

129 FERC ¶ 61,157  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Sudeen G. Kelly, Marc Spitzer,  
and Philip D. Moeller.

California Independent System  
Operator Corporation

Docket Nos. ER09-1048-000  
ER06-615-018  
ER06-615-037

ORDER ON COMPLIANCE FILING

(Issued November 19, 2009)

1. On April 28, 2009, the California Independent System Operator Corporation (CAISO) submitted a compliance filing, pursuant to Order No. 719,<sup>1</sup> that proposes revisions to its Market Redesign and Technology Upgrade Tariff (MRTU Tariff). CAISO requests that its proposed tariff revisions be made effective as of April 28, 2009. In this order, we accept CAISO's compliance filing, including the revised tariff sheets as modified and subject to a further compliance filing, to be effective April 28, 2009, as discussed below.

**I. Background**

2. In Order No. 719 and Order No. 719-A, the Commission established reforms to improve the operation of organized wholesale electric power markets<sup>2</sup> and amended its

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<sup>1</sup> *Wholesale Competition in Regions with Organized Electric Markets*, Order No. 719, 73 Fed. Reg. 64100 (Oct. 28, 2008), FERC Stats. & Regs. ¶ 31,281 (2008) (Order No. 719 or Final Rule), *order on reh'g*, Order No. 719-A, 74 Fed. Reg. 37,776 (July 29, 2009), 128 FERC ¶ 61,059 (2009).

<sup>2</sup> Organized market regions are areas of the country in which a regional transmission organization (RTO) or independent system operator (ISO) operates day-ahead and/or real-time energy markets. The following Commission-approved RTOs and ISOs have organized markets: PJM Interconnection, L.L.C. (PJM); New York Independent System Operator, Inc. (NYISO); Midwest Independent Transmission System Operator, Inc. (Midwest ISO); ISO New England, Inc. (ISO New England); California Independent System Operator Corp. (CAISO); and Southwest Power Pool, Inc. (SPP).

regulations under the Federal Power Act (FPA) in the areas of: (1) demand response, including pricing during periods of operating reserve shortage; (2) long-term power contracting; (3) market-monitoring policies; and (4) the responsiveness of RTOs and ISOs to their customers and other stakeholders. The Commission stated that these reforms are intended to improve wholesale competition to protect consumers in several ways: by providing more supply options, encouraging new entry and innovation, spurring deployment of new technologies, removing barriers to demand response, improving operating performance, exerting downward pressure on costs, and shifting risk away from consumers.<sup>3</sup>

3. In the area of demand response, Order No. 719 required each RTO and ISO to: (1) accept bids from demand response resources in the RTO's or ISO's markets for certain ancillary services, on a basis comparable to other resources; (2) eliminate, during a system emergency, a charge to a buyer that takes less electric energy in the real-time market than it purchased in the day-ahead market; (3) in certain circumstances, permit an aggregator of retail customers (ARC) to bid demand response on behalf of retail customers directly into the organized energy market; and (4) modify their market rules, as necessary, to allow the market-clearing price, during periods of operating reserve shortage, to reach a level that rebalances supply and demand so as to maintain reliability while providing sufficient provisions for mitigating market power.<sup>4</sup>

4. Additionally, the Commission recognized that further reforms may be necessary to eliminate barriers to demand response in the future. To that end, the Commission required each RTO or ISO to assess and report on any remaining barriers to comparable treatment of demand response resources that are within the Commission's jurisdiction. The Commission further required each RTO's or ISO's Independent Market Monitor to submit a report describing its views on its RTO's or ISO's assessment to the Commission.<sup>5</sup>

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<sup>3</sup> Order No. 719 at P 1. Subsequent to the filing of CAISO's compliance filing, the Commission issued an order on rehearing of Order No. 719. *Wholesale Competition in Regions with Organized Electric Markets*, Order No. 719-A, 74 Fed. Reg. 37776 (July 29, 2009), 128 FERC ¶ 61,059 (2009) (Order No. 719-A). CAISO is required to file a compliance filing addressing the requirements of Order No. 719-A on or before January 26, 2010. Accordingly, the Commission will not address compliance with Order No. 719-A in this order.

<sup>4</sup> *Id.* P 4, 15.

<sup>5</sup> *Id.* P 274.

5. With regard to long-term power contracting, Order No. 719 required each RTO and ISO to dedicate a portion of its website for market participants to post offers to buy or sell power on a long-term basis.<sup>6</sup>

6. To improve market monitoring, the Commission required each RTO and ISO to provide its Market Monitoring Unit (MMU) with access to market data, resources and personnel sufficient to carry out its duties. The Commission further required that the MMU (or the external MMU in a hybrid structure and, in some cases, the internal MMU) report directly to the RTO or ISO board of directors.<sup>7</sup> In addition, the Commission required that the MMU's functions include the core functions of: (1) identifying ineffective market rules and recommending proposed rules and tariff changes; (2) reviewing and reporting on the performance of the wholesale markets to the RTO or ISO, the Commission, and other interested entities; and (3) notifying appropriate Commission staff of instances in which a market participant's behavior may require investigation.

7. The Commission also took the following actions with regard to MMUs: (1) expanded the list of recipients of MMU recommendations regarding rule and tariff changes, and broadened the scope of behavior to be reported to the Commission; (2) modified MMU participation in tariff administration and market mitigation, required each RTO and ISO to include ethics standards for MMU employees in its tariff, and required each RTO and ISO to consolidate all its MMU provisions in one section of its tariff; and (3) expanded the dissemination of MMU market information to a broader constituency, with reports made on a more frequent basis than in the past, and reduced the time periods before energy market bid and offer data are released to the public.

8. Finally, Order No. 719 established an obligation for each RTO and ISO to establish a means for customers and other stakeholders to have a form of direct access to the RTO or ISO board of directors and thereby to increase its responsiveness to customers and other stakeholders. The Commission stated that it will assess each RTO's or ISO's compliance filing using four responsiveness criteria: (1) inclusiveness; (2) fairness in balancing diverse interests; (3) representation of minority positions; and (4) ongoing responsiveness.

9. The Commission required the RTOs and ISOs to make compliance proposals to implement the reforms adopted in Order No. 719. In each of the four areas described above, the Commission required each RTO or ISO to consult with its stakeholders and

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<sup>6</sup> *Id.* P 301.

<sup>7</sup> The use of the phrase "board of directors" herein also includes the board of managers, board of governors, and similar entities.

make a compliance filing within six months of the date that the Final Rule is published in the *Federal Register*. The compliance filing must explain how the RTO's or ISO's existing practices comply with the Final Rule's reforms, or describe the entity's plans to attain compliance.<sup>8</sup> Order No. 719 also required RTOs and ISOs to assess the technical feasibility and value to the market of smaller demand response resources providing ancillary services and report to the Commission within one year of the date that the Final Rule is published in the *Federal Register*.<sup>9</sup>

## **II. Notice of Filing and Responsive Pleadings**

10. Notice of CAISO's filing was published in the *Federal Register*, 74 Fed. Reg. 21795 (2009), with interventions and protests due on or before May 26, 2009. Interventions were filed by Exelon Corporation, Constellation Energy Commodities Group, Inc. and Constellation NewEnergy, Inc., Western Power Trading Forum (WPTF), Electric Power Supply Association, City of Santa Clara, California, Mirant Energy Trading, LLC, Mirant Delta, LLC and Mirant Potrero, LLC, Powerex Corp., Calpine Corporation, NRG Companies, Comverge, Inc., the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (collectively, Six Cities), and the Northern California Power Agency.

11. Interventions and comments were filed by Southern California Edison Company (SoCal Edison), RRI Energy, Inc. (RRI), Modesto Irrigation District (Modesto), Electricity Consumers Resource Council (ELCON), Metropolitan Water District of Southern California (Metropolitan), Wal-Mart Stores Inc. (Wal-Mart), Transmission Agency of Northern California (TANC), Pacific Gas and Electric Company (PG&E), California Department of Water Resources State Water Project (SWP), California Public Utilities Commission (CPUC), the Portland Cement Association and ArcelorMittal USA, Inc. (Industrial Consumers), and EnerNOC, Inc., Energy Connect, Inc., BluePoint Energy, LLC, CPower, Inc., the Energy Users Forum, the Alliance for Retail Energy Markets, and California Manufacturers and Technology Association (Joint Parties). The CAISO, WPTF, and Six Cities all filed answers. The CAISO's Market Surveillance Committee (MSC) also filed comments on the Barriers Report that was filed with the CAISO's April 28, 2009 compliance filing.

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<sup>8</sup> Order No. 719 at P 8, 578-583.

<sup>9</sup> *Id.* P 97, 581. See also Errata Notice, Docket No. RM07-19-000 (Mar. 23, 2009) (clarifying deadline).

### III. Discussion

#### A. Procedural Matters

12. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2009), the notices of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

13. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2009), prohibits an answer to a protest, unless otherwise ordered by the decisional authority. We will accept the answers filed by the CAISO, WPTF, and Six Cities because they have provided information that assisted us in our decision-making process.

