

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

California Independent System Operator)
Corporation)

Docket No. ER13-449-000

**MOTION FOR LEAVE TO ANSWER AND ANSWER TO PROTESTS AND
COMMENTS OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR
CORPORATION**

The California Independent System Operator Corporation (ISO)¹ files this motion for leave to answer and answer to the comments and protests submitted in this proceeding in response to the ISO's filing on November 21, 2012 of a tariff amendment to implement settlement rules to neutralize the revenue derived from intertie scheduling practices that are sometimes referred to as "circular scheduling."² The protests and comments do not provide a sufficient basis for the Commission to reject the ISO proposal. Although not raised in any comments, the ISO also raises the need to make a slight modification to the filed tariff language and will make such a change in a compliance filing if so ordered by the Commission.

¹ Capitalized terms not otherwise defined herein have the meanings set forth in Appendix A to the ISO tariff, as revised by the proposed tariff changes contained in the tariff amendment submitted in this proceeding. Except where otherwise specified, references to section numbers are references to sections of the ISO tariff as revised by the proposals in the tariff amendment. The ISO is sometimes referred to as the CAISO.

² The ISO submits this answer pursuant to Rules 212 and 213 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §§ 385.212, 385.213 (2010). The ISO requests waiver of Rule 213(a)(2), 18 C.F.R. § 385.213(a)(2), to permit it to answer the comments filed in this proceeding. Good cause for this waiver exists because the ISO's answer will provide additional information to assist the Commission in the decision-making process, and help to ensure a complete and accurate record in this case. See, e.g., *Entergy Services, Inc.*, 116 FERC ¶ 61,286, at P 6 (2006); *Midwest Independent Transmission System Operator, Inc.*, 116 FERC ¶ 61,124, at P 11 (2006); *High Island Offshore System, L.L.C.*, 113 FERC ¶ 61,202, at P 8 (2005).

I. Background

As described in the November 21 filing, circular scheduling can create serious operational difficulties for the ISO. The ISO's November 21 filing seeks to address this by creating new settlement rules that would allow the ISO to recapture revenue derived from one category of intertie scheduling practices that could be considered circular scheduling. Specifically, the November 21 filing addresses schedules awarded to a single scheduling coordinator that have an accompanying e-Tag reflecting a source and sink in the same balancing authority area. Through the proposed tariff amendments, the ISO would resettle both the direct revenue earned from such schedules and any incremental congestion revenue rights (CRR) revenue earned as a result of such schedules. Through this filing the ISO does not propose to apply the settlement rules to schedules that involve more than one scheduling coordinator. The filing also specifies several exceptions to these settlement rules.

II. Summary of Comments and Protests

A total of 14 parties intervened in the proceeding. Nine of those parties intervened without filing substantive comment on the ISO proposal,³ with five other parties filing substantive comments. Among the parties filing substantive comments, two entities – the Northern California Power Agency (NCPA) and Pacific Gas and Electric Company (PG&E) – offer unqualified support for the ISO proposal. Three other parties – Powerex Corp., Arizona Public Service Co. (APS), and the Western Power

³ Calpine, CDWR, Dynegy, Exelon, JP Morgan, Macquarie, NRG, Santa Clara, and Southern California Edison.

Trading Forum (WPTF) – offer varying levels of protest and concerns with the ISO proposal.

