142 FERC ¶ 61,191
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Philip D. Moeller, John R. Norris,
Cheryl A. LaFleur, and Tony Clark.

California Independent System Operator Corporation Docket No. ER13-872-000

ORDER CONDITIONALLY ACCEPTING TARIFF REVISIONS

(Issued March 19, 2013)

1. On February 1, 2013, pursuant to section 205 of the Federal Power Act (FPA),[1] the California Independent System Operator Corporation (CAISO) filed proposed revisions to its open access transmission tariff (OATT) to establish the terms and conditions applicable to market participants whose market-based rate authority has been suspended by the Commission, but have nevertheless been permitted to continue participating in the CAISO market.[2] In this order, we conditionally accept CAISO's proposal subject to a compliance filing, to become effective April 1, 2013, as requested.

I. Background

2. On November 14, 2012, the Commission suspended J.P. Morgan Ventures Energy Corporation's (JP Morgan) authority to sell energy, capacity, and ancillary services at market-based rates for a period of six months.[3] Nevertheless, the Commission permitted JP Morgan to participate in wholesale electricity markets within certain parameters. Under the terms of the suspension, the Commission explained:

> JP Morgan will only be allowed to participate in wholesale electricity markets by either scheduling quantities of energy products without an

[1] 16 U.S.C. § 824d (2006).

[2] CAISO Filing at 1.

[3] *J.P. Morgan Energy Ventures Corp.*, 141 FERC ¶ 61,131 (2012) (Suspension Order), *order granting clarification*, 142 FERC ¶ 61,085 (2013) (clarifying that the suspension would apply only prospectively and would not modify or abrogate agreements entered into by JP Morgan before the suspension's effective date).

> associated price or by specifying a zero-price in [its] offer, as the relevant tariffs require. Furthermore, the rate received by JP Morgan will be capped at the higher of the applicable locational marginal price [(LMP)] or its default energy bid.[4]

The Commission, however, delayed the effectiveness of the suspension until April 1, 2013, in response to concerns raised by CAISO that the generating units controlled by JP Morgan play a significant role in enabling CAISO to address system reliability needs.[5]

II. CAISO Filing

3. CAISO proposes to add a new Appendix II to its OATT (Appendix II) to establish the terms and conditions under which entities may participate in the CAISO markets after the Commission has suspended their market-based rate authority. CAISO states that the proposed revisions are necessary to address the implementation of the Suspension Order, though its proposal would apply to any market participant whose market-based rate authority has been similarly suspended by the Commission. Specifically, CAISO explains that Appendix II would apply to any market participant that meets the following three criteria: (1) the entity's market-based rate authority has been suspended by the Commission; (2) the entity is only allowed to participate in wholesale electricity markets by scheduling quantities of energy products without an associated price or by specifying a zero-price in their offer, as the relevant tariffs require; and (3) the rate received by the entity is to be capped at the higher of the applicable LMP or the entity's default energy bid.[6]

4. CAISO's proposal provides that market participants subject to Appendix II would only be permitted to submit either self-schedules or economic bids with a price of $0/MWh.[7] After the bid validation process, but before execution of the applicable market run, CAISO proposes to replace the zero-price bids of the pertinent market participants with a generated bid based on the relevant resource's proxy costs.[8] CAISO explains that generated bids for gas-fired resources include fuel costs and variable operating and

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[4] Suspension Order, 141 FERC ¶ 61,131 at P 53.

[5] *Id.*

[6] CAISO Filing at 10-11.

[7] *Id.* at 14. CAISO proposes to reject any bid submitted by a scheduling coordinator that is neither a self-schedule nor a zero-price bid. *Id.* at 3, 14.

