

**COMMENTS OF THE
TRANSMISSION AGENCY OF NORTHERN CALIFORNIA
ON THE CALIFORNIA ISO'S PROPOSAL ON MODELING AND PRICING OF
INTEGRATED BALANCING AUTHORITY AREAS**

FEBRUARY 20, 2008

Pursuant to the California Independent System Operator Corporation's ("ISO") Market Notices of February 13, 14 and 19, 2008, the Transmission Agency of Northern California ("TANC") provides these comments concerning the ISO's proposal for modeling and pricing of Integrated Balancing Authority Areas ("IBAA's"), including as to the ISO's (January 22, 2008) version of the draft Tariff language on IBAA's and the ISO's (February 6, 2008) version of the Illustrative Draft Full Network Model Business Practice Manual ("FNM BPM"). These comments address TANC's concerns with respect to: (1) the adverse impacts of the IBAA proposal on TANC and its Members on use of the California-Oregon Transmission Project ("COTP"); (2) on TANC Member Congestion Revenue Right ("CRR") holders; and (3) the ISO's stakeholder process for developing the IBAA proposal. In addition, TANC presents questions that are necessary to assist in its review of the ISO's IBAA proposal.

At the outset, TANC notes its understanding that the ISO has clarified that the above-mentioned Market Notices concerning IBAA's are not intended to limit the opportunity for additional questions and comments narrowly to the draft Tariff language and the draft illustrative FNM BPM language. Such artificial constraints, and the similar constraints imposed on stakeholders during the February 7, 2008 ISO IBAA conference call, would severely limit the potential for a robust stakeholder process. The adverse impacts on TANC and its Members from the ISO's IBAA proposal is of grave concern, and warrants a discussion far broader than one limited to the Tariff language and FNM BPM.

The first concern is that the ISO studies in support of its IBAA proposal use inaccurate information. They are based on a time-period prior to the COTP's relocation from the ISO Balancing Authority Area ("BAA") to the SMUD/Western BAA on December 1, 2005. Given the substantial implications of the COTP's relocation to the SMUD/Western BAA, the ISO's use of outdated data is a serious deficiency that should be remedied before the ISO finally considers its IBAA proposal.

TANC's second concern is that the ISO's IBAA proposal appears to inappropriately decrease the value of the COTP by pricing TANC and its Member transactions that utilize the COTP at Captain Jack. The ISO states its lack of understanding of this concern. *See* "CAISO Responses to Questions" on IBAA's, p. 7 (Posted on ISO Website on February 15, 2008) ("February 15 Response"). TANC notes, however, that the ISO has not adequately supported through studies or analyses its use of this price point for TANC and its Member COTP transactions. The ISO's IBAA

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proposal fails to recognize the value of the COTP, which among other reasons, was built to recognize the economic value of being able to move power from the Pacific Northwest to California. Furthermore, with respect to the ISO's statement on page 6 of the February 15 Response, that if "a source is not identified a TRACY_500 (COTP) schedule will be modeled at the CAPTJACK 500 by default," the ISO has not explained how using Captain Jack as a price point for non-ISO Controlled Grid facilities improves the modeling accuracy of the ISO Controlled Grid.

The IBAA proposal also adversely affects the value of CRRs allocated to certain TANC Members. The ISO explains in its February 15 Response at page 7, that "if an entity wishes to hedge potential CAISO congestion costs related to an import to the CAISO Controlled Grid from the SMUD IBAA where that import is sourced at Captain Jack, the entity need procure a CRR from (source) Captain Jack to the SMUD hub (sink)." TANC and its Members were not aware of this methodology during the CRR nomination process. Thus, it appears that the ISO has changed the rules upon which certain TANC Members relied to nominate CRRs including for future deliveries from the COTP. The ISO's failure to provide adequate notice as to the CRR nomination process has adversely impacted those TANC Members that planned to use the COTP asset in conjunction with any CRRs they held.

TANC is also concerned with the ISO's IBAA proposal on the issue of losses, including that TANC and its Members using the COTP could face duplicate charges for losses in light of the ISO's IBAA proposal to assess ISO losses for COTP imports at Tracy. While on page 19 of the February 15 Response the ISO notes that it does not "manage or price congestion or losses on the IBAA's system," the ISO's explanation does not take into account that the ISO includes losses in the price it applies for COTP transactions at Captain Jack. From this, it appears that the ISO does, in fact, intend to assess losses for TANC and its Members' COTP transactions. The ISO's failure to completely explain the affect of its IBAA proposal as to the issue of losses for the COTP leave TANC's concerns unresolved. Therefore, TANC's concern remains that TANC and its Members' use of the COTP will be unreasonably assessed ISO losses.