NCPA offers its view that the ISO “is appropriately proposing to modify its tariff to further reduce the incentives of engaging in [the] prohibited bidding practice” of circular scheduling.⁴ NCPA further states that the ISO’s proposal “will significantly reduce the up-front incentive to engage in” circular scheduling transactions.⁵ PG&E states that it “supports the CAISO’s effort to explicitly remove incentives for the practice of circular scheduling” and that it “urges the Commission to accept the CAISO’s tariff filing.”⁶

Powerex offers general support for the ISO’s proposed tariff provisions but expresses concern over how long it took the ISO to bring the filing to FERC. Powerex explains that it first contacted the ISO in early 2010 regarding the permissibility of circular scheduling in the ISO market. Powerex acknowledges that the ISO drew its attention to the definition of wheeling transactions in the ISO tariff. Powerex asserts, however, that once it understood that circular scheduling involving wheels was viewed by the ISO as inconsistent with the tariff, “Powerex was burdened by the CAISO’s clarification, and followed it, while other market participants continued to submit schedules inconsistent with the clarification provided to Powerex, which was not publicly made known to the market.” Powerex also explains its view that the ISO could have avoided this situation by configuring its systems to reject e-Tags for circular schedules. Finally, Powerex objects to what it views as a vague directive in the transmittal letter

⁴ NCPA comments at 4.

⁵ *Id.* at 5.

⁶ PG&E comments at 3.

regarding circular schedules involving multiple scheduling coordinators. It argues that this just creates another gray area in the market rules. Instead of directing scheduling coordinators to exercise due diligence to avoid multiple scheduling coordinator circular schedules, Powerex requests that the Commission require the ISO to prohibit such schedules where there was intent to engage in a circular schedule, with the ISO's Department of Market Monitoring holding the responsibility to determine whether there was such intent.

APS filed a limited protest, arguing that two aspects of the ISO's filing are too vague and could "unintentionally preclude legitimate market activities and have a chilling effect on participation in the CAISO market."⁷ APS's first point of concern deals with the admonition in the transmittal letter that if the ISO believes a single market participant "sought to circumvent the proposed settlement rules by submitting multiple e-Tags that 'chop-up' the path of what is essentially a single transaction so as to avoid application of the proposed settlement rule, then DMM would consider referring that conduct as either potentially manipulative or involving the submission of false information."⁸ APS expresses concern that what it views as legitimate market activity in which it simultaneously submits offers and bids at multiple interties could be viewed after-the-fact by the ISO as an attempt to evade the settlement rule. APS requests that the Commission require the ISO to provide a list of the types of transaction that are not meant to be covered by the proposed settlements rules and to specify what criteria the ISO will use in determining when a market participant has attempted to evade the

⁷ APS protest at 3.

⁸ ISO transmittal letter at 15.

settlement rule. APS's second concern relates to one of the exceptions to the settlement rules. Proposed section 30.5.5.2(d) excludes from the settlement rules schedules that "involve a Wheeling Through transaction that the Scheduling Coordinator can demonstrate was used to serve load located outside the transmission and Distribution System of a Participating TO."⁹ APS is concerned that the ISO proposal does not indicate what level of evidence will be required to demonstrate that the schedule was actually used to serve load. APS thus protests this proposed tariff provision on the limited basis that it lacks sufficient detail and requests that the Commission require the ISO to provide such detail.

WPTF protests three aspects of the ISO proposal. First, WPTF disagrees with the ISO proposal to apply the settlement rules irrespective of whether the import and export are split between the day-ahead and HASP. According to WPTF, this aspect of the rule removes incentives for scheduling coordinators to offer economic bids in HASP once they have been awarded a schedule in the day-ahead. Second, WPTF asserts that the ISO's proposed definition of what constitutes a circular schedule is overly broad because some schedules sourcing and sinking in the same balancing authority area are linear in the sense that the export and import are at different interties (even if those interties are in the same balancing authority area). Third, WPTF, like Powerex, finds that the statements in the transmittal letter regarding multiple scheduling coordinator transactions are problematic and create ambiguity.

⁹ Proposed section 30.5.5.2(d).

III. Answer

A. The ISO's Conduct in the Process Leading to the November 21 Filing was Appropriate

As detailed in its comments, Powerex has an extended history with the ISO on the issue of circular scheduling. Given that their concerns were a significant impetus for the creation of the stakeholder process that led to the ISO proposal, the ISO is especially gratified to see that Powerex has expressed its support for the proposed tariff language. Given that stated support, the ISO believes the Commission should not interpret Powerex's concern as a reason for rejecting the ISO proposal in this filing. Rather, Powerex clearly supports the changes the ISO proposes in this filing.