#### B. Substantive Matters

14. We find that, with certain modifications, CAISO's filing complies with Order No. 719 in the areas of: (1) demand response and pricing during periods of operating reserve shortage; (2) long-term power contracting; and (3) market-monitoring policies. Accordingly, we accept CAISO's filing with respect to those issues, to be effective April 28, 2009, subject to a further compliance filing as discussed below. CAISO is directed to make the compliance filing within 30 days of the date of issuance of this order. This order makes no findings as to CAISO's compliance with the fourth area of reforms identified in Order No. 719: the responsiveness of RTOs and ISOs to their customers and other stakeholders. The Commission recently issued a notice announcing that its staff will hold a technical conference in the near future to provide a forum for interested participants to discuss that topic.<sup>10</sup> Following that technical conference, the Commission will issue a separate order addressing CAISO's compliance with this aspect of Order No. 719.

##### 1. Demand Response and Pricing during Periods of Operating Reserve Shortages in Organized Markets

###### a. Ancillary Services Provided by Demand Response Resources

15. Order No. 719 required each RTO and ISO to accept bids from demand response resources, on a basis comparable to any other resources, for ancillary services (energy imbalance, spinning reserves, supplemental reserves, reactive and voltage control, and

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<sup>10</sup> See First Notice of Technical Conference on RTO/ISO Responsiveness, Docket Nos. ER09-1048-000, *et al.*, 74 Fed. Reg. 59159 (Nov. 13, 2009)..

regulation and frequency response) that are acquired in a competitive bidding process, if such demand response resources: (1) are technically capable of providing the ancillary service within the response time requirements and meet reasonable requirements adopted by the RTO or ISO as to size, telemetry, metering and bidding; and (2) submit a bid under the generally-applicable bidding rules at or below the market-clearing price, unless the laws or regulations of the relevant electric retail regulatory authority do not permit a retail customer to participate. All accepted bids would receive the market clearing price.<sup>11</sup>

16. Additionally, Order No. 719 directed each RTO and ISO to file, as part of its compliance filing, a proposal to adopt reasonable standards necessary for system operators to call on demand response resources, together with mechanisms to measure, verify, and ensure compliance with any such standards.<sup>12</sup> Further, Order No. 719 required RTOs and ISOs to describe their efforts to develop adequate customer baselines.<sup>13</sup> It also required RTOs and ISOs to coordinate with each other in the development of technical requirements for demand response resources participating in ancillary services markets, and provide the Commission with a technical and factual basis for any necessary regional variations.<sup>14</sup> Finally, Order No. 719 required each RTO and ISO to allow demand response resources to specify limits on the duration, frequency and amount of their service in their bids to provide ancillary services or their bids into the joint energy-ancillary services markets in the co-optimized RTO or ISO markets.<sup>15</sup>

**i. CAISO's Filing**

17. The CAISO states that it currently complies with some, but not all, of the requirements of Order No. 719 regarding demand response, as explained below. The CAISO claims that it is consistent with the requirements of Order No. 719 by allowing demand response resources to participate in ancillary services markets to the extent they are able to comply with technical requirements. The CAISO explains that it competitively procures the equivalent of regulation and frequency response service, spinning reserve service, supplemental reserve service, and energy imbalance service. The CAISO explains that the CAISO Tariff defines regulation, spinning reserve, and non-

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<sup>11</sup> Order No. 719 at P 47, 49.

<sup>12</sup> *Id.* P 61.

<sup>13</sup> *Id.* P 57.

<sup>14</sup> *Id.* P 59.

<sup>15</sup> *Id.* P 81.

spinning reserve as ancillary services. The CAISO further states that, although its Tariff does not define energy imbalance service as an ancillary service, the CAISO does address energy imbalances through its competitive markets.

18. The CAISO explains that demand response resources that enter a Participating Load Agreement with the CAISO can provide those ancillary services for which they are technically qualified under the terms of the CAISO Tariff. At this time, demand resources are limited to providing non-spinning reserve service and imbalance energy only. The CAISO states that demand response resources currently are not able to provide regulation or spinning reserve service because the CAISO Tariff requires the CAISO to maintain “sufficient ancillary services...consistent with NERC and WECC reliability standards.”<sup>16</sup> The CAISO further explains that WECC defines regulating reserve as “Spinning Reserve, immediately responsive to Automatic Generation Control,”<sup>17</sup> and spinning reserve as “unloaded generation which is synchronized and ready to serve additional demand.”<sup>18</sup> The CAISO states, therefore, that by definition, demand response resources currently cannot meet the standards for regulation and spinning reserve since demand resources are not “generation,” as defined by the WECC. The CAISO also states that it may be technically difficult for demand response resources to respond immediately to system frequency.

19. The CAISO explains that it operates an existing “Participating Load Program” (PLP)<sup>19</sup> and is developing a “Proxy Demand Resource” (PDR) product. According to the CAISO, the Participating Load Program treats a demand response resource analogously

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<sup>16</sup> CAISO Filing, Transmittal Letter at 29 (citing section 8.1 of the CAISO Tariff).

<sup>17</sup> *Id.* (citing WECC Standard BAL-STD-002-0).

<sup>18</sup> *Id.*

<sup>19</sup> The CAISO previously filed two annual demand response reports detailing the amount of demand response that the CAISO has obtained through the PLP. The first report, titled “First Annual Report of the California Independent System Operator Evaluating Demand Response in The CAISO; Re: Calendar year 2007” was filed on January 25, 2008 in Docket No. ER06-615-018. The second report, titled “Second Annual Report of the California Independent System Operator Evaluating Demand Response in the CAISO; Re: Calendar Year 2008” was filed on January 15, 2009 in Docket No. ER06-615-037. These informational filings were made in response to the Commission’s June 25, 2007 order on compliance, in which we directed the CAISO to “file annual reports evaluating its demand response programs, including the amount of demand response it has elicited.” *See California Independent System Operator Corp.*, 119 FERC ¶ 61,313 (2007).

to a supply resource, and the CAISO is developing refinements to the PLP in its upcoming “Market and Performance” (MAP) initiative. According to the CAISO, the Proxy Demand Resource product will be a simplified mechanism for demand response resources to participate in CAISO markets, providing most of the same functionality as the PLP model, but without use of a custom load aggregation to schedule the customer’s underlying load. The CAISO states that PDR is intended to reduce barriers to participation for demand resources.

20. The CAISO notes that it will soon be in compliance with all requirements of Order No. 719 once it makes its MAP filings. To allow demand response resources to provide all ancillary service products, the CAISO is considering changing the technical requirements for providing regulation and spinning reserves, two products that demand resources have not been able to provide historically. The CAISO states that this change would be requested in the CAISO’s upcoming MAP filings. The CAISO states that it plans to file a standard authorization request with WECC, asking it to create a standards drafting team to rewrite the current WECC standards for regulation and spinning reserves in order to allow non-generation resources to provide these services. The CAISO also notes that it is working with other RTOs and ISOs to implement appropriate mechanisms to measure, verify and ensure compliance of demand resources’ performance, as required by Order No. 719.<sup>20</sup>

21. The CAISO finally notes that the Commission did not require that all Order No. 719 requirements be implemented by the time of the instant filing. The CAISO explains that the Commission only required a description of the action that the CAISO has taken, or plans to take, to comply with the requirements of the order. The CAISO also states that the Commission explicitly stated in Order No. 719 that it did not intend to displace current RTO and ISO timelines for the development of market and software enhancements, which would include MAP. The CAISO claims that the MAP enhancements will achieve the Commission’s objectives that are identified in Order No. 719 when implemented in accordance with the existing timelines. Further, the CAISO notes that the Commission’s rulings on the MRTU Tariff indicate the Commission’s recognition that further enhancements of the CAISO’s demand response capabilities would not happen until the MAP initiative.

#### New Bidding Parameters

22. The CAISO states that the existing Participating Load Program permits Demand Response resources to specify the same parameters as generators and that the enhancement proposed under the Market and Performance filing will retain or expand current bidding capabilities. However, the CAISO notes that Order No. 719 stated that

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<sup>20</sup> CAISO Filing, Transmittal Letter at 32 (citing Order No. 719 at P 61).

Demand Response resources should be able to specify the maximum number of times that the resource may be dispatched during a day. The CAISO explains that generators cannot limit the number of instances that they are dispatched from one level to another. Accordingly, the CAISO asserts that in order to treat Demand Response resources comparable to generators, the CAISO interprets the Commission's requirement as applied to start-ups (i.e., the number of times that a resource is dispatched from 0 MW).

#### Smaller Demand Resource Assessment

23. The CAISO has provided an update of its progress in meeting Order No. 719 directives regarding this requirement. The CAISO has already launched a small demand response pilot, albeit not in the ancillary services markets, that concluded that demand response resources are feasible from the standpoint of dispatch, telemetry, and metering. The CAISO anticipates filing agreements with the Commission regarding three new pilot projects that will assess small demand resources' potential participation in ancillary service markets through aggregation.<sup>21</sup>

#### **ii. Protests and Comments**

24. Regarding the CAISO's commitment to provide demand resources with greater opportunities to supply additional ancillary services, Joint Parties state that the compliance filing should be more comprehensive and explicit with respect to existing technical standards, which should be carefully evaluated to determine (a) whether specifications discourage competition with narrow generator-centered definitions, (b) whether specifications can accommodate aggregations of small resources, (c) whether the specifications are truly necessary from an implementation perspective, and (d) whether there are less costly methods of achieving compliance with the appropriate standard. Joint Parties state, for example, that a requirement for telemetry with a four second scan interval is quite costly, thus ensuring that only the largest customers will be able to afford the initial outlay. Joint Parties state that it therefore may be difficult for a customer to realize enough benefit from participating in the ancillary services market to justify the expenditure required to meet such a metering requirement.

