

Joint Comments of J.P. Morgan and Shell Energy North America (US), L.P. on CAISO Draft Final Proposal on E-Tag Timing Requirements

Submitted by	Company	Date Submitted
<i>Steve Greenleaf (916) 802-5420</i>	<i>J.P. Morgan</i>	<i>January 21, 2010</i>
<i>Mike Evans (858) 526-2103</i>	<i>Shell Energy North America (US), L.P.</i>	

J.P. Morgan Ventures Energy Corporation and BE CA, LLC (together, “J.P. Morgan”) and Shell Energy North America (US), L.P., (collectively, “Joint Parties”) appreciate this opportunity to provide comments on the California ISO’s (CAISO’s) January 7, 2010, Draft Final Proposal on E-Tag Timing Requirements (“Draft Final Proposal”) and the January 14, 2010, stakeholder conference call on the same matter.

Joint Parties support the CAISO’s proposal to not change the existing e-tagging timing requirements. However, Joint Parties do not support the CAISO’s proposal to, as stated by the CAISO, apply a new HASP Reversal Settlement Rule that removes price arbitrage gains for reversed MW with no supporting e-tag and the Convergence Bidding related CRR Settlement Rule to day ahead awards which are reversed in the Hour Ahead Scheduling Process (HASP). The CAISO has not supported the need to impose these new rules. In addition, Joint Parties are concerned that the CAISO’s proposal will reduce participation in the CAISO’s day-ahead market and may result in market participants adding a risk premium to their intertie bids; a result that would be contrary to the CAISO’s objective, as stated on the stakeholder conference call, to not introduce elements into its market rules that would result in higher costs to ratepayers.

While Joint Parties agree that entities that fail to deliver on day-ahead and HASP market awards in real time should be penalized, Joint Parties do not agree that participants that fail to fully tag day-ahead awards should be subject to the proposed HASP Reversal Settlement Rule when those HASP awards are based on CAISO dispatch instructions. To do so would inappropriately and unnecessarily penalize those participants that fully intend to deliver on their day-ahead market awards but respond to CAISO real-time market price signals, follow CAISO revised schedule instructions, and adjust their day-ahead schedules in HASP. The CAISO proposal may reduce the participation of entities that may not own or control physical resources outside of California but that actively work to bring available supplies into California and that are responsive to CAISO price signals, i.e., real-time market and operating needs. As recognized by the CAISO, existing and proposed market and uplift charges will act to discourage implicit virtual bidding. That fact, combined with vigilant and appropriate monitoring to identify those entities that

consistently and systematically liquidate their day-ahead awards in the HASP and/or fail to deliver on their forward-market awards in real time, will be sufficient to deter implicit virtual bidding.

Joint Parties support the CAISO's proposal to not change the existing e-tagging timing requirements

Joint Parties support the CAISO's proposal to not change the existing e-tagging timing requirements for physical day-ahead import awards. As stated in Joint Parties' previously submitted comments on this issue, neither the CAISO nor other market participants have identified a clear problem with the existing requirement that, consistent with the WECC requirement, permits participants to finalize e-tags up until 20 minutes before the operating hour. Joint Parties concur with the CAISO's assessment that establishing a new e-tagging timing requirement would not definitively address expressed concerns about implicit virtual bidding at the interties. Joint Parties also agree with the CAISO that modifying the existing e-tagging requirements may reduce liquidity in the market, increase ratepayer costs and would require greater discussion/coordination among other Balancing Authority Areas (BAAs) and the WECC.

Joint Parties generally support the CAISO's proposal to align financial incentives to discourage implicit virtual bidding

In concept, Joint Parties agree with the CAISO that it is important to, "...to ensure that incentives, penalties and costs provide the appropriate economic signals to discourage implicit virtual bidding on the interties once the ISO implements convergence bidding in 2011." (Draft Final Proposal at p.5). Joint Parties also agree with the CAISO that the CAISO existing uplift and market charges, as well as those proposed under Convergence Bidding, will discourage parties from disguising Convergence Bids as physical bids and thus engaging in implicit virtual bidding. Joint parties contend that it is premature to conclude that these incentives will be insufficient to deter implicit virtual bidding. Joint Parties recommend that, once Convergence bidding is implemented, the CAISO continue to closely monitor bidding activity at the ties and, should it identify anomalous behavior, then consider imposition of the charges/rules it has proposed or other appropriate measures.

While application of the HASP Reversal Settlement Rule to those entities that fail to fully tag their day-ahead market awards and schedules may create incentives to address certain instances of implicit virtual bidding, i.e., those circumstances where participants fail to deliver on day-ahead awards in real time, it would unnecessarily penalize those participants that adjust their day-ahead awards in response to CAISO requests. To be clear, Joint Parties support application of the HASP Intertie Schedules Decline Charges to those that fail to deliver on their day-ahead and HASP awards in real-time. However, Joint Parties do not support application of the CAISO's proposed charges to all changes to day-ahead awards, as this would unnecessary punish those entities that fully intend to deliver on day-ahead market awards but legitimately modify their day-ahead schedules in HASP in response to CAISO market signals or operating requests.

The CAISO has failed to demonstrate that the existing rules, or those proposed under Convergence Bidding, result in any adverse impact on reliability or the market

Since its inception, this process has been an issue in search of a problem. The CAISO and other market participants have failed to demonstrate that the CAISO's existing rules, or those proposed

under Convergence Bidding, will give rise to either reliability problems or have an adverse impact on the market. While Joint Parties acknowledge that the CAISO is not proposing to implement its proposal until the start of Convergence Bidding – and Joint Parties agree that any adopted changes should be implemented no earlier than February 2011 – the fact is that it is premature to adopt any rule change until the CAISO and market participants have gained experience and data from the market after Convergence Bidding is implemented.

Based on the fact that, as stated by the CAISO, 95% of participants already submit e-tags consistent with the WECC pre-scheduling timeframe, i.e., the day before actual delivery, it is not at all established that there is an issue that needs to be addressed. It is clear from the CAISO's own data that implicit virtual bids, to the extent they exist, are *not* crowding out physical bids and supplies and thus creating reliability issues for the CAISO. Moreover, the CAISO has not demonstrated that the existing rules for e-tagging day-ahead market awards or permitting, without penalty, schedule adjustments in HASP, are adversely impacting market results. In fact, market participants have at times responsibly adjusted their day-ahead schedules in response to CAISO real-time market price signals and operating needs; needs that are the result of a number of factors and system conditions that have resulted in at times large price discrepancies between day-ahead, HASP, and real-time prices.¹

Conclusion

Joint Parties appreciate the opportunity to submit these comments on the CAISO's Draft Final Proposal. Joint Parties do not support the CAISO's Draft Final Proposal. Alternatively, Joint Parties recommend that, once Convergence Bidding is implemented, the CAISO continue to monitor overall market results and individual market participant behavior and, to the extent anomalous behavior is identified, propose appropriate rules to align market participant behavior with financial incentives in the market.

¹ See CAISO papers on Real-Time Energy Imbalance Offset issue posted at <http://www.caiso.com/2406/2406e2a640420.html>