Powerex's primary complaint seems to be that it was burdened with the knowledge that the ISO viewed the use of a wheel to complete a circular schedule as inconsistent with the tariff, while other entities continued on with their circular scheduling practices. The ISO takes exception to this complaint on several grounds. First, the ISO believes its statements to Powerex were merely a reiteration of what was clearly stated in the ISO's tariff and if such statement enhanced Powerex's understanding of the ISO tariff, it should not have created any extra-burden on Powerex but rather enhanced its compliance with the ISO tariff. Furthermore, its suggestion that other parties were able to engage in circular scheduling with impunity is nonsensical in light of recent Commission activity. In the past three months, the Commission has publicly disclosed enforcement actions against two ISO market participants for circular scheduling

activity.¹⁰ Most tellingly, in both cases, the circular scheduling activity occurred during the time that Powerex alleges other parties acted with impunity.¹¹ Equally relevant is that, as reflected in both orders, both matters were brought to FERC's attention through a DMM referral. It is thus clear that the ISO has not, as Powerex suggests, ignored circular schedules.

Setting these two circular scheduling referrals (and potentially others that may have been made) aside, Powerex suggests that the ISO should have instituted a practice of rejecting e-Tags for circular schedules. As explained in the transmittal letter, this is not a practical option.¹² Most importantly, rejection of the e-Tags would impact unrelated schedules because the circular schedule may have created counter schedules that allowed other, unrelated schedules to clear. At the time Powerex first suggested this, the ISO also did not have a ready means of screening e-Tags to determine, in real time, what schedules were circular. Most importantly rejection of e-Tags is not the proposal before the Commission. The ISO has proposed the settlement rules to address circular schedules in a manner that avoids impacts on unrelated schedules. The presence of (flawed) alternatives says nothing about the justness and reasonableness of the proposal the ISO has placed before the Commission. In any case, Powerex's suggestion that there are other means to achieving the ISO's goal is irrelevant to the ISO's request for approval of the current methodology. The ISO has

¹⁰ *Gila River Power, LLC*, 141 FERC ¶ 61,136 (2012); *Deutsche Bank Energy Trading, LLC*, 140 FERC ¶ 61,178 (2012).

¹¹ Deutsche Bank's activity occurred from January 2010 through March 2010. Gila River's activity occurred from July 2009 through October 2010.

¹² Transmittal letter at 11-12.

demonstrated that the proposed settlement rules are just and reasonable and need not justify the exclusion of all other methods in so doing.¹³

Finally, Powerex's claimed concern on the issue of circular scheduling is belied by the fact that (so far as the ISO knows), Powerex never expressed its concern about this market issue to FERC through the Enforcement Hotline. If Powerex had truly been so concerned about other parties' perceived misconduct and the ISO's supposed indifference to that misconduct, the Enforcement Hotline would have provided Powerex a ready means of raising the issue to FERC's attention.

B. The Transmittal Letter was Clear about the Scope of Ongoing Monitoring of Multiple Scheduling Coordinator Circular Schedules

Both Powerex and WPTF express concern about the statements in the transmittal letter regarding multiple scheduling coordinator transactions. As WPTF correctly notes, the ISO's expectation that scheduling coordinators exercise due diligence to avoid engaging in multiple scheduling coordinator circular schedules is not included in the proposed tariff provisions.¹⁴ Further, to remove any potential remaining confusion on the part of Powerex and WPTF, such multiple scheduling coordinator transactions will not be subject to the proposed settlement rules. However, as explained in transmittal letter, the ISO does not condone such transactions.¹⁵ If there is a noticeable increase in the volume of such transactions, the ISO will consider further

¹³ See *New England Power Co.*, 52 FERC ¶ 61,090, at 61,336 (1990), *aff'd*, *Town of Norwood v. FERC*, 962 F.2d 20 (D.C. Cir. 1992) (rate design proposed need not be perfect, it merely needs to be just and reasonable), citing *Cities of Bethany, et al. v. FERC*, 727 F.2d 1131, 1136 (D.C. Cir. 1984) (utility needs to establish that its proposed rate design is reasonable, not that it is superior to all alternatives).