25. Joint Parties also state that the Commission should encourage WECC to take a more progressive approach to technical and operating standards for ancillary services so that promising technologies are not unduly limited in the kinds of ancillary services they can provide. Joint Parties state that, while the standards should not be weakened or

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<sup>21</sup> The CAISO filed all three pilot projects with the Commission June 26, 2009 in Docket Nos. ER09-1361-000, ER09-1362-000, and ER09-1363-000. The Commission accepted these pilot program filings in an order issued on August 25, 2009. *See Cal. Indep. Sys. Operator Corp.*, 128 FERC ¶ 61,184 (2009).

diluted in any way that could negatively impact reliability, the standards should be based on the needs of transmission operators rather than on outdated standards predicated on old technologies. Joint Parties also suggest that the CAISO review the interpretations of PJM and Midwest ISO relative to the ability of demand resources to provide both regulation and spinning reserves. SWP strongly supports the CAISO's endeavors to convince the WECC to permit demand-based resources to provide spinning reserves, and requests that the Commission support removal of WECC's discriminatory restriction of this service to generators only.

26. SoCal Edison states that once the NERC complies with Order No. 693, then to the extent the CAISO believes that the WECC reliability standards need to be reviewed and modified in order to further demand response participation in ancillary services markets, the CAISO should utilize WECC's standard authorization request process to recommend necessary changes. SoCal Edison asserts that the CAISO should not circumvent the WECC process and file its own reliability standards with the Commission. SoCal Edison argues that while doing so may comply with Order No. 719, it produces an undesirable result. SoCal Edison asserts that CAISO tariffs should not be the vehicle for establishing or modifying reliability standards. SoCal Edison notes that WECC has well-established policies and procedures for the proper design and review of these standards. SoCal Edison states that rather than circumventing this process via the tariff, the Commission should encourage WECC to evaluate the enhanced use of demand response resources in ancillary service markets and recommend any appropriate changes.

27. Wal-Mart notes that the CAISO has been diligently working to develop the technical capabilities to incorporate the two ancillary services that currently are not available. Wal-Mart believes that this process complies with the Order No. 719 requirements for the CAISO to develop and report to the Commission on its compliance with the requirement to accept bids for ancillary services from demand response resources on a comparable basis to other resources. Wal-Mart also agrees that the important point of Order No. 719 is to establish comparable rules among supply side resources and demand response resources, and believes that the CAISO complies with Order No. 719 through its MAP enhancements program and workshops for extending the ancillary services demand response resources can provide.

28. PG&E notes that, under Order No. 719, the CAISO must accept bids from demand response resources in the CAISO's ancillary services markets on a basis comparable to any other resources, "unless not permitted by the laws and regulations of the relevant electric retail regulatory authority," and the CAISO must permit qualified aggregators of retail customers to bid demand response directly into the CAISO's organized markets, "unless the laws and regulations of the relevant electric retail regulatory authority expressly do not permit a retail customer to participate." PG&E notes that, in its compliance filing, the CAISO spends little time discussing the interaction of the CAISO

and the CPUC, the “relevant retail regulatory authority,” with respect to the incorporation of demand response into the CAISO markets.

29. PG&E states that it has urged the CPUC to fully evaluate the effect that incorporation of demand response into the CAISO markets will have on CPUC demand response policies. PG&E has urged the CPUC, in the interim while it carries out that evaluation, to “clearly state that: (1) [demand response] should continue to be bid into the CAISO through the [Investor-Owned Utilities] IOUs; and (2) it is premature for aggregators to directly participate in the CAISO market.”<sup>22</sup> PG&E states that, while no Commission action is necessary at this time, the CAISO’s ongoing process to incorporate demand response into its markets should reflect the input of the CPUC, who should evaluate the effect that incorporation of demand response into the CAISO markets would have on the CPUC’s demand response policies.

30. Regarding Participating Load Refinements under MAP, SoCal Edison notes that on page 20 of the Compliance Report the CAISO states that:

The CAISO believes this concern is misplaced, in light of the fact that 90% of load is served through bundled, retail rates, and customers therefore do not see the Locational Marginal Price. For large load-serving entities, the PLP model actually provides the right incentive to sell demand response in the high cost areas because such actions will drive down the overall Default Load Aggregation Price.

SoCal Edison notes that access rules are under review in California and therefore the amount of load served through bundled retail rates is subject to change. SoCal Edison argues that CAISO tariffs should be developed through the CAISO’s well-functioning stakeholder process and should not be judged by a cursory determination of the size of a problem in today’s market. SoCal Edison argues that tariffs should be based on well-founded principles and should be fully vetted by stakeholders to produce optimum results. SoCal Edison asserts that the Commission should remain supportive of this process and not use compliance filings as an independent means to effect change.

31. Joint Parties note that Order No. 719 requires RTOs and ISOs to describe their efforts to “develop adequate customer baselines” to help system operators measure and verify load reductions and thus determine the proper value of the demand response reduction.<sup>23</sup> Joint Parties plan to participate in CAISO’s stakeholder effort over the next

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<sup>22</sup> PG&E Comments at 4 (citing CPUC proceeding A. 08-06-003, Exhibit 202, page 1-3).

<sup>23</sup> Joint Parties Comments at 6 (citing Order No. 719 at P 57).

several months to develop appropriate customer baselines for a Proxy Demand Resource by December 31, 2009. Joint Parties note that as baselines are currently the only method for measuring and verifying the demand response reduction, this effort is a crucial component of direct participation in wholesale markets.

32. In its comments in ER09-1048-000,<sup>24</sup> ELCON encourages the Commission to scrutinize the provisions relating to demand response in each of the compliance filings to ensure they meet Order No. 719's "comparable terms" and "reasonableness" criteria. ELCON maintains that despite Order No. 719's clear mandate to improve demand response access to markets, the compliance filings of each RTO and ISO do not implement either the directives or the overarching principles enumerated in Order No. 719. ELCON maintains that the RTOs and ISOs have not granted comparable treatment and have not established reasonable terms for demand response. Accordingly, the primary shortcoming of the demand response protocols is that the RTOs and ISOs appear to have incorrectly equated "comparable treatment" to "identical treatment."

33. ELCON maintains that RTOs and ISOs have proposed to place conditions and requirements on demand response providers identical to those for generators, based on systems and practices originally established to meet the specific needs of generation, and it argues that applying such a one-size-fits-all standard will inhibit demand response. Instead of blindly applying standards designed for generation resources, ELCON argues that RTOs and ISOs should recognize that a policy of identical conditions does not result in equivalent opportunities, because demand response resources and generation resources have fundamentally different attributes. Finally, ELCON asserts that when implementing "comparable treatment," the protocols for demand response providers should not be based on the limitations of generators but instead on a source-neutral basis that also reflects concern for system reliability.

34. In addition, ELCON states that RTOs and ISOs should pursue nationwide uniformity with respect to the treatment of demand response resources. ELCON maintains that the lack of standardization among the RTOs and ISOs with respect to demand response protocols imposes significant costs on the large industrial consumers who likely will provide the bulk of demand response resources. ELCON states that large industrial customers typically have many facilities throughout the country and often have major loads within the footprints of more than one RTO or ISO. ELCON maintains that it is a tremendous burden for demand response-capable loads to respond to the different, often conflicting, rules and procedures. According to ELCON, the complexity and burden of addressing regionally-disparate demand response programs on a case-by-case basis inhibits the participation of demand response resources. However, through

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<sup>24</sup> ELCON filed the same comments in each of the RTO and ISO compliance filing proceedings.

standardization, RTOs and ISO can reduce delays, inefficiencies, and transaction costs for demand response providers. In its comments, ELCON suggests that it is not too late for the Commission to revisit the issue to adopt *pro forma* tariff language that would promote demand response consistently on a nationwide basis. ELCON also supports a national conference among the six RTOs and ISOs to discuss consistency with respect to demand response resources.

### iii. Commission Determination

35. With one exception, we will accept the CAISO's filing as in compliance with the directives of Order No. 719 as it relates to allowing demand response resources to provide ancillary services, insofar as the CAISO has provided us with an adequate roadmap to full compliance. We acknowledge the CAISO's intention to achieve the objectives of Order No. 719 when its MAP initiative is implemented.<sup>25</sup> Once submitted, the MAP initiative filings containing demand resource enhancements will be analyzed on a *de novo* basis to determine if they meet all of the directives of Order No. 719. The CAISO has provided a roadmap to compliance with the directives of Order No. 719, and we accept that roadmap today, but the onus remains on the CAISO to timely file a fully compliant enhanced demand resource proposal that addresses all directives of Order No. 719 regarding demand response participation in its markets. We also note that the CAISO has been working on the design and implementation of an enhanced demand resource program since the Market Redesign and Technology Upgrade (MRTU) proposal was accepted in 2006.<sup>26</sup> In the MRTU Order, the Commission directed the CAISO to work with interested stakeholders in developing new avenues for incorporating demand resources into the CAISO markets.<sup>27</sup> The MAP initiative is expected to address these and other issues. While there is currently no concrete timeline related to the MAP initiative filings that will enhance demand resource participation, we note that the final draft proposal of the enhanced demand resource product – the PDR product – was recently approved by the CAISO Board of Governors,<sup>28</sup> and is currently scheduled for implementation in the spring of 2010.<sup>29</sup> In Order No. 719, we noted that no compliance requirement was meant to “displace the timelines of any market improvements that RTOs

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<sup>25</sup> CAISO Filing, Transmittal Letter at 24.

