UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	))	**Docket No. ER04-938-002**

ANSWER OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION TO REQUEST FOR REHEARING AND CLARIFICATION OF THE JULY 26, 2005 ORDER AND MOTION FOR LEAVE TO FILE ANSWER

On July 26, 2005, the Commission issued its Order on Rehearing and Compliance Filing in the captioned proceeding, 112 FERC ¶ 61,136 ("July 26, 2005 Order"), which concerns Amendment No. 61 to the California Independent System Operator Corporation ("ISO") Tariff.[1] On August 24, 2005, Coral Power, L.L.C., Energia Azteca X, S. de R.L. de C.V., and Energia de Baja California, S. de R.L. de C.V. (jointly, the "Coral Group") submitted a request for rehearing and clarification of the July 26 Order. Pursuant to Rules 212 and 213 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §§ 385.212, 385.213 (2005), the ISO hereby submits its answer to the Coral Group's motion for clarification and request for rehearing. To the extent the Commission believes that the ISO's answer pertains to Coral's request for rehearing as opposed to the motion for clarification, the ISO respectfully requests leave to file an answer to the Coral Group's request for rehearing.[2]

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[1] Capitalized terms not otherwise defined herein have the meanings set for in the Master Definitions Supplement, Appendix A to the ISO Tariff.

[2] To the extent necessary, the ISO seeks waiver of Rule 213(a)(2) (18 C.F.R. § 385.213(a)(2)) to permit it to submit an answer to the Coral Group's request for rehearing. Good cause for this waiver exists because this answer will assist the Commission in its understanding of the proceeding and its decision-making process. *See, e.g.*, *Williams Energy Marketing &*

As explained below, the Coral Group's filing is a collateral attack on the Commission's August 17, 2004 order in this proceeding, 108 FERC ¶ 61,193 ("August 17, 2004 Order"). On this basis alone, the request for rehearing should be rejected. Moreover, the Coral Group persists in misunderstanding the Commission's orders in this proceeding and in the Amendment 50 proceeding and the distinction between the two different categories of decremental reference prices ("DRPs") approved by the Commission. That misunderstanding underlies the entirety of the Coral Group's filing. Accordingly, the Commission must deny the relief that the Coral Group requests.

I. ANSWER

A. The Coral Group's Filing is a Collateral Attack on the August 17, 2004 Order, and Therefore Should be Rejected.

The Coral Group erroneously alleges that, in the July 26, 2005 Order, the Commission "appears to have unilaterally revised" the five-tier pricing formula contained in Section 7.2.6.1.1 of the ISO Tariff and previously approved by the Commission. Coral Group at 7.[3] The Commission language to which the Coral Group points is the statement that, during the period when a generating unit is shut down to manage Intra-Zonal Congestion, "the production reduction resulting from the shut down is that associated with the unit's minimum operating level, *and the shut-down reference price is the appropriate reference price, as*

Trading Company v. Southern Company Services, Inc., 104 FERC ¶ 61,141, at P 10 (2003); *New England Power Pool and ISO New England Inc.*, 103 FERC ¶ 61,304, at P 9 (2003); *Barton Village, Inc., et al. v. Citizens Utilities Company*, 100 FERC ¶ 61,244, at P 9 (2002). In particular, the ISO's answer clarifies many of the issues raised and misunderstandings reflected in the Coral Group's motion for clarification and request for rehearing.

[3] The five-tier pricing formula is discussed further in Section I.B, below.

described in footnote 8 to paragraph 20" of the August 17, 2004 Order. Coral Group at 7-8 (quoting July 26, 2005 Order at P 20 and adding the emphasis shown above).[4]

Contrary to the Coral Group's claims, the Commission has not undone the reference price formula in Section 7.2.6.1.1. The Commission's orders in this proceeding simply recognize that the first tier of the formula cannot apply to the calculation of decremental reference prices for the operating range from zero MW to Pmin because, under the ISO Tariff, there are no bids for the capacity between zero MW and Pmin. Thus, a tier one reference price -- which is bid-based -- cannot be calculated for capacity between zero MW and Pmin. Because the tier one formula does not apply to capacity below Pmin, Potomac Economics must calculate reference prices for such capacity based on the other tiers in Section 7.2.6.1.1, in descending order.