¹⁴ WPTF protest at 9.

¹⁵ Transmittal letter at 8.

appropriate action, including, as explained in the transmittal letter, “prospective revisions to the tariff to prohibit such arrangements.”¹⁶ With these factors in mind, the ISO does not see what additional clarity is necessary on this issue.

C. Transactions Structured to Evade the Settlement Rules will be Treated as any Other Instance of Suspected Manipulation or Provision of False Information

The ISO is sympathetic to APS’s request for additional guidance on what specific activity would be construed by DMM as “chopping up” an e-Tag. It is not, however, in a position to offer such guidance. Any time a market participant structures its market activities with the intent of evading the clear purpose and consequences of a market rule, such conduct potentially could be viewed as involving market manipulation or the submission of false information. The ISO’s comment in the transmittal letter about submitting the two legs of a circular schedule on different e-Tags was merely recognition of one way that such evasion could happen with the proposed settlement rules. Without having a complete understanding of all of the facts and circumstances, the ISO would never be able to answer the theoretical question APS poses. Additionally, APS’s question relates to a potential referral DMM might take as the ISO’s independent market monitor. As stated in the ISO tariff, the “decision to make . . . a referral is committed to the sole discretion of DMM.”¹⁷ As such, the ISO cannot speak for what action DMM will take in this regard. That any such referral would be a discretionary act by DMM, not the ISO, is also reflective of the fact that APS’s protest on

¹⁶ Transmittal letter at 15.

¹⁷ ISO tariff, Appendix P, section 11.1.1.

this point does not relate to the specific tariff provisions that are before the Commission and is thus outside the scope of the ISO's tariff filing.

D. Clarification of Evidence Necessary to Demonstrate a Wheeling Transaction Served Load

APS expresses concern that the ISO has not provided sufficient detail regarding what evidence must be submitted to prove that a wheeling transaction was used to serve load outside the transmission and distribution system of a Participating TO, and thus exempt from the proposed settlement rules. At the time of filing, the ISO viewed this as an implementation detail that did not need to be in the tariff. Nevertheless, to provide guidance to APS and other market participants, the ISO takes this opportunity to explain how it intends to implement proposed section 30.5.5.2(d). These details will be provided in the ISO business practice manuals so that participants have clear direction regarding the mechanics for implementing this exception.

Essentially, if a load serving entity anticipates that it will use a wheeling transaction to serve load outside the ISO, the ISO will require that an employee of the company with the authority to bind the company to provide a signed document attesting to the fact that the company serves load at the location that will be the ultimate sink of the wheel. The ISO will then provide the entity with a special resource ID to use for scheduling the wheel. If the e-Tag for a wheeling transaction reflects such a resource ID as the sink of the transaction, then the ISO's systems will be configured not to apply the proposed circular scheduling settlement rules.

E. Applying the Settlement Rules across Day-Ahead and HASP is a Basic Element of the ISO Proposal

Contrary to WPTF's suggestion, the ISO does not believe it would be appropriate to limit the proposed circular scheduling rules only to circumstances where both the import and export occur in the same market (either day-ahead or HASP). Allowing schedules to be split across markets would be too big of an exception to the rule and would make it too easy to avoid the settlement rules. A scheduling coordinator could simply schedule one leg of the transaction in day-ahead and the other leg in HASP to avoid the proposed settlement consequences. As explained above, there are many ways that a scheduling coordinator can structure a transaction to avoid a market rule and such conduct would be subject to potential DMM referral. Therefore, the ISO could have followed WPTF's suggestion and relied on DMM referral to address this concern. However, where there would be such an obvious way to avoid the rule, the ISO believes that as a matter of prudent market design it should structure its rules to prevent this obvious opportunity for abuse. Further, where a scheduling coordinator needs to adjust its day-ahead schedule to account for changed circumstances, it can submit a decremental bid in the HASP which should accomplish its goals without triggering the circular scheduling settlement rules.