<sup>26</sup> *Cal. Indep. Sys. Operator Corp.*, 116 FERC ¶ 61,274 (2006) (MRTU Order).

<sup>27</sup> *Id.* P 690.

<sup>28</sup> “General Session Minutes ISO Board of Governors Meeting,” September 10-11, 2009 at P 4-5. <http://www.caiso.com/245a/245a9ec9407b0.pdf>.

<sup>29</sup> See “Memorandum re: Briefing on 2009-2011 Market Initiatives Release Plan,” October 21, 2009. <http://www.caiso.com/244f/244f93f02ba00.pdf>.

and ISOs are currently undertaking.”<sup>30</sup> Nevertheless, we expect the CAISO to meet its current schedule in implementing demand resource enhancements.

36. We reject CAISO’s request to not allow demand resources to specify the number of times they may be dispatched to different output levels during the day. Order No. 719 stated:

The Commission determines that each RTO and ISO is required to allow demand response resources to specify limits on the duration, frequency and amount of their service in their bids to provide ancillary services—or their bids into the joint energy ancillary services markets in the co-optimized RTO markets. As noted in the NOPR (and several commenters agree), these limits are comparable to the limits generators may specify on price, quantity, startup and no-load costs, and minimum downtime between starts. All RTOs and ISOs must incorporate new parameters into their ancillary services bidding rules that allow demand response resources to specify a maximum duration in hours that the demand response resource may be dispatched, a maximum number of times that the demand response resource may be dispatched during a day, and a maximum amount of electric energy reduction that the demand response resource may be required to provide either daily or weekly.<sup>31</sup>

37. The “comparable” treatment of demand resources, in this case, dictates recognition of the inherent characteristics of demand response resources in determining bidding parameter rules, not necessarily identical treatment as afforded to generation. Demand response resources must be provided with the bidding flexibility laid out in Order No. 719 in order to have comparable access to the CAISO’s markets. The CAISO has misinterpreted the Commission’s intent regarding the requirement that demand resources be allowed to specify the number of times they are “dispatched” during a day. This requirement was intended to provide demand resources the ability to specify the maximum number of times that they are dispatched from one output level to another, not simply the number of start-ups in a given day. The proper recognition of demand response resource characteristics in enforcing this bidding parameter is similar to the market rules treatment of certain types of generation that allow for those types of generation to have competitive access to the CAISO’s markets. For example, generators may establish “forbidden operating regions” of output at which the CAISO cannot dispatch the resource. Also, generators may elect to be “use-limited” resources<sup>32</sup> or to

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<sup>30</sup> Order No. 719 at P 579.

<sup>31</sup> *Id.* P 81.

<sup>32</sup> “Use-limited” resources are those that, due to design considerations,

(continued...)

provide “Contingency Only”<sup>33</sup> service in the ancillary services market. This same comparability of access should be afforded to demand response resources as well, and thus, we will require the CAISO to allow demand response resources the ability to specify the maximum number of times that they may be dispatched to a different output level during a day.

38. While Order No. 719 requires that the RTO accept bids from demand response resources in ancillary services markets to the extent technically feasible, the CAISO states that demand response resources currently cannot meet the WECC standards for regulation or spinning reserve service because demand resources are not “generation,” as defined by the WECC. As stated previously, the CAISO is in compliance with the directives of Order No. 719 insofar as it has provided us with an adequate roadmap to full compliance. The Commission acknowledges the CAISO’s intention to achieve the objectives of Order No. 719 when its MAP initiative is implemented.<sup>34</sup>

39. Joint Parties’ request for more detail in the CAISO’s filing regarding demand response participation in the ancillary services markets is unfounded. The CAISO has provided adequate detail in its roadmap to full compliance with the directives of Order No. 719, and the very issues for which Joint Parties request more detail are currently being considered in the CAISO stakeholder process; we expect the CAISO to articulate the details of interest to the Joint Parties in its upcoming proposal. We therefore encourage Joint Parties and other market participants to continue participation in the CAISO stakeholder process. Regarding ELCON’s request that the Commission conduct thorough, independent analyses of all Order No. 719 compliance filings, we note that the Commission is required under section 205 of the FPA, to ensure that rates are just and reasonable and not unduly discriminatory or preferential, and the instant filing in this proceeding is no exception.

40. Regarding PG&E’s comments requesting that the CAISO’s ongoing demand response development process, the Commission strongly encourages all stakeholders to participate in the development of demand resource participation in the CAISO markets.

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environmental restrictions on operations, cyclical requirements, (such as the need to recharge or refill), or for other non-economic reasons, are unable to operate continuously on a daily basis, but are able to operate for a minimum set of consecutive trading hours each trading day. *See* Appendix A of the CAISO Tariff.

<sup>33</sup> A “Contingency Only” resource is one that provides operating reserve capacity that may be dispatched by the CAISO only in the event of a contingency or an imminent or actual system emergency. *Id.*

<sup>34</sup> CAISO Filing, Transmittal Letter at 24.

We also encourage the CAISO to consider the comments of all interested stakeholders in designing and implementing demand response enhancements and initiatives, including the directives contained in Order No. 719.

41. We disagree with SoCal Edison's assertion that the CAISO is using the instant proceeding to change the demand response development process. The CAISO has provided no tariff revisions related to demand response participation in its markets. However, we do agree with SoCal Edison that any such revisions should come as a result of the CAISO's ongoing stakeholder process.

42. We agree with ELCON that "comparability" is not achieved by setting conditions for demand response resources the same as those set for generating resources. We address a few specific issues in this order and require CAISO to adequately address "comparability" in a way which enables demand response resources to participate on terms that both address the characteristics of demand response resources and ensure reliable operations. However, ELCON's assertion regarding "comparable treatment" of demand response vis-à-vis generation is, in the case of the CAISO, premature. The CAISO has not yet filed its MAP initiative demand resource enhancement proposal, and thus it is inappropriate to prejudge the CAISO's upcoming filing on the comparability standard before it is fully vetted in the stakeholder process and filed with the Commission.

43. ELCON also requests that the Commission pursue uniform demand response standards. In Order No. 719, the Commission specifically chose not to develop "a standardized set of minimum requirements for minimum size bids, measurement, telemetry and other factors, and instead allowed RTOs and ISOs to develop their own minimum requirements, including bidding parameters."<sup>35</sup> It would be inappropriate to use the compliance filing process as a forum to reconsider that determination in the Final Rule. However, we note that the North American Energy Standards Board (NAESB) has adopted Phase I business practice standards for the measurement and verification of demand response, a first step in a process that may lead to greater standardization through the NAESB consensus process.<sup>36</sup> Furthermore, the Commission will continue to examine the need for further generic policy reforms to identify and eliminate barriers to comparable treatment of demand response, and ELCON's concerns with standardization can be addressed in relevant future Commission proceedings.

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<sup>35</sup> Order No. 719 at P 86.

<sup>36</sup> *Standards for Business Practices and Communication Protocols for Public Utilities*, Notice of Proposed Rulemaking, Docket No. RM05-5-017, FERC Statutes and Regulations ¶ 32,646 (Sep. 17, 2009).

**b. Eliminating Deviation Charges During System Emergencies**

44. In Order No. 719, the Commission required RTOs and ISOs to modify their tariffs to eliminate a deviation charge to a buyer in the energy market for taking less electric energy in the real-time market than was scheduled in the day-ahead market. This charge would be eliminated only during a real-time market period for which the RTO or ISO declares an operating reserve shortage or makes a generic request to reduce load in order to avoid an operating reserve shortage.<sup>37</sup> Order No. 719 also directed RTOs and ISOs to modify their tariffs to eliminate deviation charges for virtual purchasers, during the same period as they are eliminated for physical purchasers, unless the RTO or ISO makes a showing upon compliance that it would be appropriate to assess such deviation charges for virtual purchasers during this period.<sup>38</sup>

**i. CAISO's Filing**

45. The CAISO claims that its Tariff complies with the Commission's directives regarding the imposition of deviation charges on real-time purchasers since the current CAISO markets have no deviation penalties for over-scheduling of demand. The CAISO states that because of the CAISO's imbalance market, a Scheduling Coordinator for load that uses [less] energy than scheduled is paid the Locational Marginal Price (i.e., if a demand response resource takes less energy in real-time than was scheduled day-ahead, then the demand response resource is paid for the difference as uninstructed energy, with no deviation charges)

46. The CAISO notes that the CAISO Tariff does have deviation charges in section 11.23 (which is not currently effective) and section 11.24. Section 11.23, however, has an exception for load, and section 11.24 only applies to under-scheduling, i.e., circumstances in which the metered load is greater than the amount scheduled day-ahead. The CAISO states, therefore, that loads that reduce demand in response to a system emergency or a CAISO request would face no penalty charges.

