to delay action on ISO's waiver request until the state process is completed. FERC rejected arguments by NRG in opposition to ISO's motion and noted that Calpine, the party most directly affected by FERC's action, did not oppose ISO's motion.

Responsible attorneys: Anthony Ivancovich and Anna McKenna

<u>California Public Utilities Commission matters</u>

- **Resource adequacy proceeding for compliance year 2013 (R.11-10-023)**

The ISO filed comments urging the CPUC to modify the resource adequacy program to ensure that the ISO has sufficient flexible capacity available to manage the operational needs and maintain the reliability of the electric grid as the system undergoes significant transformation with the addition of renewable resources to meet the renewable portfolio standard of 33 percent, and the simultaneous reduction of a potential 12,079 MWs of existing generation that uses once-through cooling technology. The ISO proposed that the CPUC adopt the ISO's proposal to create the framework for flexible capacity to be considered in the resource adequacy program by taking the following actions: (i) adopt the

ISO's three flexible capacity categories as advisory targets for 2013; (ii) find that either a companion track or new resource adequacy proceeding should be launched in Summer 2012 to directly address the nature and implementation of a flexible capacity requirement for resource adequacy compliance year 2014; and (iii) require that load-serving entities show all resource adequacy resources procured at the 90% level for each of the twelve months of 2013. In addition, on April 30, 2012, the ISO filed its 2013 Local Capacity Technical Analysis for consideration in the 2013 resource adequacy requirements program. These results will also be used by the ISO as local capacity requirements.

Responsible attorney: Beth Ann Burns

- **Demand response programs for 2012-1014 (A.11-03-001, 002, 003)**

On April 19, 2012, the CPUC issued a final decision approving utility demand response programs and budgets for the 2012-2014 period. The ISO and third party demand response providers argued for a transition from a utility-centric demand response model toward a competitive solicitation model for demand response procurement. The decision directs that this issue be considered within the ongoing demand response proceeding R01-07-001 or a successor docket addressing global demand response issues.

Responsible attorney: Bill Di Capo

- **Augmentations to demand response programs for 2012 (SCE Advice Letter 2721-E; SDG&E Advice Letter 2351-E)**

On April 25th, the CPUC Energy Division sent a letter to SCE and SDG&E requesting that they file advice letters proposing additional programs in their service territories for summer 2012, focusing on areas potentially affected by the SONGS outage (e.g., south Orange County and the greater San Diego region). In its advice letter, SCE proposes to expand its "Schedule 10/10" program, a summer program available to non-residential customers. SCE estimates that the potential system peak demand reduction in the Orange County area to be approximately 12 MW. In its filing, SDG&E proposes an expansion of its commercial stand by-generator demand response program. On May 3, the ISO submitted comments proposing that the CPUC consider modifying all available IOU <u>non-emergency</u> demand response programs so that they would be triggered whenever the ISO has issued an alert or warning notice. While the CPUC Energy Division letter did not request PG&E to consider demand response program augmentation, the ISO asked the CPUC to modify all three utilities non-emergency demand response programs.

Responsible attorney: Bill Di Capo

Rulemaking concerning long-term procurement plans (R.12-03-014)

The CPUC initiated the new, two year, long term procurement proceeding on March 22, 2012 with a preliminary scoping ruling. The ISO submitted comments on the ruling on April 6, 2012, urging the CPUC to address local area capacity needs, driven by once-through cooling requirements, in the Los Angeles and Big Creek/Ventura areas consistent with the ISO's once-through cooling study conducted with several state agencies as part of the 2011/2012 transmission planning cycle. The ISO emphasized the importance of a decision on local area capacity needs by the end of 2012 so that load serving entities will have sufficient time to conduct power purchase solicitations and procure any necessary new generation to be available to replace retired once-through cooling units.

