



CALIFORNIA ISO

California Independent
System Operator

February 2, 2004

The Honorable Magalie Roman Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, DC 20426

**Re: California Independent System Operator Corporation,
Docket No. ER02-1656-009, 010 and 011 and Investigation of
Wholesale Rates of Public Utility Sellers of Energy and
Ancillary Services in the Western Systems Coordinating
Council, Docket No. EL01-68-017**

Dear Secretary Salas:

Enclosed for filing in the above-captioned dockets, please find the Status Report of California Independent System Operator Corporation ("ISO").

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Charles F. Robinson', is written over a horizontal line.

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

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| California Independent System Operator Corporation |) | Docket No. ER02-1656-000 |
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| Investigation of Wholesale Rates of Public Utility Sellers of Energy and Ancillary Services in the Western Systems Coordinating Council |) | Docket No. EL01-68-017 |
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**STATUS REPORT OF THE
CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION**

The California Independent System Operator Corporation ("ISO")¹ respectfully submits this monthly progress report ("Report") in compliance with the Commission's November 27, 2002 "Order Clarifying The California Market Redesign Implementation Schedule", 101 FERC ¶ 61,266 (2002) ("November 27 Order"), issued in the above-referenced dockets.

The November 27 Order required the ISO to file reports on the first Monday of each month, beginning in January 2003, to update the Commission on the ISO's progress in designing and implementing the market redesign effort. The Commission directed the ISO to file a full market redesign implementation plan, including a detailed timeline with the sequential and concurrent nature of the design elements, the software and vendors (once selected) to be used and the cost estimates for each element. The November 27 Order required that the first report include explanations of the following: (1) any alternative methods of

developing market redesign elements; (2) the ISO's progress in developing the market redesign elements; (3) the action required to establish such elements; and (4) a detailed breakdown of the total start-up costs.² The Commission directed the ISO to update the market redesign implementation plan on a monthly basis, indicating the progress made and the upcoming steps.

On January 10, 2003, the ISO filed its first Status Report in compliance with the November 27 Order. Subsequent to the first filing, the ISO continues to file monthly Status Reports with the Commission on the first Monday of each month. The instant Report is intended to satisfy the monthly reporting requirement in the November 27 Order, update the information included in prior Status Reports and generally advise the Commission of the current status of the market redesign implementation effort.

I. FEBRUARY STATUS REPORT

Sections A and B include a narrative of the significant changes to the "Program Plan – High Level" schedule activity that have occurred since the filing of the prior month's Status Report. Section C includes a narrative regarding the budget along with an updated Budget Tracking and Status Report³. Section D identifies the ISO's key market redesign implementation issues including the previous month's accomplishments, major milestones, upcoming activities, issue

¹ Capitalized terms not otherwise defined herein are used in the sense given in the Master Definitions Supplement, Appendix A to the ISO Tariff.

² November 27, Order at P 9.

³ The narrative includes only non-confidential information.

resolution with stakeholders and items requiring timely resolution by the Commission in order to meet the project schedule.

A. Phase IB Status

Overall: Phase IB involves implementing software that (1) contains an economic dispatch algorithm to clear overlapping Real-Time Energy bids continuously so that there will be a single price in each five-minute interval, and (2) allows, *inter alia*, generators to modify unit availability in Real-Time and enable the ISO to impose penalties for uninstructed deviations. The ISO continues to assess the Phase IB implementation date and will apprise the Commission of the final “go-live” date upon completion of the assessment.

Market Simulation: On January 23, 2004, the ISO and participants completed the second round of market simulation with the focus being the customized dispatch scenarios with the 23 key participants. The ISO did not run a market simulation the last week of January to allow both participants and the ISO to update their systems so changes can be tested when market simulation resumes on February 2nd. The ISO conducted one-on-one conference calls with the 23 participants from January 26-29, 2004. The purpose of the calls was to (1) review the dispatch scenarios and revise as needed and 2) obtain additional feedback from each participant about their own readiness assessment for implementing Phase IB. Participants were asked to provide a self assessment in three categories: 1) current status, 2) operational readiness and 3) organizational readiness.

In the January 12, 2004 Status Report, the ISO reported that it conducted its own readiness assessment in mid-December evaluating the Phase IB schedule, resource allocation, risks and impacts. The ISO identified critical areas, which included training, system application development and testing and hardware upgrades of existing Infrastructure hardware. The upgrades to the Infrastructure hardware is on track to be completed March 1, 2004.

Training: In the January 12, 2004 Status Report, the ISO reported that certain preconditions must be met prior to starting hands-on operator training, including 1) operator screens being in place; 2) operating procedures updated to reflect Phase IB modifications; 3) operator roles and responsibilities clearly defined; and 4) a training environment adequate for detailed hands-on training. Operator roles and responsibilities have been clearly defined and the operating procedures are targeted for completion the first week of February 2004. Training environment issues have been resolved and development of the remaining operator screens are scheduled for completion the second week of February 2004. The ISO's operator hands-on training will begin on February 23, 2004 and conclude on March 31, 2004, as scheduled.

System Application Development and Testing: The balance of system application development and testing, including load and performance testing, is scheduled for completion mid-March 2004. The ISO continues to assess the critical areas and has received delivery commitment dates from key parties. Certainty for the implementation date cannot be known until these critical

elements are delivered and tested, and at that time the ISO will be able to determine the "go-live" date.