[8] *Id.* at 4, 14.

maintenance costs.[9] In the event that the resource clears the market, CAISO proposes that the resource would be paid the applicable LMP.[10]

5. CAISO argues that the substitution of generated bids for zero-priced bids is necessary to avert the harmful effects of dispatching resources based on their submission of zero-price bids.[11] According to CAISO, dispatching resources based on their zero-price bids would cause these resources to be dispatched out of the merit order that would result had they submitted bids that reflect their actual marginal costs.[12] CAISO contends that dispatching resources out of merit order, particularly those that would not have cleared the market under normal circumstances, could depress the market-clearing prices paid to all market participants. Further, CAISO asserts that lower clearing prices may discourage resources without contractual must-offer obligations from bidding into the market and may require CAISO to increase its reliance on exceptional dispatch procedures.[13] By dispatching resources based on their generated bid, instead of their zero-price bid, CAISO contends that the affected resources would be dispatched in merit order and that LMPs would not be depressed.

6. CAISO further asserts that its proposal to substitute market participants' zero-price bids with generated bids produces a result that is consistent with the cap established in the Suspension Order.[14] CAISO explains that a resource's generated bid will always be less than a resource's default energy bid, which is calculated in the same manner as generated bids, but includes a 10 percent adder. As a result, CAISO reasons that its

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[9] *Id.* at 12. In comparison, CAISO explains that cost-based default energy bids are calculated in the same manner as generated bids but include a 10 percent adder. *Id.* (citing OATT § 39.7.1).

[10] *See* Att. C ¶¶ 15-16 (Hildebrandt Declaration).

[11] CAISO Filing at 11-14. Further, CAISO states that this approach is similar to its existing tariff rules regarding resources with resource adequacy contracts subject to must-offer requirements and resources with capacity procurement mechanism designations that do not submit bids into the market but have not notified CAISO of a forced outage. In such cases, CAISO says its OATT directs CAISO to insert a generated bid for such capacity. *Id.* at 12.

[12] *Id.* at 11.

[13] *Id.* at 12.

[14] *Id.* at 13; Hildebrandt Declaration ¶¶ 15-17.

proposed use of the generated bid would ensure that a resource's overall rate is capped at the higher of the LMP or its default energy bid.[15]

7. According to CAISO, a number of options for calculating default energy bids are available to market participants under the CAISO tariff, including an option based on a resource's variable costs, an option based on a weighted average of locational marginal prices in the applicable node, a negotiated option, or an alternative variable cost option available to frequently mitigated units. In its filing, CAISO proposes to restrict how market participants subject to Appendix II can calculate their default energy bid for purposes of the rate cap. Specifically, CAISO proposes to limit market participants to calculating their default energy bid pursuant to the variable cost option.[16] CAISO states that if the resource of a market participant lacks a variable cost option default energy bid during the suspension period, CAISO will create a default energy bid of $0/MWh for the resource. In support of its proposal, CAISO posits that the Suspension Order "only references the cost-based option."[17]

8. Similarly, CAISO proposes in Appendix II to limit the pertinent market participant's calculation of start-up and minimum load costs to the proxy cost option, eliminating the registered cost option.[18] CAISO states that under the proxy cost option, "market participants can submit start-up and minimum load bids each operating day up to the cost-based levels reflecting fuel and variable operating costs at minimum load."[19] Thus, CAISO argues that limiting affected market participants to the proxy cost option would ensure that they recover their costs without earning excessive revenues, which CAISO suggests would be inappropriate in light of the fact that the Commission has suspended the market participant's market-based rate authority. Furthermore, CAISO argues that this limitation would be consistent with the Suspension Order in that it would prevent such market participants from affecting the "economic outcome" of the CAISO markets.[20]

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[15] CAISO Filing at 13.

[16] *Id.* at 14-15; Att. A § 3.1.

[17] CAISO Filing at 15.

[18] *Id.* at 15-17; Att. A § 4.1.

[19] CAISO Filing at 16. In comparison, CAISO explains that the registered cost option is more market-oriented and allows resources to register their costs at values that are up to 200 percent of their projected proxy costs. *Id.*

[20] *Id.* at 17.