Further, TANC has concerns with the discretion the ISO affords itself in its IBAA proposal. For instance, the ISO claims that if it "cannot obtain agreement from the affected BAA, the CAISO will determine the appropriate weighting factors based on available information." February 15 Response at 2. The ISO does not provide a justifiable basis for pricing IBAA's based on this proposal and provides no safeguards to ensure that it will take appropriate measures to consult with IBAA's to ensure the accuracy of its "available information." The ISO also provides no support for its assertion that "since the weighting factors will be determined based on the physical characteristics of, and resultant power flows on, the system in question, the CAISO does not anticipate that it will be difficult to agree on or determine the appropriate factors." February 15 Response at 2.

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With respect to the ISO's February 15, 2008 indication that "the weighting/Intertie Distribution Factors used to determine hub prices will be listed in the BPMs," the proposal to relegate such pricing information to the BPMs is contrary to the FERC's "rule of reason." February 15 Response at 2. Pricing details, including distribution factors and weighting and pricing nodes, have a significant impact on rates, terms, conditions and charges and must be included in the Tariff rather than left to the BPMs. The ISO's blanket statement on page 21 of the February 15 Response, that it has "struck the right balance of tariff language that reflects the rates terms and conditions as it pertains to IBAAAs," does not resolve TANC's concerns that the complete modeling and pricing provisions of the ISO's IBAA proposal, as well as provisions on defining and modifying existing IBAAAs, are absent from the ISO's draft Tariff. Also of concern is the ISO's proposal to provide illustrative BPM language for now and to make "more broad reaching conforming changes" to the BPMs "in the next releases of the BPM." February 15 Response at 21. The ISO fails to adequately vet the IBAA proposal with stakeholders when undetermined amounts of information relevant to the modeling and pricing of IBAAAs has yet to be provided to stakeholders for review.

The ISO's February 19, 2008 Market Notice indicates that the ISO has established a March 6, 2008 stakeholder meeting in Folsom. The February 19, 2008 Market Notice indicates that the purpose of the March 6, 2008 meeting "is to further discuss elements of the CAISO IBAA proposal and the draft tariff language." In light of the significant concerns that have been raised with the substance of the IBAA proposal, including as to the basis for applying the proposal on a piecemeal and discriminatory manner, the ISO is ill-advised in rushing to implementation issues. Instead, the ISO should ensure that the March 6, 2008 stakeholder meeting is conducted in a format that provides all stakeholders and participants with all relevant substantive information, including technical analyses and studies (that use accurate and relevant data), on the basis and authority (including boundary limits) for its IBAA proposal.

Finally, TANC seeks the ISO's response to the following questions concerning the ISO's IBAA proposal:

1. Please provide the data that supports the ISO's answer on page 6 of the February 15 Response that provides in pertinent part, "The CAISO determined that injections at Captain Jack (Northern terminus of the COTP) have a materially different impact on the CAISO Controlled Grid than injections from either the SMUD hub (as defined) or the Western hub."
2. Please reconcile the ISO's statement on page 28 of the February 15 Response that it does not intend to "establish prices internal to the IBAAAs system" with its establishment of the Captain Jack price point.
3. Please provide the ISO's studies and data quantifying cost to the ISO or its markets from pricing COTP transactions by TANC and its Members at Tracy versus Captain Jack?

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4. Please provide the ISO's studies and data quantifying the incremental benefit to the ISO or its markets from modeling COTP deliveries at Captain Jack versus Tracy?
5. Please confirm that scheduling at Tracy will be unaffected by pricing COTP transactions at Captain Jack.
6. The ISO acknowledges that a significant factor in its determination to establish the SMUD/Western and TID IBAA's was based on data of a time period prior to the COTP's relocation to the SMUD/Western Control Area. *See* February 15 Response at p. 20. Please explain: (1) has or will the ISO revise its studies with current data reflecting the COTP's location in the SMUD/Western Control Area, and if so, what were the results of those studies; and (2) if not, what is the basis for the ISO's belief that reliance on the old data is reasonable?
7. Reference page 35 of the ISO's Modeling and Pricing of IBAA's Presentation (1/22/08 Update) where the ISO provides three reasons as to why the ISO claims it is "important to settle schedules where they are modeled." Please explain in detail how the ISO's IBAA proposal as it applies to the COTP: (1) ensures LMP of schedules are consistent with the bid used; (2) minimizes Bid Cost Recovery Uplift; and (3) ensures price signals are consistent with the system needs.
8. Please provide the ISO's quantification of the difference in bid price recovery uplift for pricing TANC and its Members COTP use at Captain Jack versus Tracy.
9. Please explain how "compensating injections" as described on page 9-10 of the February 15 Response helps minimize Bid Cost Recovery Uplift as it applies to the COTP.
10. On page 20 of the February 15 Response, the ISO lists the indicative criteria that, among others, is used to identify and determine IBAA's. Please provide for each of the six listed criteria on page 20, and any other criteria considered, all data and analyses that the ISO used to model and treat the SMUD/Western and TID systems as IBAA's. If the information has previously been provided for each of the criteria, please indicate specifically when the information or data was provided.