

July 2, 1999

The Honorable David P. Boergers
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

**Re: California Independent System Operator Corporation
Docket No. ER99-1971-_____**

Dear Secretary Boergers:

Enclosed for filing please find an original and fourteen copies of tariff sheets for the California Independent System Operator Corporation ("ISO") FERC Electric Tariff, Original Volumes I and III, submitted in compliance with the Commission's May 26, 1999 Order in the above-captioned docket.

On March 1, 1999, the ISO filed Amendment No. 14 to the ISO Tariff.¹ Amendment No. 14 included a series of proposed revisions to the ISO Tariff that principally constitute Phase I of the ISO's comprehensive redesign of its Ancillary Service markets, in compliance with the Commission's October 28, 1998 order in Docket Nos. ER98-2843 *et al.*² The proposed revisions were products of an extensive process through which all interested stakeholders were involved in

¹ Capitalized terms not otherwise defined herein are used in the sense given in the Master Definitions Supplement, Appendix A to the ISO Tariff.

² *AES Redondo Beach, L.L.C., et al.*, 85 FERC ¶ 61,123 (1998).

assessing the problems that had arisen in those markets during the first year of the ISO's operation and in developing proposals to address them. Amendment No. 14 also included several other proposed changes to the ISO Tariff.

Numerous parties submitted motions to intervene, comments and/or protests to Amendment No. 14. On April 12, 1999, the ISO submitted its Answer to Motions to Intervene, Request for Clarification, Comments and Protests in the above-captioned docket (the "April 12 Answer"). In the April 12 Answer, the ISO agreed, in response to various intervenor comments and questions on Amendment No. 14, to make a number of small non-substantive modifications to the ISO Tariff that would be submitted in a compliance filing.

On May 26, 1999, the Commission issued an order in the above-captioned docket and Docket Nos. ER98-2843 *et al.* which accepted Amendment No. 14 with certain modifications (the "May 26 Order").³ In the May 26 Order, the Commission directed the ISO to make certain modifications to the Amendment No. 14 Tariff revisions, including those modifications which the ISO committed to make in the April 12 Answer. The Commission directed the ISO to submit a compliance filing containing those Tariff changes within 30 days of the May 26 Order. 87 FERC at 61,823.

On June 25, 1999, the ISO filed a Motion for Extension of Time in this proceeding, requesting an additional week to finalize the compliance filing required by the May 26 Order. On June 29, 1999, the Commission granted the requested extension.

The ISO now submits revised Tariff sheets in Attachment A to this filing which incorporate the modifications ordered by the Commission. The ISO also submits blacklined Tariff provisions showing the modifications made in this compliance filing, which are discussed in further detail below:

I. Rational Buyer

In Amendment No. 14, the ISO proposed certain revisions to the ISO's Ancillary Service procurement process that will enable the ISO to purchase additional quantities of one Ancillary Service that can substitute for another Ancillary Service, in order to reduce total costs (the "Rational Buyer" process). The Commission accepted the Rational Buyer proposal in the May 26 Order, but directed the ISO to the Tariff to clarify how settlements will be made on the Rational Buyer procurement process. 87 FERC at 61,808-10.

As an initial matter, the ISO notes that the one example of an aspect of Rational Buyer that the Commission identifies as requiring clarification is

³ *AES Redondo Beach, L.L.C., et al.*, 87 FERC ¶ 61,208 (1999).

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inapplicable to the final version of Rational Buyer as proposed in Amendment No. 14. In the May 26 Order, the Commission notes:

For example, the ISO's discussion of the Rational Buyer Implementation in Attachment C describes and illustrates the procedures to be used to determine settlements. The ISO's stated objective in the discussion is to ensure that no classes of users would be made worse off as a result of the Rational Buyer procurement. However, the manner in which the ISO's rates charged for Ancillary Services would reflect these procedures is not clearly specified in Section 2.5.28 of the Tariff or in the billing and settlement protocols submitted in Attachment E.

87 FERC at 61,810. Attachment C to the Amendment No. 14 transmittal letter consisted of materials presented at a January 1999 meeting of the ISO Governing Board and were intended to provide the Commission with background on the extensive stakeholder process that resulted in the Tariff revisions proposed in Amendment No. 14. See March 1 Transmittal letter at 14. In some instances, proposals were revised at the subsequent ISO Governing Board meeting in February. Such was the case with this aspect of Rational Buyer.