9. With respect to multi-stage generating unit resources' transition costs, CAISO proposes in Appendix II to limit these market participants to registering a transition cost of $0/MWh.[21] CAISO claims that such a limitation is consistent with the Suspension Order.[22]

10. CAISO also proposes to restrict the conditions under which market participants subject to Appendix II may offer ancillary services, submit residual unit commitment bids, and indicate ramping rates. CAISO proposes in Appendix II that market participants with suspended market-based rate authority may either self-schedule or submit a zero-price bid ($0/MWh) for ancillary services capacity and may submit only zero-price bids for residual unit commitment availability bids. CAISO states that it will reject all other bids.[23] In addition, CAISO notes that, in theory, a market participant could submit a ramp rate of $0/MWh and avoid being dispatched by the CAISO market software. CAISO states that it believes this is a form of competitive bidding covered by the Commission's prohibition on competitive bidding by a market participant with suspended market-based rate authority. CAISO, therefore, proposes to automatically enter the maximum ramp rate in its Master File for all resources bid by a market participant governed by Appendix II in order to prevent competitive bidding and/or withholding.[24]

11. In addition, CAISO argues that the Commission should reject a related filing by JP Morgan in Docket No. ER13-830-000, which CAISO states proposes a materially different implementation of the Suspension Order that could adversely impact the CAISO market and its participants as well as CAISO's ability to continue to operate the system reliably.[25]

12. CAISO requests an effective date of April 1, 2013, so that the proposed revisions can take effect on the same date that the suspension of JP Morgan's market-based rate authority begins.[26]

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[21] Att. A at § 4.2. CAISO notes that in addition to recovering start-up and minimum load costs, multi-stage generating resources are allowed to recover the cost of transitioning from one configuration to another. CAISO Filing at 17.

[22] *Id.* at 17.

[23] *Id.* at 15, 17-18; Att. A at §§ 2.2, 5.2.

[24] CAISO Filing at 18; Att. A at § 6.1.

[25] CAISO Filing at 3, 7-10.

[26] *Id.* at 20.

III. Notice and Responsive Filings

13. Notice of CAISO's filing was published in the *Federal Register*, 78 Fed. Reg. 9685 (2013). On February 7, 2013, the Commission issued an errata notice shortening the comment date, with interventions and protests due on or before February 20, 2013.

14. A timely motion to intervene was filed by the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California. Timely motions to intervene and comments were filed by the California Department of Water Resources State Water Project (State Water Project), Pacific Gas and Electric Company (PG&E), Calpine Corporation (Calpine), Southern California Edison Company (SoCal Edison), and Northern California Power Agency (NCPA). JP Morgan filed a timely motion to intervene and protest. On February 28, 2013, CAISO filed an answer to JP Morgan's protest.

15. Calpine, PG&E, SoCal Edison, and State Water Project request that the Commission accept CAISO's proposal. Calpine, PG&E, and SoCal Edison support CAISO's proposal to replace zero-price bids submitted by market participants with suspended market-based rate authority with a generated bid based on the resource's marginal costs.[27] Calpine and SoCal Edison opine that the regular and foreseeable use of zero-price bids by JP Morgan, or any similarly situated entity, could have the effect of depressing clearing prices in the CAISO market. As a result, market participants could unreasonably become subject to the consequence of another entity's violations.[28]

16. PG&E asserts that market participants subject to Appendix II should be paid no more than their default energy bid when that price is less than the LMP.[29] Otherwise, PG&E contends that CAISO's proposal would allow these market participants to receive market-based rates in excess of their costs. PG&E states that, while superior to the JP Morgan proposal, the CAISO proposal still does not result in a full market-based rate suspension because it permits JP Morgan to receive market-based LMP prices, even if those prices exceed the generator's costs. PG&E thus requests that the Commission clarify the distinction between an entity's losing its market-based rate authority and an entity's being subjected to "tight mitigation rules" such that the entity still receives market-based rates. In the alternative, PG&E requests a technical conference discussing

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[27] Calpine Comments at 2; PG&E Comments at 3; SoCal Edison Comments at 3.

[28] *See* Calpine Comments at 3; SoCal Edison Comments at 3.