In any event, the Coral Group is not permitted to challenge the Commission statement that "the shut-down reference price is the appropriate reference price, as described in footnote 8 [of the August 17, 2004 Order]," because the Coral Group's challenge goes to the methodology for determining the appropriate reference price to charge a unit being shut down, which was set forth in footnote 8 of the August 17, 2004 Order. The Coral Group declined to seek rehearing (or even clarification) of *any* of the directives in the August 17,

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[4] Footnote 8 of the August 17, 2004 Order states:

> [A] unit with a minimum operating level of 150 MW that is shut down pursuant to the CAISO intra-zonal congestion management procedure will be charged the lesser of the market clearing price or the shut-down reference price in $/MWh multiplied by 150 MW and by the period of the shut-down.

2004 Order.[5] As such, Coral Group is prohibited from collaterally attacking that Order now, as it attempts to do in its present filing.[6]

Moreover, the Coral Group is wrong in asserting that the statement from the July 26, 2005 Order quoted above "occurred in the compliance phase" of this proceeding. Coral Group at 10. The Commission made the statement in response to an ISO request for clarification of the August 17, 2004 order. July 26, 2005 Order at PP 16, 20. Indeed, in paragraphs 16-20 of the July 26 Order, the Commission expressly states that it is responding to the ISO's request for clarification of the August 17, 2004 Order and, in fact, the Commission goes on to clarify what it intended in that Order. The Commission's discussion had nothing whatsoever to do with compliance or the ISO's September 16, 2004 compliance filing in this proceeding.[7] It appears that the Coral Croup is trying to mischaracterize this as a compliance filing issue because the Coral Group failed to seek rehearing of the Commission's determination in August 17, 2004 Order regarding the prices to be charged units that are shut down. That should not be countenanced by the Commission. Because the Coral Group failed to seek rehearing of the August 17, 2004 Order, the Coral Group cannot collaterally attack the Commission's decision now.

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[5] The Coral Group states that it did not protest Amendment No. 61, and provides purported reasons why it did not do so (Coral Group at 9 n.7), but the Coral Group provides no explanation why it failed to seek rehearing or clarification of the August 17, 2004 Order.

[6] *See, e.g.*, *California Independent System Operator Corporation*, 104 FERC ¶ 61,128, at P 13 (2003); *PJM Interconnection, LLC*, 109 FERC ¶ 61,094, at P 22 (2004).

[7] Indeed, the Commission's statements identified by the Coral Group occur under the heading "**a. Request for Rehearing,**" not under the heading "**Compliance Filing**," which applies to other portions of the July 26, 2005 Order.

B. The Coral Group Fails to Correctly Distinguish Between the Two Separate Categories of Decremental Reference Prices.

Not only must the Coral Group's arguments fail on procedural grounds, they fail on substantive grounds as well. Contrary to the Coral Group's assertions, the Commission has not abandoned or "unilaterally revised" the pricing formula set forth in Section 7.2.6.1.1 of the ISO Tariff.[8] In that regard, in the August 17, 2004 Order ruled that:

> [T]he pricing methodology proposed in Amendment No. 61 should be consistent with the methodology currently in place for the determination of decremental bid reference prices. ISO Tariff section 7.2.6.1.1 sets forth a multi-tiered approach that the independent entity utilizes in the determination of decremental bid reference levels for use in managing intra-zonal congestion. . . . We find that the instant filing represents enhancements to this methodology, and, as such, the ultimate price that an entity will face should follow this established methodology.
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> Therefore, we direct the independent entity calculating decremental reference prices to utilize the current methodology when determining the shut-down reference price for a particular generating unit.

August 17, 2004 Order at PP 12-13. The Commission did not undo that determination in its July 26, 2005 Order. Accordingly, the provisions of Section 7.2.6.1 and the pricing formula in Section 7.2.6.1.1 apply both to DRPs between zero MW and a generating unit's minimum operating level ("Pmin") and to DRPs between Pmin and a generating unit's maximum operating level ("Pmax"), in the manner explained below.

The Coral Group's baseless claim that the Commission has veered from its prior decision in the August 17, 2004 Order appears to be grounded in the

[8] Section 7.2.6.1.1 contains a five-tier pricing formula for determining DRPs "for use in managing Intra-Zonal Congestion as set forth above in Section 7.2.6.1 [of the ISO Tariff]."