As the materials in Attachment C to the Amendment No. 14 filing indicate, as of January, the ISO proposed to implement the Rational Buyer approach in a manner that would ensure that no class of users would be made "worse off" as a result of the Rational Buyer procurement than they would have been under existing procedures. Stakeholders raised concerns, shared by the ISO Market Surveillance Committee, that these elements of the Rational Buyer proposal would result in adverse efficiency impacts. These concerns centered on the possible impacts of paying Ancillary Service suppliers different prices from those assessed against users of Ancillary Services procured through the ISO's auctions, and the likelihood that this price differential would encourage inefficient self-provision by high-cost suppliers. At the February meeting of the ISO Governing Board, the advantages and disadvantages of the various alternatives for settlement under the Rational Buyer proposal were reviewed. The ISO's proposal was revised, and the final Rational Buyer procedure approved by the ISO Governing Board ensures that both suppliers and users of Ancillary Services face the same prices, but does not necessarily assure that no class of users is made worse off.

Under the Rational Buyer procedure ultimately approved by the Board and submitted as part of Amendment No. 14, the ISO will identify each Scheduling Coordinator's MW obligation as its share of the ISO's initial reliability-based requirements for Regulation, Spinning Reserve, Non-Spinning Reserve, and Replacement Reserve. The ISO will then charge for these obligations based on the prices resulting from operation of the Rational Buyer procedure. This

approach may involve either a net surplus or net deficit in Ancillary Services settlement. Such imbalances will be resolved based on each Scheduling Coordinator's share of total Ancillary Service charges.

In compliance with the May 26 Order, the ISO submits revisions to Sections 2.5.28 *et seq.* of the Tariff and Appendix C to the ISO's Settlement and Billing Protocol which clarify how the ISO will implement settlements under the Rational Buyer approach. Blacklined Tariff provisions showing revisions that clarify settlements under the Rational Buyer procedure are submitted as Attachment B to this filing.

II. Effective Price for Uninstructed Deviations

Amendment No. 14 included a number of elements designed to eliminate certain incentives for generators to act contrary to ISO dispatch instructions. Under one proposal, the amounts payable to generators that disregard a dispatch instruction would be modified to eliminate the opportunity for Scheduling Coordinators to profit by ignoring such instructions. This would be accomplished by providing for the settlement of such "uninstructed deviations" from an ISO dispatch instruction at the weighted average of the prices applicable to generators that complied with that dispatch instruction, referred to as the "effective price."

In the May 26 Order, the Commission accepted the ISO's effective price proposal. 87 FERC at 61,811. In the order, the Commission notes that Pacific Gas & Electric Company ("PG&E") had identified certain corrections to the formulae in the effective price Tariff provisions which the ISO had committed to make in a compliance filing. *Id.* The ISO had also committed to slightly revise the definition of "Effective Price" in response to PG&E's comments. The ISO now submits these corrections. Blacklined Tariff provisions showing revisions that correct certain formulae related to the effective price proposal and which clarify the definition of "Effective Price" are provided as Attachment C to this filing.⁴ Attachment C also reflects the incorporation of the effective price provisions of Settlement and Billing Protocol Appendix D, as approved by the Commission, into the currently effective version of those provisions found in Section 23.5 of the Tariff. The ISO had committed to make these changes in its April 12 Answer.⁵

⁴ The ISO notes that certain of the revisions requested by PG&E were also requested by Southern California Edison Company ("SCE").

⁵ As indicated in the ISO's March 11, 1999 Report submitted in Docket Nos. ER98-3760 *et al.*, the ISO has committed to eliminate all "temporary" sections of the ISO Tariff and to incorporate the necessary changes into the "permanent" provisions of the ISO Tariff as part of a negotiated settlement addressing hundreds of unresolved issues, which is currently being finalized.

III. Separate Pricing of Regulation Up and Down

In Amendment No. 14, the ISO submitted Tariff revisions which will establish separate pricing for upward and downward components of Regulation. The ISO had been applying the same price to both components of Regulation; the result being that the scarcer of the two products would establish the market clearing price for both products. The Amendment No. 14 Tariff revisions correct this inefficiency.