47. The CAISO also notes that under the CAISO Tariff, there are no virtual purchasers. The CAISO states that, at the ties, there are purchasers that are the equivalent of virtual purchasers, i.e., system resources without attached physical resources. The CAISO explains that the discussion above is equally applicable to such purchasers.

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<sup>37</sup> Order No. 719 at P 111.

<sup>38</sup> *Id.* P 127.

ii. **Commission Determination**

48. The Commission finds that the CAISO is in compliance with the directive of Order No. 719 regarding elimination of deviation charges during system emergencies. To maintain compliance, the Commission would expect to see this exemption of demand response resources and virtual bidders from deviation charges during system emergencies retained in the MAP filings.

c. **Aggregation of Retail Customers**

49. Order No. 719 required RTOs and ISOs to amend their market rules as necessary to permit an Aggregator of Retail Customers to bid demand response on behalf of retail customers directly into the RTO's or ISO's organized markets, unless the laws or regulations of the relevant electric retail regulatory authority do not permit a retail customer to participate. The Commission determined that allowing an ARC to act as an intermediary for many small retail loads that cannot individually participate in the organized market would reduce a barrier to demand response participation.<sup>39</sup>

50. The Commission directed RTOs and ISOs to submit compliance filings to propose amendments to their tariffs or otherwise demonstrate how their existing tariffs and market rules comply with the Final Rule.<sup>40</sup> The Commission indicated that tariff revisions are to be made in accordance with certain specified criteria and flexibilities:

(1) The ARC's demand response bid must meet the same requirements as a demand response bid from any other entity, such as a load-serving entity. For example:

- Its aggregate demand response must be as verifiable as that of an eligible load-serving entity or large industrial customer's demand response that is bid directly into the market;
- The requirements for measurement and verification of aggregated demand response should be comparable to the requirements for other providers of demand response resources, regarding such matters as transparency, ability to be documented, and ensuring compliance;
- Demand response bids from an ARC must not be treated differently than the demand response bids of a load-serving entity or large industrial customer.

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<sup>39</sup> *Id.* P 154.

<sup>40</sup> *Id.* P 163.

(2) The bidder has only an opportunity to bid demand response in the organized market; it does not have a guarantee that its bid will be selected.

(3) The term “relevant electric retail regulatory authority” means the entity that establishes the retail electric prices and any retail competition policies for customers, such as the city council for a municipal utility, the governing board of a cooperative utility, or the state public utility commission.

(4) An ARC can bid demand response either on behalf of only one retail customer or multiple retail customers.

(5) Except for circumstances where the laws and regulations of the relevant retail regulatory authority do not permit a retail customer to participate, there is no prohibition on who may be an ARC.

(6) An individual customer may serve as an ARC on behalf of itself and others.

(7) The RTO or ISO may specify certain requirements, such as registration with the RTO or ISO, creditworthiness requirements, and certification that participation is not precluded by the relevant electric retail regulatory authority.

(8) The RTO or ISO may require the ARC to be an RTO or ISO member if its membership is a requirement for other bidders.

(9) Single aggregated bids consisting of individual demand response from a single area, reasonably defined, may be required by RTOs and ISOs.

(10) An RTO or ISO may place appropriate restrictions on any customer’s participation in an ARC-aggregated demand response bid to avoid counting the same demand response resource more than once.

(11) The market rules shall allow bids from an ARC unless this is not permitted under the laws or regulations of relevant electric retail regulatory authority.

**i. CAISO’s Filing**

51. The CAISO states that the CAISO Tariff, market design, and software cannot currently accommodate the provision of demand response through an ARC. The CAISO claims that the implementation of such functionality requires resolution of complex scheduling, metering, and settlement issues. The CAISO expects to resolve these issues through the MAP initiative, specifically by implementation of the PDR product.

52. The CAISO claims that it is actively moving forward with efforts to enable direct participation by ARCs. The CAISO notes that on December 22, 2008, it released a direct participation issue paper,<sup>41</sup> which was circulated for public comment. The CAISO claims that on January 5, 2009, it conducted a stakeholder conference call to discuss the Direct Participation Issue Paper.

53. The CAISO states that it is currently working on the resolution of certain business issues. In its filing, the CAISO anticipated that a stakeholder meeting, scheduled for April 30, would consider efforts needed in the following seven key areas: (1) qualification – program definition, participant and resource qualification; (2) registration – resource characteristics, enrollment, transfers, testing and auditing; (3) scheduling – system and resource forecasting, resource scheduling and bidding; (4) notifications – market schedules & awards, real-time dispatch, outages; (5) metering & telemetry – data availability, data sharing, data type, accuracy and granularity; (6) settlement – calculation of load changes, calculation of credits and charges; and (7) performance and compliance evaluation – resource, participant, program, and system performance. As is the case with other demand response enhancements included in the MAP initiative, the CAISO believes that the effort discussed above is consistent with the Commission’s directive that the CAISO file a description of the actions that it has taken or plans to take to comply with Order No. 719, without displacing timelines for the development of other major enhancements.

## ii. Protests and Comments

54. Joint Parties support CAISO’s conceptual design for PDR and believe PDR will allow ARCs to bid demand response resources directly in CAISO markets. Joint Parties state that the CAISO appropriately recognizes that there are a number of issues that need to be resolved prior to the end of 2009 for PDR to be available for Summer 2010, and Joint Parties intend to work closely with CAISO staff and stakeholders to facilitate the development of protocols that will encourage the direct participation of demand response resources in CAISO energy and ancillary services markets by May 2010.

55. Wal-Mart asserts that completion of the MAP initiative will help resolve the current complexities that prevent ARCs from being able to bid demand response into the CAISO markets. While the Commission must ultimately determine whether the outcome of that initiative satisfies the requirements of Order No. 719, Wal-Mart is confident that the CAISO will continue to effectively address the concerns the Commission and stakeholders have raised.

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<sup>41</sup> “Issue Paper, Direct Participation of Demand Response Resources in CAISO Electricity Markets,” found at <http://www.caiso.com/20a5/20a5e36d2a40.pdf>.

**iii. Commission Determination**

56. We find the CAISO in compliance with the directive of Order No. 719 regarding ARCs, insofar as the CAISO has provided us with an adequate roadmap to full compliance. Development and implementation of ARCs in the CAISO markets should be fully addressed by the CAISO in its MAP initiative filings providing for demand resource enhancements. However, we note that, once filed, the MAP initiative filings will be reviewed closely by the Commission to ensure that the CAISO's ARC proposal meets the Commission's objectives laid out in Order No. 719.

**d. Market Rules Governing Price Formation During Periods of Operating Reserve Shortage**

57. In Order No. 719, the Commission established reforms to remove barriers to demand response by requiring RTOs and ISOs to reform their market rules in such a way that prices during operating reserve shortages more accurately reflect the value of energy during such shortages. Order No. 719 required each RTO or ISO to reform or demonstrate the adequacy of its existing market rules to ensure that the market price for energy reflects the value of energy during an operating reserve shortage.<sup>42</sup> As such, it stated that each RTO or ISO may propose in its compliance filing one of four suggested approaches to pricing reform during an operating reserve shortage, or develop its own alternative approach to achieve the same objectives.<sup>43</sup> Each RTO or ISO must address how its selected method of shortage pricing interacts with its existing market design.<sup>44</sup>

58. Order No. 719 also required each RTO or ISO to provide adequate factual support for its compliance filing. To that end, the Commission outlined six criteria it will consider in reviewing whether the factual record compiled by the RTO or ISO meets the

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<sup>42</sup> Order No. 719 at P 194.

<sup>43</sup> The four approaches are: (1) RTOs and ISOs would increase the energy supply and demand bid caps above the current levels only during an emergency; (2) RTOs and ISOs would increase bid caps above the current level during an emergency only for demand bids while keeping generation bid caps in place; (3) RTOs and ISOs would establish a demand curve for operating reserves, which has the effect of raising prices in a previously agreed-upon way as operating reserves grow short; or (4) RTOs and ISOs would set the market-clearing price during an emergency for all supply and demand response resources dispatched equal to the payment made to participants in an emergency demand response program. *Id.* P 208.

<sup>44</sup> *Id.* P 204.

requirements of the rule.<sup>45</sup> The Commission allowed an RTO or ISO to phase in any new pricing rules over a few years, provided that this period is not protracted.<sup>46</sup> The phase-in period must be justified as part of the RTO's or ISO's overall proposal to change its pricing rules.

**i. CAISO's Filing**

59. Under the current CAISO Tariff, as approved by the Commission, the CAISO states that it has a limited scarcity pricing mechanism that raises energy bids to the bid cap when there are insufficient energy bids in real-time and no contingency events have occurred. The CAISO notes that in its September 2006 MRTU Order,<sup>47</sup> the Commission ordered the CAISO to implement a more comprehensive scarcity pricing mechanism during periods of operating reserve shortages in its post-MRTU enhancements (currently, the MAP enhancements). The CAISO states that the Commission directed that prices should rise when energy and reserves are short in both the day-ahead and real-time markets regardless of whether there is a transmission or generation outage.<sup>48</sup> The CAISO notes that according to the Commission's order, the mechanism should apply administratively determined graduated prices to various levels of reserve shortage so that prices would reflect the economic value of the reserves necessary to resolve the shortage; the prices for both reserves and energy in California should increase automatically as the severity of the shortage increases.<sup>49</sup>

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<sup>45</sup> The six criteria are: (1) improve reliability by reducing demand and increasing supply during periods of operating reserve shortages; (2) make it more worthwhile for customers to invest in demand response technologies; (3) encourage existing generation and demand resources to continue to be relied upon during an operating reserve shortage; (4) encourage entry of new generation and demand resources; (5) ensure that the principle of comparability in treatment of and compensation to all resources is not discarded during periods of operating reserve shortage; and (6) ensure market power is mitigated and gaming behavior is deterred during periods of operating reserve shortages including, but not limited to, showing how demand resources discipline bidding behavior to competitive levels. *Id.* P 246-247.