Coral Group's failure to recognize the following two things: (1) the fact that the Commission has approved the calculation of two separate categories of decremental reference prices ("DRPs")[9] -- a DRP that applies to a generating unit's capacity between zero MW and Pmin[10] and a separate DRP that applies to a generating unit's capacity between Pmin and Pmax;[11] and (2) the fact that the tier one reference price methodology does not -- and cannot -- apply to capacity between zero MW and Pmin because it is a bid-based methodology, and there are no bids between zero MW and Pmin under the ISO Tariff.

The Coral Group is under the mistaken impression that it can submit valid DEC bids for Energy below Pmin (and that such bids can serve as the basis for calculating the DRP between zero MW and Pmin pursuant to the tier one methodology set forth in Section 7.2.6.1.1 of the ISO Tariff).[12] The Coral Group cannot do that under the ISO Tariff! As discussed in greater detail below, any decremental ("DEC") "bids" between zero MW and Pmin that the Coral Group

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[9] In both the instant proceeding and the proceeding on Amendment No. 50 to the ISO Tariff ("Amendment No. 50"), the Coral Group has failed to properly distinguish between the two different categories of decremental reference prices and the different treatment of each of the two categories of DRPs. *See, e.g.*, Motion to Intervene, Protest in Part, and Request for Refunds of the Coral Group, Docket No. ER04-938-000 (filed July 9, 2004); Protest of the Coral Group to Refund Report and Request for Clarification, Docket No. ER03-683-009 (June 8, 2005).

[10] The Commission and the ISO have also referred to this DRP as the shut-down reference price or SDRP). A unit's SDRP is also sometimes known as its "shut-down reference level."

[11] DRPs between Pmin and Pmax were approved by the Commission in the Amendment 50 proceeding. *See* Refund Report of the ISO, Docket No. ER03-683-009, at 1-4 (May 18, 2005) (containing background information on Amendment No. 50). In contrast, DRPs between zero MW and Pmin were approved by the Commission in the instant Amendment No. 61 proceeding. *See California Independent System Operator Corporation*, 108 FERC ¶ 61,193, at PP 5, 10-13 (2004).

[12] To that end, the Coral Group states that it has submitted "bids for dec's below Pmin." Coral Group at 12-13.

submitted are not valid for purposes of Dispatch by the ISO and cannot be used by Potomac Economics to determine the appropriate DRP between zero MW and Pmin (*i.e.*, the shut-down reference price) because they are not valid “accepted decremental bids.” Indeed, as the Coral Group itself admits, any such “bids” are really offers to “be completely shut down” (Coral Group at 1 n.2).

Section 7.2.6.1 of the ISO Tariff states in relevant part that the ISO will “apply the decremental reference prices determined by” Potomac Economics (“Potomac”) (the independent entity that determines DRPs for the ISO) and that the ISO “shall Dispatch Generating Units according to the decremental reference prices thus established . . . .” Further, Section 7.2.6.1 states that “[w]here the ISO must reduce a Generating Unit’s output, the ISO shall Dispatch Generating Units according to the decremental reference prices . . . No Generating Unit shall be Dispatched below its minimum operating level or above its maximum operating level.” Thus, the ISO Tariff forbids the ISO from dispatching a generating unit below Pmin based on the DRPs that Potomac determines.[13] That is why, in Amendment No. 61, the ISO sought to implement a separate DRP – the shut-down reference price (“SDRP”) – applicable to the operating range between zero MW and Pmin. The ISO would charge that separate SDRP when it shuts down a unit.

In response to the ISO’s filing of Amendment No. 61, the Commission approved new tariff language in Section 7.2.6.1 which provides that generating

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[13] As the Commission has stated, “[a] unit’s minimum operating level is the lower limit of the respective unit’s dispatchable range.” August 17, 2004 Order at P 5 n.5. Indeed, the Coral Group itself notes that “[r]unning below Pmin is not operationally feasible. Instead, a unit must be completely shut down.” Coral Group at 1 n.2.

units "shut off due to Congestion as set forth in this Section 7.2.6.1 shall be charged the lesser of the decremental reference price for the operating range between zero MW output and the unit's minimum operating level or the relevant Market Clearing Price." It is this language that the Commission was apparently referring to in footnote 8 of the August 17, 2004 Order when it stated that the unit in question would be charged "the lesser of the market clearing price or the shut-down reference price . . ."