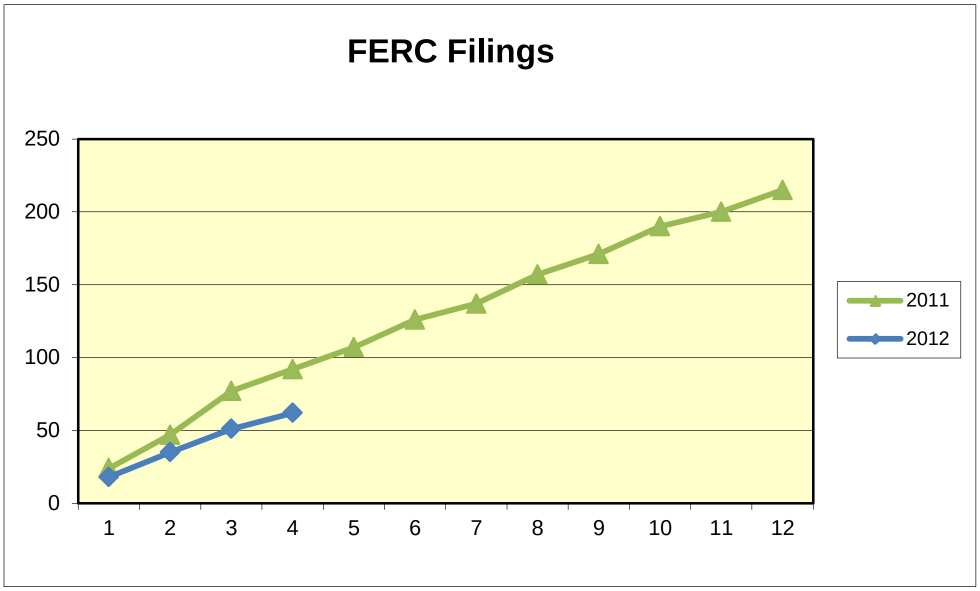
Responsible attorney: Judi Sanders

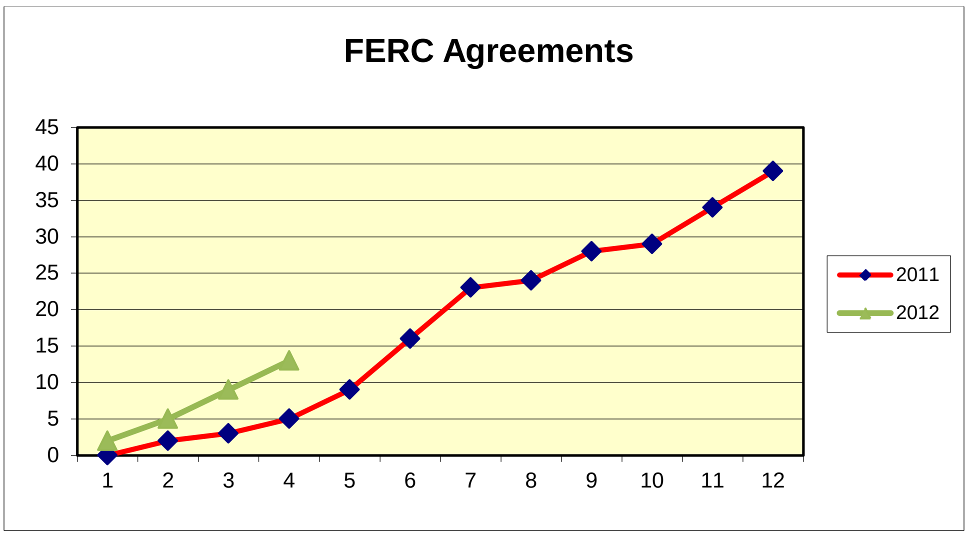
Application of SDG&E to enter into power purchase agreements (A.11-05-023)

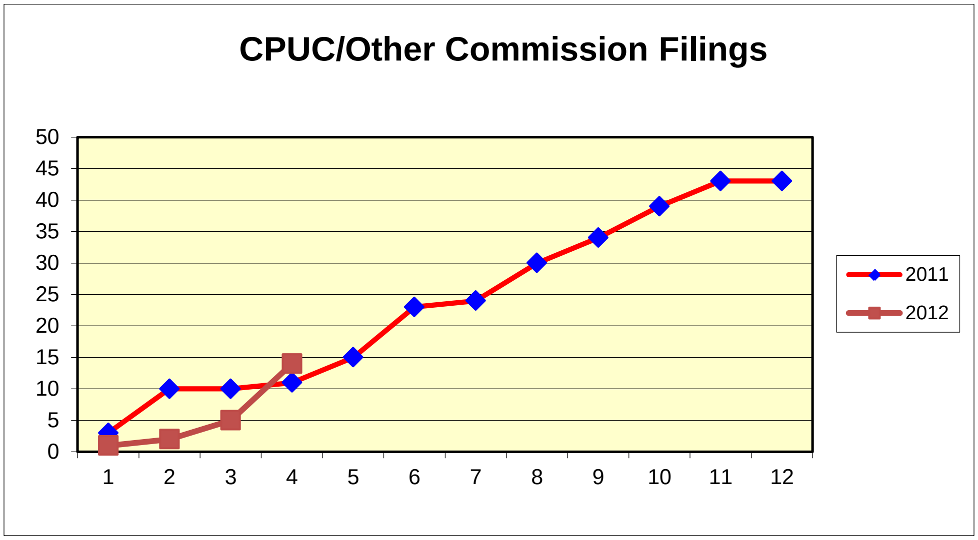
This proceeding involves the application of SDG&E for approval of purchase power tolling agreements with three generating facilities: Escondido Energy Center, Pio Pico Energy Center and Quail Brush Power. Because the approval of these agreements is contingent on a finding that these resources are needed to meet local capacity needs in the San Diego area, the CPUC deferred consideration to this docket. The ISO has filed its local capacity requirements and once through cooling studies and these studies show a substantial need for generation in the San Diego and greater San Diego/Imperial Valley local areas. The ISO intervened in the proceeding on February 24, 2012 and agreed to provide testimony supporting its study results for the purposes of assisting the CPUC with a decision on local needs. ISO filed testimony on March 9, 2012 and supplemental testimony on April 6, 2012.