Phase IB Weekly Conference Calls: The ISO continues to hold weekly conference calls every Friday. The conference calls are open to all Market Participants and are structured to keep stakeholders informed about the progress of Phase IB implementation and respond to questions.

Market Simulation Exit Criteria: The ISO will assess the success of January's market simulation against the Exit Criteria with the participants during the January 30, 2004 conference call. The purpose of the Exit Criteria is for both the ISO and participants to determine when market simulation can be deemed complete and successful.

B. Integrated Forward Market/Locational Marginal Pricing Status

Siemens Power Transmission and Distribution Inc. was awarded the contract for providing the software, installation, licenses and maintenance of a software system to execute an optimized forward energy market using a full network model, produce locational marginal prices and execute a real-time dispatch using a full network model to produce nodal prices.

C. Market Redesign Budget Update

Attachment A -- the Budget Status and Tracking Report is not being provided this month as the overall program budget is under review by an independent consultant (as mentioned in the January report) who was hired at the request of the ISO Board of Governors. Although the independent consultant

gave a status report to the Board at their January 22nd meeting, it is anticipated that the consultant will make his complete assessment, including recommendations of the format of the budget reporting going forward, at the February meeting. Until such time as the Board accepts his report, the budget information would be incomplete to continue reporting in the format we have used to date: the current format only provides limited information of overall program costs and focuses on reporting of expenditures. Now that the core of the project is moving to the execution stage, and contracts are being negotiated and signed with vendors, a comprehensive and more complete forecast of overall costs projections can be made. The Budget Status and Tracking Report will be re-formatted to incorporate this information and provided in future monthly Status Reports. The Budget Status and Tracking Report will remain confidential until such time that the information contained in the report does not disclose confidential business information or jeopardize the ISO's negotiations with vendors regarding implementation of the market redesign.

D. Key Issues

1. Settlements and Market Clearing Request for Proposals

During December 2003, the Settlements and Market Clearing Request for Proposal ("RFP") Evaluation team selected a preferred vendor for the Settlements portion of the original RFP. The ISO started contract negotiations with the preferred vendor on January 8, 2004. Based on the Settlements evaluation process, the ISO bifurcated the Settlements and Market Clearing RFP. The ISO issued a Market Clearing Request for Bid

("RFB") on December 22, 2003 and the ISO received responses from four of the seven vendors who were issued the Market Clearing RFB on January 16, 2004. The ISO is currently evaluating the potential vendors' responses and is targeting completing its review process and vendor selection by the first week of February 2004.

2. Locational Marginal Pricing Studies

The ISO published the "Preliminary Analysis of Market-Based Price Differentials" on October 6, 2003 based on the ISO's third Locational Marginal Pricing ("LMP") Price Dispersion Study. The production and analysis of the model results is nearing completion for the final LMP Price Dispersion Study, which will be completed and published early in 2004. This report will include simulation of a full year of LMPs using the market bids submitted in the ISO's current zonal market, and will be followed by monthly reports with additional results for months subsequent to the period examined in the end-of-year report.

3. Congestion Revenue Rights Study

The ISO began holding bi-weekly Congestion Revenue Rights ("CRR") conference calls with Market Participants on January 26, 2004. The purpose of the calls is to solicit input into the second Congestion Revenue Rights Study. The purpose of the second CRR Study is to investigate the approximate quantity of CRR allocations that load-serving entities will need in order to maximize their hedge against congestion costs. Such a determination depends on an assessment of both (a) simultaneous feasibility of releasing particular configurations of CRRs, and (b) the revenue stream going to the CRR holders,

based on estimated Locational Marginal Prices. The ISO anticipates completing the second CRR Study in early November 2004.

In response to Market Participants' request for a common level of understanding CRRs, the ISO is developing a series of classes. The classes will begin in February 2004 and will include the following topics:

- CRR Educational Materials Overview
- CRR Basics
- Shift Factors
- Pricing and Aggregate Pricing Nodes
- Load Distribution Factors
- Operating Constraints
- Allocation Process
- Locational Marginal Pricing Basics
- Settlements

4. CPUC Procurement Proceedings

On January 22nd, the California Public Utilities Commission ("CPUC") issued a decision on the threshold issues regarding the procurement requirements for California. Among other things, they addressed certain elements of resource adequacy such as a planning reserve margin of 15-17% that allows for the "lumpiness" of investment but must be met by January 1, 2008. This requirement has interim benchmarks to create a gradual phase-in period over the next few years. In addition, the decision establishes a capacity obligation where each utility must procure "90% of summer (May through

September) peaking needs (loads plus planning reserves) one year in advance". Further, the CPUC stated it will open a new "procurement related Order Instituting Ratemaking ("OIR")", in the first quarter of 2004. Therefore, the ISO anticipates the CPUC issuing further decisions regarding additional resource adequacy issues over the coming months. The ISO is currently performing a detailed review of the current decision to determine its impact on the ISO's MD02 proposal.

II. CONCLUSION

In Section I of this Report, the ISO has responded to the Commission's request for specific information on progress, critical issues, budget and alternative methods for the market redesign implementation effort. The ISO appreciates having the opportunity to comment and report on the progress being made on its market redesign.

Respectfully submitted,



Charles F. Robinson
Anthony J. Ivancovich


Counsel for the California Independent
Operator Corporation

Dated: February 2, 2004

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon the Public Utilities Commission of the State of California, upon all parties of the official service lists maintained by the Secretary for Docket Nos. ER02-1656-000 and EL01-68-017.

Dated at Folsom, California, this 2nd day of February 2004.


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