<sup>46</sup> *Id.* P 258.

<sup>47</sup> MRTU Order at P 1077.

<sup>48</sup> CAISO Filing, Transmittal Letter at 44 (citing MRTU Order at P 1077).

<sup>49</sup> *Id.* (citing MRTU Order at P 1079).

60. The CAISO notes that the Commission in Order No. 719 did not revise timelines for enhancements to RTO and ISO markets. The CAISO states that in the instant filing, therefore, the CAISO's obligation is to update the Commission on the status of its development of a scarcity pricing mechanism that complies with the Commission's orders. The CAISO states that in developing its scarcity pricing mechanism, the CAISO has followed its standard stakeholder process, which has involved multiple rounds of proposals with written comments and discussion after each round, extending for over a year. The CAISO has issued a straw proposal, a revised straw proposal, a draft proposal, a revised draft proposal, and a final proposal. The CAISO states that the initial issue paper was published on May 31, 2007, with a final proposal published July 15, 2008.<sup>50</sup>

61. The CAISO states that its staff initially planned to present a system-wide scarcity pricing design to the CAISO Governing Board (Governing Board, or Board) prior to the implementation of MRTU, after which the CAISO would work on the development of sub-regional scarcity pricing. The CAISO states that because of the need to focus on the MRTU implementation and on products with more immediate deadlines, the stakeholder process was temporarily placed on hold. The CAISO states that, during this period, the CAISO concluded that it would be beneficial to combine the consideration of system-wide and sub-regional scarcity pricing and to bring a combined proposal to stakeholders after both the CAISO and stakeholders have the advantage of experience under the MRTU markets. The CAISO states that under the revised schedule, the CAISO will reopen the stakeholder process 6 months after the start-up of MRTU (i.e., in October 2009) and present a combined system-wide and sub-regional scarcity pricing design. The CAISO states that a final design would be presented to the CAISO Governing Board upon completion of the stakeholder process.

62. The CAISO states that because it is not attempting to demonstrate the adequacy of its current systems and is not as yet able to propose its specific reforms, it would be premature to attempt to file the factual record in support of the CAISO's position. The CAISO states that it plans to file the full factual record required by Order No. 719 when it files its proposal.

## ii. Protests and Comments

63. Regarding Order No. 719's directive on price formation during periods of operating shortage, Joint Parties argue that the CAISO may not be able to meet the Commission-imposed timetable of implementing a graduated reserve shortage pricing

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<sup>50</sup> All of the documents issued by the CAISO, as well as stakeholder comments, are available on the CAISO's Web site at <http://www.caiso.com/1bef/1bef12b9b420b0.html>.

mechanism within 12 months after “MRTU Release 1.”<sup>51</sup> Joint Parties note that other than providing a date by which the stakeholder process would be reopened, the CAISO’s compliance filing did not set out any other target dates for completing the stakeholder process, obtaining approval from the CAISO Governing Board, submitting a design proposal for approval by the Commission, or implementation. Joint Parties point out that the CAISO’s stakeholder process to discuss the design was suspended in the middle of 2008, so the CAISO could focus on MRTU implementation.

64. Joint Parties assert that the principal reason an acceptable Scarcity Pricing mechanism was not included in MRTU Release 1 is because stakeholders were unable to agree on important elements of the design, including the degree of geographic granularity, cost allocation, an appropriate trigger mechanism, and the shape of the demand curve. Joint Parties claim that many of these disagreements remain to be resolved and unless the CAISO has a fully developed design that it is willing to unilaterally impose with little additional stakeholder input, it is likely that waiting until October to resume the stakeholder process will not allow enough time for the CAISO to hear and deal with stakeholder concerns, obtain Board and Commission approval, and still meet the April 1, 2010 start date.

65. Joint Parties note that the Commission has stated that “existing rules that do not allow for prices to rise sufficiently during an operating reserve shortage to allow supply to meet demand are unjust, unreasonable, and may be unduly discriminatory.”<sup>52</sup> Joint Parties state that, without a properly structured scarcity pricing mechanism, electricity users that might otherwise offer demand response resources into the CAISO’s energy and ancillary services markets lack an important motivation to do so. Joint Parties therefore request the Commission to (a) reaffirm its earlier instructions to the CAISO that a Scarcity Pricing mechanism that conforms to the 2006 MRTU Order be implemented on April 1, 2010, (b) direct the CAISO to resume its stakeholder process for Scarcity Pricing immediately, and (c) direct the CAISO to publish a schedule with defined milestones leading up to an April, 2010 implementation date. Joint Parties also assert that the Commission should also condition final approval of the CAISO’s implementation plan for Scarcity Pricing on a determination from the CAISO’s Department of Market Monitoring (the DMM) that the screens and systems it uses to detect and prevent exercise of market power are functioning properly and that the mechanisms approved for use provide the DMM with sufficient tools to prevent the exercise of market power.

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<sup>51</sup> MRTU Order at P 1079.

<sup>52</sup> Order No. 719 at P 192.

iii. **Commission Determination**

66. The Commission finds the CAISO to be in compliance with the directives of Order No. 719 regarding the implementation of price formation during periods of operating reserve shortages, insofar as the CAISO has provided us with an adequate roadmap to full compliance. Further, while the Commission recognized the Joint Parties' concern regarding the feasibility of the timeline previously imposed by the Commission on the CAISO to implement an adequate scarcity pricing mechanism, the Commission will not order the CAISO to take any specific steps or file any additional reports regarding its stakeholder process involving this issue. The Commission expects the CAISO to meet the deadline imposed by the Commission in its 2006 MRTU Order, and the Commission has been furnished with no evidence that the current deadline is infeasible.

e. **Reporting on Remaining Barriers to Comparable Treatment of Demand Response Resources**

67. Order No. 719 required each RTO and ISO to assess and report on any remaining barriers to comparable treatment of demand response resources that are within the Commission's jurisdiction, and to submit its findings and any proposed solutions to the Commission, along with a timeline for implementation.<sup>53</sup> The Commission required RTOs and ISOs to identify all known barriers, to provide an in-depth analysis of those that are practical to analyze in the compliance time frame given, and to supply a time frame for analyzing the remainder, including, but not limited to, technical requirements and performance verification limitations.<sup>54</sup> Finally, Order No. 719 required RTOs and ISOs to identify any significant minority views in its report.

68. The CAISO retained the consulting team of Freeman, Sullivan & Co. (FSC) and Energy and Environmental Economics Inc. (E3) to draft a report (Barriers Report) for the CAISO's review and adoption. The CAISO states that it hosted a web and telephone-based stakeholder conference on April 8, 2009, to review the preliminary results of the Barriers Report with stakeholders and to solicit additional feedback.<sup>55</sup> The CAISO thereafter provided stakeholders with the opportunity to submit written comments, which were considered in the preparation of the final report. The CAISO claims it has accepted the Barriers Report as accurately reflecting the concerns expressed by stakeholders. The

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<sup>53</sup> *Id.* P 274.

<sup>54</sup> *Id.* P 275.

<sup>55</sup> The CAISO states that the stakeholder presentation used in the conference is available at <http://www.aiso.com/2388/238811d7558f00.pdf>.

CAISO states that the barriers thus identified will be taken into consideration by the CAISO as it decides how best to encourage additional demand response participation in its markets. The CAISO states that stakeholders will have the opportunity for additional input when the CAISO proposes actions to accomplish that expanded participation. The consultants report identified a number of significant barriers to demand response in California, including reliability rules, exclusion of curtailment service providers from wholesale markets, limitations of currently installed metering and communications capabilities, and a number of potential market design issues.

69. On July 10, 2009, the ISO Market Surveillance Committee (MSC) filed its “Comments on Barriers to Demand Response and the Symmetric Treatment of Supply and Demand Resources” (MSC Comments).

70. A number of parties filed comments on barriers that demand response resources faced in seeking access to CAISO’s wholesale markets. RRI, Joint Parties, SWP, the CPUC and Industrial Customers all filed comments, and in many cases specific suggestions about barriers that should be addressed, processes that should be pursued, or collaborations required to address both state and Federal regulatory issues. Six Cities and CAISO filed answers.

#### **i. Commission Determination**

71. The Commission finds that the CAISO has complied with the directive of Order No. 719 to provide a list and full assessment of remaining barriers to comparable treatment of demand response resources that are within the Commission’s jurisdiction. We also find that the MSC has appropriately filed its comments on the Barriers Report, providing the Commission and stakeholders with valuable insights. The Commission will also accept the comments and answers to comments filed in this proceeding.<sup>56</sup>

### **2. Long-Term Power Contracting in Organized Markets**

72. In Order No. 719, the Commission required each RTO and ISO to dedicate a portion of its website for market participants to post offers to buy and sell electric energy on a long-term basis.<sup>57</sup> The Commission did not mandate any specific form for the

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<sup>56</sup> CAISO’s report and the comments and answers filed in this proceeding will provide information that will be considered by the Commission staff in its evaluation of remaining barriers to demand response participating in CAISO’s wholesale markets.