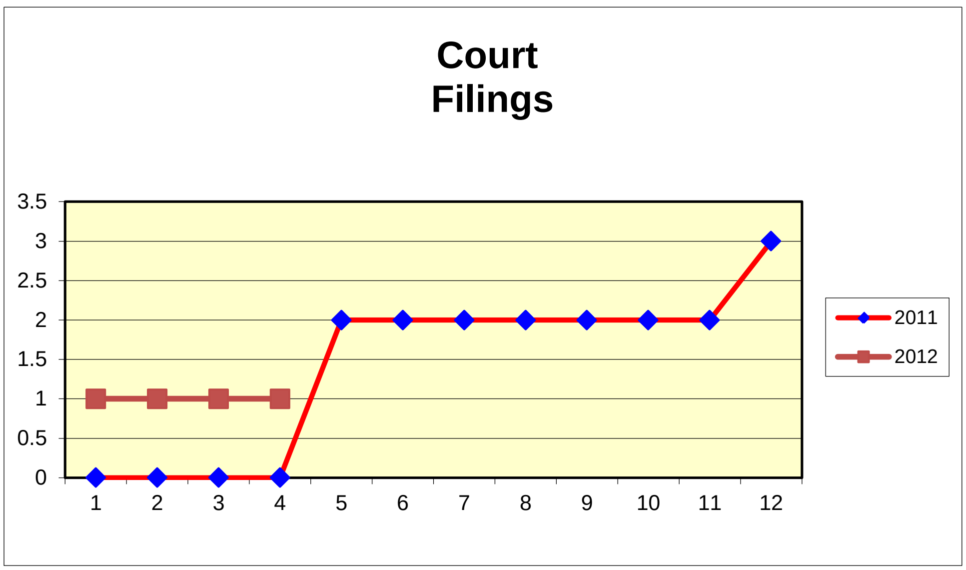
Responsible attorney: Judi Sanders

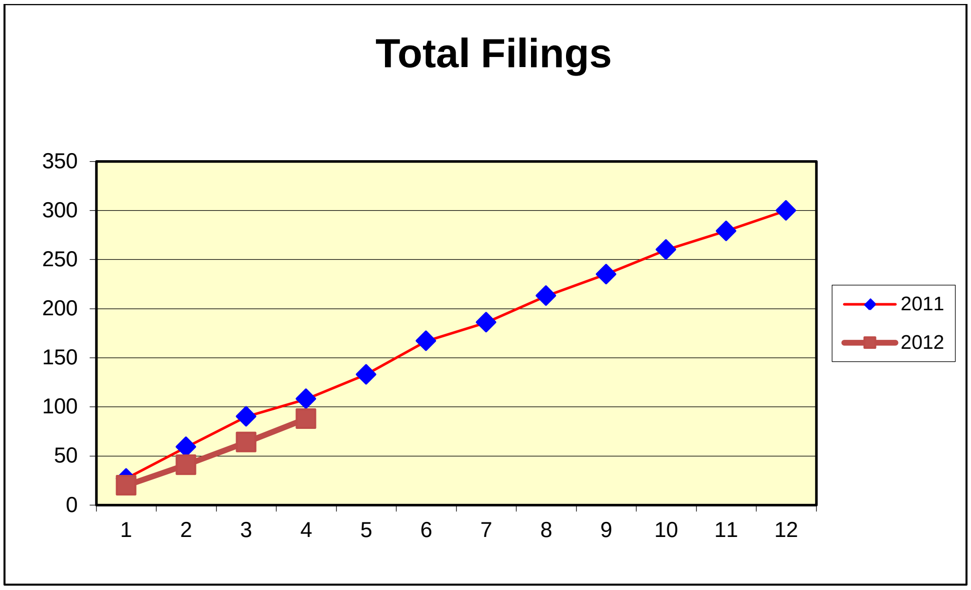
Regulatory Filings Through April 2012






CPUC/Other Commission Filings
50
45
40
35
30
25
20
15
10
5
0
1
2
3
4
5
6
7
8
9
10
11
12
2011
2012


Court
Filings
3.5
3
2.5
2
1.5
1
0.5
0
1
2
3
4
5
6
7
8
9
10
11
12
2011
2012


Total Filings
350
300
250
200
150
100
50
0
1
2
3
4
5
6
7
8
9
10
11
12
2011
2012