[29] PG&E clarifies that the default energy bid should only be calculated using the variable cost option, consistent with CAISO's proposal. PG&E Comments at 6.

how the suspension of an entity's market-based rate authority works in the context of organized wholesale markets.[30]

17. SoCal Edison argues that the rate that market participants with suspended market-based rate authority receive should be capped at the LMP, but states that the Commission should have the discretion to determine if these market participants should receive the default energy bid when the default energy bid is less than the LMP.[31] SoCal Edison also supports CAISO's proposal to limit market participants with suspended market-based rate authority to choosing only the proxy cost option for their start-up and minimum load costs.

18. JP Morgan contends that several aspects of CAISO's proposal contravene the directives of the Suspension Order.[32] First, JP Morgan objects to CAISO's proposal to convert its zero-price bids to generated bids based on the resource's proxy costs before each market run. JP Morgan argues that this proposal conflicts with the Commission's directive that JP Morgan submit offers for energy products without an associated price or at $0/MWh.[33] Further, JP Morgan argues that, contrary to the assertion of CAISO, replacing JP Morgan's bids with generated bids would have no effect on system reliability and, in times of high demand, have no effect on the LMP.[34]

19. Second, JP Morgan asserts that CAISO's proposal is inconsistent with the rate cap established in the Suspension Order.[35] JP Morgan explains that CAISO would only dispatch its resources when its zero-price bid, converted to the generated bid, is less than or equal to the marginal price. Because, under CAISO's proposal, JP Morgan would receive the LMP, JP Morgan argues that it would never receive the default energy bid.[36] Additionally, JP Morgan contends that CAISO's proposal would obligate JP Morgan to generate electricity without the opportunity to recover its costs of production in the event that its costs exceed the LMP.[37]

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[30] *Id.* at 6.

[31] SoCal Edison Comments at 4.

[32] JP Morgan Protest at 6-12.

[33] *Id.* at 7.

[34] *Id.* at 8.

[35] *Id.* at 8-9.

[36] *Id.* at 8.

[37] *Id.* at 9.

20. Third, JP Morgan argues that CAISO's use of the generated bid, rather than its default energy bid, to replace its zero-price bids ignores the Commission's finding in the Suspension Order that JP Morgan's default energy bid represents a reasonable opportunity to recover costs.[38] According to JP Morgan, the Commission has previously recognized that the 10 percent adder included in the default energy bid is used to reflect a supplier's incidental and operating costs.[39] Thus, JP Morgan argues that the generated bid, which does not include the 10 percent adder, does not appropriately measure marginal costs.[40]

21. Fourth, JP Morgan asserts that CAISO's proposal fails to revise the tariff provisions pursuant to which market participants are compensated when their generation resources are exceptionally dispatched.[41] Consequently, JP Morgan contends that CAISO's proposal eliminates JP Morgan's ability to recover its costs when its resources are exceptionally dispatched and CAISO mitigates the associated payment. JP Morgan claims that its energy bid, which CAISO proposes to replace with the generated bid, would be used to establish its exceptional dispatch payment if its bid is less than both the LMP and default energy bid. Because its default energy bid is by definition greater than its generated bid, JP Morgan argues that its mitigated exceptional dispatch payments would always be less than its default energy bid and, thus, not reflect its costs.[42] JP Morgan expresses concern that its resources would be exceptionally dispatched during the suspension period due to the outage of the San Onofre Nuclear Generating Station.

22. Based on its assertion that CAISO's proposal is inconsistent with the restrictions established by the Commission, JP Morgan asserts that CAISO's filing constitutes an out-of-time request for rehearing of the Suspension Order.[43] JP Morgan argues that CAISO's proposal cannot be justified on reliability or efficiency grounds and, rather, imposes additional, unauthorized penalties on JP Morgan by preventing JP Morgan from recovering the costs of energy it generates during the suspension period.

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[38] *Id.* at 9-10.

[39] *Id.* at 10 (citing *Cal. Indep. Sys. Operator Corp.*, 116 FERC ¶ 61,274 (2006)).

[40] *Id.*

[41] *Id.* at 11-12.

[42] *Id.* at 11.