The Coral Group alleges that the Commission erred in ruling in its August 17, 2004 Order (as affirmed in the July 26, 2005 Order) that the SDRP is a cost-based price because the first tier of the DEC reference price methodology as set forth in Section 7.2.6.1.1(a)(1) contemplates a bid-based reference price. Coral Group at 12-13. Potomac correctly does not apply the tier one methodology to determine SDRPs because the tier one methodology utilizes "accepted decremental bids" over the previous 90 days for purposes of calculating the DRP. As discussed above, there are no accepted bids available for the capacity between zero MW and Pmin because, under Section 7.2.6.1, the ISO is not permitted to Dispatch a unit below Pmin. Thus, the first tier of the DEC reference price methodology necessarily can only apply to a generating units market based bids above Pmin; it cannot apply to a unit's capacity between zero MW and Pmin (*i.e.*, SDRPs) because the tier one methodology only applies to bid-based reference levels, and there are no bid-based reference levels for capacity below Pmin.[14]

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[14] It would be nonsensical to utilize bids associated with capacity between Pmin and Pmax to calculate the reference prices for capacity below Pmin.

Under Section 7.2.6.1.1, if this first tier of the pricing formula does not apply (for example, with regard to SDRPs), then the second tier (contained in Section 7.2.6.1.1(a)(2) of the ISO Tariff) may be applicable. The second tier "allows for a consultative approach to the development of decremental bid reference levels."[15] If the second tier does not apply, then the third, fourth, or fifth tier (contains in Sections 7.2.6.1.1(a)(3), -(4), and -(5), respectively) may be applicable; each of those tiers provide for determining cost-based prices rather than market-based prices.[16] It is those latter tiers that may apply to SDRPs, because, as explained above, SDRPs are cost-based rather than bid-based.[17]

The Commission's statements in footnote 8 of the August 17, 2004 Order and paragraph 20 of the July 26, 2005 Order indicate that the Commission understands how Section 7.2.6.1 and Section 7.2.6.1.1 operate with regard to SDRPs.[18] Thus, the Coral Group is wrong in its assertion that "the Commission envisions the SDRP to be a cost-based price that differs from the five-tier pricing system," which is the basis for the Coral Group's present filing. Coral Group at 8.

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[15] *California Independent System Operator Corporation*, 107 FERC ¶ 61,042, at P 60 (2004).

[16] *Id.*

[17] The five-tier pricing formula for determining DRPs is paralleled by a five-tier pricing formula for determining AMP reference prices for energy bids, as described in Section 3.1.1.1(a) of Appendix A to the Market Monitoring and Information Protocol. That section recognizes that energy bids occur between Pmin and Pmax, just as Section 7.2.6.1 recognizes that decremental Dispatch occurs only between Pmin and Pmax and not below Pmin. Thus, Section 7.2.6.1, read in conjunction with MMIP, Appendix A Section 3.1.1.1, shows that there are no bids for capacity below Pmin that can be used for purposes of determining a bid-based reference price under the tier one methodology.

[18] The ISO notes that on August 25, 2005, it submitted in the captioned docket a motion for clarification of July 26, 2005 Order concerning the appropriate DRP to charge a generating unit that has been shut down and cannot restart in time to meet its Day-Ahead schedule for the next day due to legitimate operational limitations.

II. CONCLUSION

For the reasons explained above, the Commission should reject the Coral Group's pleading, or, in the alternative, refuse to grant the relief requested therein.

Respectfully submitted,

/s/ Anthony J. Ivancovich

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Counsel for the California Independent System Operator Corporation

Dated: September 8, 2005

CALIFORNIA ISO

California Independent
System Operator

September 8, 2005

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 Nos. ER04-938-002

Dear Secretary Salas:

Enclosed please find an electronic filing of an Answer of The California Independent System Operator Corporation to Request for Rehearing and Clarification of the July 26, 2005 Order and a Motion for Leave to file Answer

Thank you for your attention to this filing.

Respectfully submitted,

/s/ Anthony J. Ivancovich
Anthony J. Ivancovich

Counsel for the California Independent
System Operator Corporation

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list for the captioned proceeding, in accordance with Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Folsom, California, on this 8th day of September, 2005.

/s/ Anthony J. Ivancovich
Anthony J. Ivancovich