The Tariff provisions originally submitted with Amendment No. 14 implemented this change with a single set of formulae. One commenter, the Transmission Agency of Northern California, requested that the ISO state separate formulae for the upward and downward components of Regulation in the relevant portions of the ISO Tariff. The ISO agreed to make this change. April 12 Answer at 32. In the May 26 Order, the Commission noted the ISO's commitment to make this change and accepted the ISO's proposal to establish separate pricing for upward and downward components of Regulation. 87 FERC at 61,812. Blacklined Tariff provisions reflecting the addition of separate formulae for downward Regulation are submitted as Attachment D to this filing.⁶

IV. Trades of Ancillary Services Between Scheduling Coordinators

Amendment No. 14 also included certain Tariff revisions which will permit Scheduling Coordinators to engage in trades of Ancillary Services in order to provide an alternative means for Scheduling Coordinators to fulfill Ancillary Service obligations. This aspect of Amendment No. 14 was widely supported. Based on a misreading of revisions to Section 2.5.7.4.1 of the ISO Tariff, one commenter, Electric Clearinghouse, Inc., expressed concerns that the ISO's proposal improperly limited trades of Ancillary Services between Scheduling Coordinators to resources within the ISO Control Area. In its April 12 Answer, the ISO replied that no such limitation was intended and offered to revise Section 2.5.7.4.2 to eliminate any potential confusion. April 12 Answer at 23-24.

The Commission's May 26 Order accepted the Tariff revisions implementing inter-Scheduling Coordinator trades of Ancillary Services and directed the ISO to make Tariff revisions which clarify that trading with resources outside the ISO Control Area is permitted. Blacklined Tariff provisions showing such revisions are provided as Attachment E to this filing.

⁶ The ISO notes that certain formulae for Regulation are modified by the Rational Buyer settlement revisions set forth in Attachment B. These modifications are reflected for both upward and downward Regulation in Attachment D and the Tariff sheets submitted with this compliance filing.

V. Miscellaneous Tariff Revisions

As noted above, the ISO committed to make a number of other non-substantive revisions to the ISO Tariff in response to various comments and questions on Amendment No. 14. See April 12 Answer at 32-35. These Tariff revisions are submitted, in blackline form, as Attachment F to this filing.

In addition, the ISO is submitting a number of corrected Tariff Sheets as part of Attachment A. One sheet corrects the inadvertent misnumbering of Section 2.5.20.3 in the Tariff sheets submitted with Amendment No. 14. The ISO committed to make this correction in response to a comment from the Metropolitan Water District. The ISO is also submitting a number of supplemental Tariff sheets inadvertently omitted from the March 1 Amendment No. 14 filing. As the ISO explained in its April 12 Answer, these sheets do not reflect any substantive changes from amendment No. 14, but are merely additional sheets containing pre-existing Tariff provisions which were created by the insertion of new and expanded Tariff provisions in Amendment No. 14. See April 12 Answer at 35.

VI. Supporting Documents

The documents submitted in support of this compliance filing are as follows:

- Attachment A** Revised Tariff sheets;
- Attachment B** Blacklined Tariff provisions showing revisions that clarify settlements under the Rational Buyer procedure;
- Attachment C** Blacklined Tariff provisions showing revisions that correct certain formulae related to the effective price proposal and which clarify the definition of "Effective Price";
- Attachment D** Blacklined Tariff provisions showing the addition of separate formulae for downward Regulation;
- Attachment E** Blacklined Tariff provisions showing revisions that clarify that inter-Scheduling Coordinator trades of Ancillary Services are permitted for resources outside the ISO Control Area;
- Attachment F** Blacklined Tariff provisions showing a number of miscellaneous, non-substantive Tariff revisions the ISO committed to make in its April 12 Answer; and
- Attachment G** Notice of filing suitable for publication in the Federal Register

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Also enclosed is a 3½ inch diskette containing the notice of filing in WordPerfect format. In addition, an extra copy of the filing is enclosed. Please date-stamp the extra copy with the time and date of filing and return it to the messenger. Thank you for your assistance in this matter.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have served the foregoing document upon all parties on the official service list compiled by the Secretary in the above-captioned proceeding, 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 Washington, D.C. this 2nd day of July, 1999.

Sean A. Atkins