[43] *Id.* at 12-13.

23. Additionally, JP Morgan contends that CAISO's proposal would impose a confiscatory rate.[44] Unlike other market participants with active market-based rate authority, JP Morgan notes that under CAISO's proposal, sellers subject to Appendix II would not have the authority to structure their bids to protect against losses. JP Morgan argues that the Suspension Order addresses this issue by entitling JP Morgan to recover at least the costs it incurs in generating electricity sold into the CAISO market by capping its rate at the higher of its default energy bid or the applicable LMP.[45] Therefore, JP Morgan requests that the Commission reject CAISO's proposal.

IV. Discussion

A. Procedural Matters

24. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2012), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

25. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2012), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We are not persuaded to accept CAISO's answer and will, therefore, reject it.

B. Substantive Matters

26. We conditionally accept CAISO's proposal, to be effective April 1, 2013, as requested, because we find that CAISO's proposal largely represents a reasonable implementation of the Suspension Order. However, as discussed below, CAISO's proposal may subject applicable market participants to a confiscatory rate and, therefore, we direct CAISO to submit a compliance filing within 15 days of the date of this order.

27. As an initial matter, CAISO's proposal does not constitute an out-of-time request for rehearing, as CAISO does not seek to alter the limitations imposed by the Commission in the Suspension Order. For example, Appendix II will require applicable market participants to submit zero-price bids, as required by the Suspension Order. Notably, however, the Suspension Order did not address the procedures by which CAISO or any market operator would dispatch affected resources.

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[44] *Id.* at 13-14 (citing *Bluefield Waterworks & Impovement Co. v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679, 690 (1923); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 114 FERC ¶ 61,070, at P 4 (2006)).

[45] *Id.* at 13.

28. CAISO's proposal to replace applicable zero-price bids with generated bids represents a reasonable implementation of the Suspension Order. We agree with CAISO, Calpine, and SoCal Edison that the use of zero-price bids could have the unintended effect of depressing the market clearing prices in the CAISO markets, thus adversely affecting other market participants. CAISO's proposed use of the generated bid for dispatching purposes accounts for this adverse effect and, thus, ensures that market-clearing prices are not unnecessarily suppressed. Furthermore, CAISO's proposal will ensure that resources are economically dispatched in merit order and that market-clearing prices accurately reflect resources' marginal costs.[46] Lastly, as discussed above, this aspect of CAISO's proposal is consistent with the requirements of the Suspension Order, which did not address any market operator's dispatch procedures. Therefore, we find that CAISO's proposed use of the generated bid reflects a just and reasonable application of the Suspension Order's directives.

29. We agree with JP Morgan, however, that CAISO's proposal may produce a confiscatory rate in the event that the LMP falls below an applicable resource's default energy bid because, in that case, the LMP would not allow the relevant market participant to recover its costs of generating electricity.[47] Under CAISO's proposal, applicable market participants would always receive the LMP, even if that rate is less than the resource's default energy bid. Where the affected resource's generated bid sets the market-clearing price, all market participants would receive a rate equal to the affected resource's generated bid; however, the generated bid does not account for all of a market participant's costs. In particular, the generated bid is comprised of a resource's fuel costs and its variable operation and maintenance costs. Notably, the generated bid does not account for a resource's fixed or incidental costs. In comparison, the Commission has previously recognized that a resource's default energy bid, which is by definition 10 percent higher than the generated bid, presents market participants with a reasonable opportunity to recover their costs.[48] Moreover, the Suspension Order specifically states that "the rate received by JP Morgan will be capped at the higher of the applicable [LMP] or its default energy bid."[49] To the extent that the CAISO proposal subjects market participants such as JP Morgan to a more restrictive rate cap than that which was imposed

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[46] Moreover, the Commission has previously found that the generated bid option provided flexibility to elect the appropriate cost representation where no obvious cost-basis exists. *Cal. Indep. Sys. Operator Corp.*, 136 FERC ¶ 61,238, at P 17 (2011).