<sup>57</sup> Order No. 719 at P 277. The Commission defined “long-term” as one year or more, but stated that RTOs and ISOs may include offers for contracts of less than a year on their websites as well. *Id.*

website, but instead allowed each RTO or ISO to work with its stakeholders to implement the website. This discretion includes decisions over the type and amount of data to be posted by participants, whether participants must include a proposed price in their posting, and password and security requirements.<sup>58</sup> Order No. 719 directed each RTO or ISO to explain in its compliance filing the actions it has taken to comply with these requirements and to provide information on the bulletin board that it has chosen to implement.<sup>59</sup>

**a. CAISO's Filing**

73. The CAISO plans to provide a link on its website to a multi-ISO/RTO "bulletin board" page to be hosted by PJM which will allow willing sellers and buyers to voluntarily post and read offers for long-term power. The CAISO notes that the multi-ISO/RTO bulletin board is expected to launch in September 2009. The CAISO understands that additional information concerning the bulletin board will be set forth in PJM's Order No. 719 compliance filing. The CAISO understands that it will have certain administrative duties by way of identifying market participants who are eligible to post on the bulletin board. The CAISO states that it does not expect these duties, or any other aspect of the bulletin board, to result in significant costs. The CAISO is therefore not proposing any specific new cost recovery provisions in this area.

74. In PJM's Order No. 719 compliance filing, PJM states that it will recover the cost for the creation and maintenance of the bulletin board through the administrative service provisions of its OATT (Schedule 9-3 Market Support Service). PJM commits to cover ongoing operating costs up to \$20,000 annually. If annual operating costs exceed \$20,000, PJM states that it will provide the CAISO with six months notification so that they can elect to reimburse PJM for the increased costs on a pro rata basis, or develop an alternative solution to support long-term power contracting activities in the CAISO region.<sup>60</sup> The CAISO states that otherwise, neither the CAISO nor any of the other ISOs or RTOs will play any role beyond facilitating the posting of this information and will not review postings for accuracy. The CAISO states that, consistent with Order No. 719, the CAISO's link to the bulletin board will make it clear that neither the CAISO nor the other participating members will have any liability for the content of user postings.

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<sup>58</sup> *Id.* P 303.

<sup>59</sup> *Id.* P 309.

<sup>60</sup> PJM April 29, 2009 Filing, Docket No. ER09-1063-000, at 35-36.

**b. Commission Determination**

75. We accept CAISO's explanation on its compliance with this Order No. 719 requirement. We agree that a nationwide bulletin board will facilitate long-term power contracts between parties effectively, and we encourage participating ISOs and RTOs to work cooperatively in the development of this effort. We note that PJM's Order No. 719 compliance filing is pending in Docket No. ER09-1063-000.

**3. Market Monitoring Policies**

**a. Structure and Tools**

76. In Order No. 719, the Commission declined to mandate a specific structure for the MMU. Instead, it required each RTO or ISO, through its stakeholder process, to decide on its own MMU structure – external, internal, or hybrid.<sup>61</sup> Additionally, Order No. 719 required each RTO and ISO to include provisions in their tariffs: (1) obliging themselves to provide their MMUs with access to market data, resources and personnel sufficient to enable them to carry out their duties; (2) granting MMUs full access to the RTO or ISO database; and (3) granting MMUs exclusive control over any MMU-created data.<sup>62</sup>

**i. CAISO's Filing**

77. The CAISO states that it will maintain its hybrid market monitoring structure comprised of a Department of Market Monitoring (DMM) and the MSC. The CAISO states that Appendices O and P of the proposed revisions to the CAISO Tariff clearly indicate that there are two separate market monitoring bodies, spell out their respective responsibilities, and provide the DMM with the resources it needs to carry out its responsibilities.

78. The CAISO states that adequate tools will be provided to preserve DMM's independence. The CAISO explains that CAISO management has never denied the DMM the resources it needs to carry out its responsibilities. With respect to the CAISO granting the DMM full access to the RTO or ISO database of market information, the CAISO states that section 7 of Appendix P complies with this Commission requirement. The CAISO claims that it would grant exclusive control to the DMM of any data created by the DMM, including any reconfiguration of data or information obtained by the CAISO. The CAISO also states in section 7 of Appendix O that the MSC will review the catalogs of information, data, and evaluation criteria developed by the DMM.

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<sup>61</sup> Order No. 719 at P 326.

<sup>62</sup> *Id.* P 328.

**ii. Comments and Protests**

79. No adverse comments were filed.

**iii. Commission Determination**

80. We will accept the CAISO's market monitoring structure; however, we disagree with the CAISO's classification of its structure as a "hybrid," and therefore condition our acceptance on either a reclassification of the structure and the filing of any necessary tariff revisions to reflect that reclassification, or clarification in the tariff that it is an advisory role that the MSC performs.

81. The CAISO states that it employs a "hybrid" market monitoring structure, i.e., employing both an internal and external market monitor. However the CAISO does not assign the MSC with specific responsibility for performing any of the three core functions of a market monitoring unit.<sup>63</sup> The Commission defines a market monitoring unit as performing one or more of the three core functions.<sup>64</sup> The CAISO's internal market monitor – the DMM – is assigned responsibility for performing the three core functions of a market monitoring unit set out in Order No. 719.<sup>65</sup> The MSC, on the other hand, may review DMM's work products and provide comments to DMM. Appendix O of the CAISO Tariff provides that the MSC will perform an advisory service for the DMM and the Governing Board. The use of the word hybrid to describe the CAISO market monitoring structure does not follow its use in Order No. 719.<sup>66</sup> Thus, CAISO's

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<sup>63</sup> Core functions of an MMU include: identifying ineffective market rules, reviewing the performance of the markets, and making referrals to the Commission.

<sup>64</sup> Order No. 719 states that "Market Monitoring Unit means the person or entity responsible for carrying out the market monitoring functions that the Commission has ordered Commission-approved independent system operators and regional transmission organizations to perform" (amended paragraph to the Commission's regulations at Part 35, Section 28(b)(7)). 18 C.F.R. § 35.28(b)(7). Although P 341 of Order No. 719 may seem to suggest a Market Monitoring Unit could perform no core functions, such a reading would conflict with the definition of a Market Monitoring Unit set forth in 18 CFR 35.28(b)(7). The thrust of P 341 was to clarify that any internal division of an ISO/RTO that performs a core MMU function must report to the board, rather than to management. When this determination is read in conjunction with the definition of an MMU, it becomes clear that any internal division that holds itself out as a market monitor must both perform at least one of the core functions, and must report to the board rather than to management.

<sup>65</sup> CAISO Filing, Transmittal Letter at 61-62.

structure is not truly a hybrid one, as the external advisor (the MSC) is not assigned responsibility for any of the core market monitoring functions.

82. We therefore give the CAISO the option of either: (1) deeming its MSC as only providing consultation service, or (2) clarifying its tariff to indicate that the MSC is responsible to perform, in whole or in part, one or more of the core functions, and thus is a Rule 28(b)(7) MMU and part of a hybrid market monitoring structure. If the CAISO chooses the first option it must modify the tariff section covering the “CAISO Market Surveillance Committee” in Appendix O, section 5, which is currently titled “Duties of the Market Monitor” to read “Duties of the Market Surveillance Committee”. If CAISO chooses the second option and desires the MSC to be a Rule 28(b)(7) MMU, we will require the CAISO in its compliance filing to indicate how the MSC satisfies the requirements of Order No. 719. If the MSC is assigned responsibility to perform or assist in the performance of one or more core function, the CAISO will need to revise a number of sections of Appendix O accordingly. We find that giving the CAISO the choice outlined above is consistent with the Commission’s conclusion in Order No. 719 that each RTO and ISO should have the ability to choose which structural relationship it desires for its MMU. To comply with this directive, the CAISO is required to submit a compliance filing within 30 days of the date of issuance of this order, reflecting the option chosen and revisions to the contents of Appendix O of the CAISO Tariff and any other place in the CAISO Tariff that misclassifies the MSC.

#### **b. Oversight**

83. Order No. 719 requires MMUs, for purposes of supervision over their market monitoring functions, to report to their RTO’s or ISO’s board of directors, rather than management, with management representatives on the board excluded from this oversight function. An RTO or ISO may permit its MMU to report to management for administrative purposes (i.e., pension management and payroll).<sup>67</sup> For hybrid MMUs (i.e., MMUs with both an external and internal market monitor), the Commission stated that an internal market monitor may report to management, provided that if the internal MMU is responsible for carrying out any core MMU functions,<sup>68</sup> both it and the external market monitor must report to the board.<sup>69</sup>

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<sup>66</sup> Order No. 719 at P 327.

<sup>67</sup> *Id.* P 339.

<sup>68</sup> Core MMU functions include identifying ineffective market rules, reviewing the performance of the markets, and making referrals to the Commission.

<sup>69</sup> *Id.* P 341.