F. Application of the Settlement Rules to Schedules Sourcing and Sinking in the Same Balancing Authority Area is an Appropriate and Reasonable Approach

The genesis of WPTF's protest regarding "linear schedules" is its view that due to the ISO's footprint, a schedule sourcing and sinking in the same balancing authority could actually alter flows of power. As is clear in the transmittal letter, the ISO

disagrees with this characterization.¹⁸ Outside of transmission on a DC line, a circular schedule would not require a balancing authority to increase or decrease generation in its balancing authority area. The fact that the two interties involved in the circular schedule may be hundreds of miles apart does not alter this reality.

WPTF also suggests that there may be legitimate business drivers for a scheduling coordinator to have a schedule that sources and sinks in the same balancing authority area. Those legitimate business needs must be balanced against the operational concerns the ISO described in the transmittal letter. Where such a schedule is submitted merely because it would minimize transmission fees, the ISO does not believe the tradeoff is appropriate. WPTF also suggests that one reason for needing to submit such schedules is when external transmission is unavailable. The ISO agrees with WPTF that in such stranded load or stranded generation situations, a scheduling coordinator should not be subject to the proposed settlement rules. Indeed, the ISO's belief in this regard is so strong that it specifically included it as one of the four exceptions in its proposed tariff language.¹⁹

IV. Correction to the Submitted Tariff Language Regarding the Application of CRR Clawback Rule to Affiliate Transactions

Although no parties raised the issue in comments or protests, after the filing was made and shortly before comments and protests were due, the ISO became aware that there was an error in filed tariff as reflected in the discrepancy between the transmittal letter and the proposed tariff language regarding application of the CRR clawback rule

¹⁸ Transmittal letter at 4.

¹⁹ Proposed section 30.5.5.2(c).

to affiliates. The transmittal letter states: “As with the convergence bidding clawback rule, the ISO will apply this CRR clawback on a scheduling coordinator basis and will not apply it to affiliates as well.”²⁰ In outlining the clawback rule, proposed tariff section 11.2.4.7 states that the CRR clawback rule will apply to a CRR Holder and parenthetically states “(or any affiliate of that CRR Holder).” These two statements are clearly inconsistent and represent an unfortunate oversight in the ISO’s filing.

The statement in the transmittal letter reflects the ISO’s policy intent. The parenthetical statement in the tariff was included inadvertently and was missed through the ISO’s tariff stakeholder process and internal review of the tariff language before it was filed. If so ordered, the ISO is prepared to submit a compliance filing that involves removing the parenthetical. With the removal of that statement, the ISO wishes to clarify that, as with convergence bidding, if a scheduling coordinator uses circular schedules to benefit the CRR position of an affiliate, such conduct would be considered for possible referral by DMM.

V. Conclusion

The ISO’s November 21 filing represents the culmination of an extensive and robust stakeholder process. The proposal provides a just and reasonable method of creating disincentives for market participants to engage in one form of circular scheduling activity that can impact ISO system operations detrimentally. The protests from APS and WPTF and the comments from Powerex offer no basis for the Commission to withhold approval of the ISO’s proposal. Aside from the minor

²⁰ Transmittal letter at 14.

correction regarding the CRR clawback rule, the ISO requests that the Commission approve the ISO proposal as filed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have served the foregoing document upon the parties listed on the official service lists in the above-referenced proceedings, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Folsom, California this 27th day of December 2012.

Susan L. Montana
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