Comments of Calpine Corporation on

California ISO
IFM Supply Pool Alternatives Discussion
Of August 14, 2009

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Calpine appreciates the opportunity to comment on the discussion regarding alternatives to the current practice of limiting the IFM supply pool to resources that are selected in the LMPM runs to meet the CAISO forecast of demand.

First, Calpine is not convinced that there is a well-defined problem to which alternative solutions can be evaluated. The CAISO straw proposal identifies 2 IFM hours in which prices rose to near the bid cap. These two hours represent less than 0.07 percent (seven one-hundredths of one percent) of the more than 3000 hours of IFM prices that have been printed since Go-Live.

The level of prices that were printed in these two hours appears directly related to the actions of market participants, not necessarily to a market flaw that needs to be fixed. First, the bid-in demand was significantly (7 percent) higher than the CAISO demand forecast. Second, apparently, the bid-in demand was not at all price responsive (otherwise, it would have been curtailed in the IFM at the bid price.) Both of these contributing factors appear to be completely in the discretion of, and under the control of market participants.

Additionally, it appears that the outcomes of the market in this particular instance are idiosyncratic and not systematic. It was reported on the call that at least in one other instance where bid-in demand was similarly higher than the CAISO forecast, no pricing anomalies were noted.

Therefore, Calpine is not convinced that any action is warranted.

Nonetheless, if the CAISO concludes that some modifications are needed, Calpine offers the following guiding principles:

- The CAISO should not protect market participants from their own bids
- The CAISO should take no steps that further encourage, or facilitate self-scheduling, and rather should facilitate bidding.
- The CAISO should move toward the FERC-mandated structure as soon as practicable.

Turning to the Alternatives presented in the Straw Proposal, these principles lead us to conclude that either Alternative 1 or Alternative 4 are superior to the alternatives.

Alternative 1 appears to be the most-transparent and least intrusive option to expanding the pool of resources. Our support to Option 1 however is heavily conditioned. In particular, before making this change—or selecting any other alternative -- Calpine would request that the CAISO clearly state the problem for which they seek a solution and identify the frequency of occurrence (presuming it is more than just the 2 hours identified). The problem should be stated in terms of software or modeling shortcomings, and not a subjective view of resulting prices. Second, the CAISO should demonstrate that demand bidding could not have avoided the perceived problem.

Alternative 4 is the most consistent with FERC orders. However, Calpine shares the concerns of DMM that using demand bids in the LMPM may result in unintended consequences and incentives. Convergence bidding will be a near-perfect complement to the imposition of alternative 4 and as such, we agree with the Straw proposal's view that they be implemented concurrently.

In Calpine's view, alternatives 2 and 3, including SCE's modification to Alternative 3, appear to fail any objective test against Calpine's principles. Most importantly, they appear to protect market participants from the effects of their own bid strategy and support self-scheduling.

Alternatives 2 and 3 do not encourage demand bidding, and SCE's modification, offers an administrative intervention with no apparent purpose other than to lower prices when bids do not achieve the desired outcome. Existing bid mechanisms can and should result in market price formation.

The suggestion that current forward scheduling targets (85 percent) are a barrier to demand bidding is a non-sequitur. Calpine's view is that price responsive demand bids may have entirely solved this "problem" and even in this extreme case, 93 percent of the load would have been served in the IFM. If demand bids are more than 15 percent above the CAISO forecast, there are a larger set of problems that need to be addressed.

Finally, alternatives 2 and 3 appear to add opaque curtains to the clearing of the market – further frustrating any efforts for independent entities to replicate CAISO market outcomes – a goal we hope the CAISO seeks. These curtains are drawn at the CAISO discretion.

Calpine appreciates the opportunity to submit these comments.