

Memorandum

To: ISO Board of Governors
From: Steve Berberich, President and Chief Executive Officer
Date: May 21, 2014
Re: **CEO Report**

This memorandum does not require Board action.

OVERALL CONDITIONS

The ISO is entering this summer with adequate resources but heightened concern about the reliability risk created by hot dry conditions and increased risk of fires. The month of May began with normal operating conditions for this time of year with loads in the 28,000-30,000 MW range and heavy system maintenance. In addition, on May 1, the ISO implemented 15-minute scheduling for both interties and internal resources with no significant disruptions.

Warmer weather started the week of May 5, which pushed peak load up to 40,000 MW for the first time this year. Conditions worsened over the course of the next week as several fires spread across the San Diego area and created significant operating challenges. Thanks to the public's response to San Diego Gas and Electric's conservation messages and the close collaboration between our operators and SDG&E, we did not lose load on the transmission system. SDG&E should be commended for their operations, public outreach and collaboration with us to help maintain system reliability.

SUMMER LOADS AND RESOURCES ASSESSMENT

Earlier this month, the ISO released its annual summer assessment highlighting expected and possible extreme operating conditions for the coming summer. In this year's report, we highlighted the impact of the drought and the continued focus on Southern California given the San Onofre retirement.

In general, we expect limited risk of load shedding incidents because of continued moderate load outlooks due to residual effects of the recession and California's energy efficiency programs. Overall for the ISO, we project a 23.8% operating reserve margin, falling to 13.6% under extreme conditions. In the southern zone (south of Path 26) under normal operating conditions, we project 28.2% operating reserves and 15.1% under extreme conditions, while in the North (north of path 26) under normal conditions, we expect 22.7% and 7.6% respectively. Note that Northern California conditions are tighter because of drought driven hydro de-rates.

Two other risks remain for the upcoming summer: direct water curtailments to power plants and fires. While we do not expect power plant water curtailments, the possibility exists if the extreme conditions persist. Extreme fire conditions are expected and, as noted above, are already having significant impact on operating conditions.

Finally, it should be noted that operating reserve margins will remain important but will become increasingly overshadowed by system flexibility attributes as the key measure of reliability. We plan to highlight those margins as well in next year's assessment.

EIM TRANSITIONAL COMMITTEE

The energy imbalance market (EIM) presents a critical strategic opportunity to harness resources across the West more efficiently for the benefit of customers and the environment. Having good, independent governance over those markets is critical to their credibility and success and the formation of an EIM Transitional Committee is an important step toward creating that governance model. We are deeply appreciative of all of those who are willing to serve and those who ultimately are named to the committee.

FERC ORDER 764 IMPLEMENTATION

On May 1, the ISO implemented FERC Order 764 requiring the ISO to provide the option to schedule power transfers at 15-minute intervals as opposed to the current hourly approach. As I noted in my CEO Board report a year ago, "The intent is to facilitate the integration of variable energy resources on the grid. The ISO supports the order and believes it will allow us to enhance renewable integration with less operational impact. In addition, the proposed changes also address some fundamental market design challenges that have existed since the new market went live in 2009 – namely a mismatch between the settlement of the interties and the real time market."

Because of the fundamental changes to our market, implementation of Order 764 impacted many of our systems and interfaces. In fact, the system changes are the largest since the implementation of the market redesign in 2009. Overall, the implementation went quite smoothly with relatively few issues. I am extremely proud of the enormous work nearly every corner of the ISO put into making FERC Order 764 so successful. Importantly, I would like to thank and commend our market participants who also made this successful. They too put in an enormous amount of work over a short period of time and made our go-live effort successful.

INTERCONNECTION PROCESS ENHANCEMENTS

The ISO has been committed to improving the interconnection process to make it smoother, better understood and more responsive to stakeholder needs. The proposal before the Board today continues that effort and focuses on improvements to the independent study and fast track processes. In particular, the proposal revises the capacity allocation procedures, behind the meter connection processes, and incorporates FERC order 792 requirements associated with small generator interconnections.

MARKET MONITORING ANNUAL REPORT

In April, the ISO issued its 2013 Market Issues and Performance Report, produced by the Department of Market Monitoring. The report highlights overall market performance, competitiveness, and market costs. Of particular note, wholesale prices remain competitive, averaging very close to estimates of a very competitive benchmark. DMM also noted that real-time prices were systematically lower than day ahead prices – a reversal from previous years. That change is attributable to a decrease in brief but high real-time prices caused by limitations in ramping energy. Ancillary service costs were about 31% less than in 2012 and exceptional dispatches declined and remained relatively low - .26% of total energy compared to .53% in 2012.

Renewable energy continued to grow on the system in 2013 with an increase in peak hour generating capacity of about 2,000 MW, mostly from solar additions. A net of about 600 MW of conventional generation was also added to the system in 2013.

RENEWABLE INTEGRATION

New solar and wind peaks continue to be established as new resources are connected to the grid. The latest solar peak of 4,501 MW was set at 11:48 a.m. on May 2. The wind generation peak of 4,768 MW was set on April 12 at 5:48 p.m.