Comments on the Straw Proposal for Modifying Rules
Limiting the Supply Bid Pool in the Integrated Forward Market
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The two hours of high prices in the IFM on July 26 reflect the combined effect of a set of sub-optimal market rules and practices:

- the rule limiting the pool of available supply bids in the IFM to those bids dispatched in the Local Market Power Mitigation (LMPM) process;
- the application of the LMPM process based on CAISO Forecast of CAISO Demand, rather than bid-in demand;[1] and
- the apparent lack of price-responsive demand in the IFM.

The CAISO has offered four options to address this perceived problem. Southern California Edison has also offered a proposed solution.

Option 4, running the LMPM based on bid-in demand, seems the best theoretical solution to this problem. Knowing that the supply pool reflects the amount of bid-in demand that clears the IFM would encourage responsible demand bidding. However, Dynegy shares the CAISO's concern that adopting this solution prior to the implementation of convergence bidding would encourage strategic load bidding. Market participants cannot properly react to strategic load bidding without convergence bidding. So while Dynegy supports Option 4, it does not want to see this option implemented prior to the implementation of convergence bidding. Dynegy urges the CAISO to spare no effort to implement convergence bidding and Option 4 at the earliest possible time.

Option 1, using all bids in the IFM, is the next best solution. Dynegy supports the implementation of this option. However, restricting the IFM supply bid pool to the amount of cleared bid-in demand, while not an optimal solution without convergence bidding, creates the right incentive for demand to bid into the IFM in a responsible way. Simply opening up the IFM supply bid pool will not discourage strategic demand bidding. This option, therefore, is not a panacea that will address all of the current problems.

Dynegy does not support either Option 2 (using all bids in the IFM if the bid-in demand exceeds the CAISO forecast of CAISO demand), or Option 3 (using the greater of the CAISO demand forecast and bid-in demand in the LMPM process). The apparent problem at hand does not warrant the implementation of either of these options, both of which would continue to encourage self-scheduling and discourage submitting price-responsive demand. These options would discourage submitting price-responsive demand by providing demand with the "optimal" set of IFM supply bids, regardless of how much inelastic demand was bid relative to the CAISO's demand forecast.

[1] As the CAISO is aware, in 2005 FERC directed the CAISO to run the LMPM process based on bid-in demand, but allowed the CAISO to run the LMPM process using the CAISO forecast of demand to prevent further delays to MRTU implementation. Running the LMPM process based on bid-in demand was one of many things left out of the initial MRTU implementation to try to speed MRTU's implementation.

Dynegy does not support SCE's proposed option, which seeks to add artificial elasticity to an apparently inelastic demand curve, but in so doing effectively implements an arbitrary clearing price cap well below the current level of the bid cap.

Dynegy appreciates the opportunity to submit these comments.