[47] In contrast to the LMP, the default energy bid is designed to contribute to the recovery of the generator's fixed costs. *Cal. Indep. Sys. Operator Corp.*, 119 FERC ¶ 61,076, at P 501 (2007).

[48] Suspension Order, 141 FERC ¶ 61,131 at P 53.

[49] *Id.*

by the Commission, CAISO's proposal is inconsistent with the requirements of the Suspension Order. Therefore, in order to ensure that CAISO's proposal is consistent with the Suspension Order and does not impose a confiscatory rate, we direct CAISO to submit a compliance filing within 15 days of the issuance of this order revising Appendix II to provide that market participants subject to Appendix II are to be paid the higher of their default energy bid or the applicable LMP.

30. Furthermore, we agree with JP Morgan that the rate it receives for mitigated exceptional dispatches may be confiscatory under CAISO's proposal. Specifically, JP Morgan contends that CAISO will use its generated bid to establish its exceptional dispatch payments if its energy bid is less than both the LMP and default energy bid.[50] An exceptional dispatch payment based on a resource's generated bid would result in a below-cost rate because its generated bid does not include any contribution towards a resource's fixed or incidental costs. In order to avoid this confiscatory result, we clarify that CAISO is to pay market participants with suspended market-based rate authority for mitigated exceptional dispatches at the higher of the default energy bid or the LMP at all times. Thus, section 11.5.6.7.3 of CAISO's OATT should not apply to market participants with suspended market-based rate authority. To the extent necessary, we direct CAISO to revise its tariff within 15 days of the issuance of this order to provide that market participants subject to Appendix II that receive exceptional dispatches subject to mitigation are paid the higher of their default energy bid or the applicable LMP.

31. Lastly, we note that section 5.1 of CAISO's proposal conflicts with the plain language of the Suspension Order in failing to permit market participants to self-schedule ancillary services. Section 5.1 would only permit a market participant to offer either a "Submission to Self-Provide Ancillary Services, or an Ancillary Services Bid with a $0/MW price." Importantly, the CAISO OATT defines a "Submission to Self-Provide Ancillary Services" differently than it defines "self-schedule." Thus, in its compliance filing, we direct CAISO to revise this provision in a manner consistent with the Suspension Order.

32. PG&E's assertion that market participants subject to Appendix II should receive a rate no higher than the default energy bid represents a collateral attack on the Commission's holding in the Suspension Order, which capped JP Morgan's recovery at the higher of the applicable LMP or its default energy bid.[51] Consequently, we reject

[50] This contention is incorrect. CAISO's OATT states that when the bid price is less than the default energy bid, and the LMP is less than *both* the default energy bid price and the default energy bid, then the resource will receive the bid price for its exceptional dispatch. Alternatively, when the bid price is less than the default energy bid but the LMP is *higher* than the bid price, the resource will receive the LMP for its exceptional dispatch. CAISO OATT § 11.5.6.7.3.

[51] Suspension Order, 141 FERC ¶ 61,131 at P 53.

PG&E's request to convene a technical conference to discuss the significance of market-based rate suspension in the context of organized whole markets. Furthermore, we will dismiss PG&E's request that the Commission clarify the distinction between an entity's losing its market-based rate authority and an entity's being subjected to "tight mitigation rules" as an out-of-time request for clarification.

33. Finally, CAISO argues that the Commission should reject a related filing by JP Morgan in Docket No. ER13-830-000. In a concurrently-issued order, the Commission conditionally approves the relevant portions of JP Morgan's filing, subject to the requirement that JP Morgan submit a compliance filing within 15 days of the date of this order to revise its proposal to conform to the procedures determined to be just and reasonable in the instant proceeding.[52]

The Commission orders:

(A) CAISO's proposed revisions are hereby conditionally accepted, to become effective April 1, 2013, as discussed in the body of this order.

(B) CAISO is hereby directed to submit a compliance filing within 15 days of the date of this order, as discussed in the body of the order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

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[52] *J.P.Morgan Ventures Energy Corporation*, 142 FERC ¶ 61,190 (2013).