**i. CAISO's Filing**

84. The CAISO states that in section 3.1, it is adding a tariff requirement that the DMM report to the Governing Board on all matters pertaining to its core market monitoring responsibilities.<sup>70</sup> Currently, the DMM regularly reports to the Governing Board on its observations regarding market design, performance and structure as well as participant behavior. The CAISO states that the Board is readily available to protect the DMM's independence if the need arises. DMM can report any independence concerns directly to the CAISO Governing Board. The CAISO states that the Board can conduct special meetings, if it learns that management is overstepping its bounds.

85. The CAISO explains that section 3.1 also provides that the DMM shall inform CAISO management of its findings, enabling the CAISO to take immediate action, if appropriate, to remedy issues identified by the DMM. The CAISO states that it is very important to stakeholders that the CAISO be positioned to respond to any concerns regarding its markets in an immediate and effective manner. The CAISO asserts that under section 3.1, the DMM will report to the CAISO management for administrative matters, consistent with Order No. 719. The CAISO states that it is neither practical nor desirable to have the DMM report to the Board for administrative purposes.

86. The CAISO states that the DMM necessarily depends on senior management for a range of administrative support to be effective in carrying out its responsibilities. The DMM relies on the support of the CAISO's Information Technology department to assist with finding the systems that allow the DMM to effectively monitor market activity on a real-time basis, getting those systems installed and providing technical support. The CAISO claims that the DMM also relies on the procurement department for contracting support, the finance department for budget support, human resources for support in managing the employees effectively and ensuring it has resources needed to hire, train, and retain effective staff, and the legal department for advice and counsel. The CAISO states that all of these functions "work well" to support the DMM as an internal unit at the CAISO.

87. The CAISO states that combined with the new provisions that protect the independence of the DMM in carrying out its core functions – section 3.2 prohibits the alteration of reports by the CAISO, section 3.3 provides that the DMM director may not be terminated without approval by the Governing Board, and section 4 relates to adequate funding, tools and staffing to do the job – this administrative support will ensure the DMM is effective while preserving the DMM's independence.

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<sup>70</sup> CAISO Filing, Transmittal Letter at 55.

88. The CAISO similarly states that CAISO management has always respected the independent judgments of the DMM staff and has never attempted to dictate conclusions or alter recommendations. The CAISO states that the proposed tariff language ensures that such operating practices will continue and its proposed tariff language memorializes the current practice.

**ii. Comments and Protests**

89. No adverse comments were filed.

**iii. Commission Determination**

90. The Commission accepts the CAISO's proposed language regarding independence and oversight. The Commission will accept the CAISO's filing as requiring the DMM to report to the Governing Board for all core functions, and to report to management for administrative matters. We remind the CAISO that the functions performed by CAISO management on behalf of the DMM must be purely administrative in nature, and should not result in a material impact in the level of available funding and/or resources provided to the DMM. Budget levels and independence from CAISO management may be an area for future Commission review (i.e., via a potential future RTO audit). We note that the MSC provides the CEO and Governing Board with independent expert advice and recommendations. If the CAISO chooses to designate the MSC as an external Market Monitoring Unit, then we will require the CAISO to revise section 3 of Appendix O accordingly.

**c. Functions**

91. Order No. 719 required each RTO and ISO to assign the following functions to its MMU in its tariff:

(1) evaluate existing and proposed market rules, tariff provisions and market design elements, and recommend proposed rule and tariff changes to the RTO or ISO, and also to the Commission's Office of Energy Market Regulation and to other interested entities (i.e., state commissions and market participants);

(2) review and report on the performance of the wholesale markets to the RTO or ISO, the Commission, and other interested entities (i.e., state commission and market participants);<sup>71</sup> and

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<sup>71</sup> Order No. 719 provided that an RTO or ISO may require its MMU to submit its reports in draft form to the RTO or ISO for review, but may not alter the reports generated by the MMU or dictate its conclusions. Order No. 719 at P 360.

(3) identify and notify the Commission's Office of Enforcement of instances in which a market participant's behavior, or that of the RTO or ISO, may require investigation, including suspected tariff violations, violations of Commission-approved rules and regulations, market manipulation, and inappropriate dispatch that creates substantial concerns regarding unnecessary market inefficiencies.<sup>72</sup>

**i. CAISO's Filing**

92. The CAISO states that the DMM's responsibilities are outlined in section 5.1, 5.2, 5.3, 11 and 12 of Appendix P. The DMM's obligations to review market rules are addressed in section 5.1 and section 12. The CAISO explains that regarding flawed market rules the DMM will submit recommendations only and CAISO will implement solutions to problems the DMM identifies. The CAISO explains that "section 12 adopts virtually verbatim from the Order the regulations governing a market monitoring unit's obligation to refer perceived market rule flaws to the Commission."<sup>73</sup>

93. The CAISO explains that in section 5.2 the DMM must also report on market trends quarterly via quarterly reports and comprehensive annual state of the market reports. The CAISO notes that the DMM must also conduct conference calls in conjunction with its quarterly reports. The CAISO explains that in section 5.3 the DMM must also refer to the Commission instances in which a market participant or the CAISO itself is suspected of a Market Violation. For all Rules of Conduct violations, it is the CAISO's responsibility to investigate potential violations, not the market monitor's. The CAISO explains that it will refer to the DMM for further investigation "any matter for which the particular circumstances preclude the objective determination that a Rules of Conduct violation did or did not occur, and if DMM concurs with the CAISO's conclusion that the circumstances preclude such an objective determination, then DMM shall refer the matter to the Commission under the protocol on referrals outlined in Section 11 of Appendix P."<sup>74</sup>

94. In Appendix A of the CAISO Tariff, the term Market Violation is defined as "A violation of a market behavior rule promulgated by the Commission or a violation of a provision of this tariff other than those provisions that carry a sanction specifically enumerated under Section 37 of this Tariff." The CAISO states that this definition

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<sup>72</sup> *Id.* P 354.

<sup>73</sup> CAISO Filing, Transmittal Letter at 61.

<sup>74</sup> *Id.* 228, "(Blacklined Tariff Sheet)."

“tracks the definition provided in the Commission’s market monitoring policy statement.”<sup>75</sup>

**ii. Comments and Protests**

95. No adverse comments were filed.

**iii. Commission Determination**

96. The Commission accepts most aspects of the CAISO’s filing relating to the functions of the DMM, as identified in Order No. 719. We accept the CAISO’s delineation of responsibilities of the DMM, including responsibility for quarterly and annual reporting and performance of the three core functions, as identified by Order No. 719. The Commission also accepts the CAISO’s proposal as it relates to the functions of the MSC, including, its ability to review and provide pre-publication comment on all quarterly and annual reports that the DMM produces per Appendix O section 5.6. If the CAISO chooses to designate the MSC as an external Market Monitor Unit, then we will require the CAISO to revise Appendix O, as noted above in Paragraph 82, to reflect the core functions that the MSC will perform. Therefore, we direct the CAISO to submit a compliance filing within 30days of the date of issuance of this order consistent with Paragraph 82 above.

97. We will require the CAISO to conform its proposed definition of Market Violation to that set forth in our regulations.<sup>76</sup> The protocols for the referral of suspected violations to the Commission, which the CAISO includes in its tariff, use this term, and must therefore be consistent with the Commission’s definition.

98. We also observe that the CAISO Tariff’s section 37 includes sanctions for some matters that do not meet the test set out by the Commission for activity that is subject to sanction by the RTO or ISO itself. In order for an RTO or ISO to impose its own sanction for a given activity, three qualifications must be met:<sup>77</sup>

- (1) The activity must be expressly set forth in the tariff,
- (2) The activity must involve objectively identifiable behavior, and

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<sup>75</sup> *Id.* 62.

<sup>76</sup> 18 C.F.R. § 35.28(b)(8).

<sup>77</sup> *Market Monitoring Units in Regional Transmission Organizations and Independent System Operators*, 111 FERC ¶ 61,267, at P 5 (2005).

- (3) The activity does not subject the actor to sanctions or consequences other than those expressly approved by the Commission and set forth in the tariff, with the right of appeal to the Commission.

99. While many of the activities subject to sanction set forth in section 37 of the CAISO's tariff do meet these tests, sections 37.5 and 37.6 impose sanctions for more broadly worded activity that does not. Section 37.5.1.1 states that "The Market Participant shall provide accurate and factual information and not submit false or misleading information, or omit material information, in any communication with FERC, FERC-approved market monitors, FERC-approved regional transmission organizations, or FERC-approved independent system operators, or jurisdictional transmission providers, unless the Market Participant exercised due diligence to prevent such occurrences." Similarly, section 37.6 states that "Except as provided below in Section 37.6.4 (Review by FERC), all information that is required to be submitted to the CAISO under the CAISO tariff, CAISO Business Practice manuals, or jurisdictional contracts must be submitted in a complete, accurate, and timely manner. Market Participants must comply with requests for information or data by the CAISO authorized under the CAISO Tariff, including timelines specified for submitting Bids and other information."

100. Submitting false or misleading information to an RTO or ISO would, of course, constitute a violation of a Commission regulation.<sup>78</sup> Nevertheless, it does not meet the test of objectively identifiable behavior, and thus a suspected violation should be referred to the Commission, and not be subject to sanction by the CAISO. We will therefore require the CAISO, in addition to revising its proposed definition of Market Violation, to review section 37 and make such adjustments as may be necessary to conform to the requirements for behavior subject to internal sanction.

101. We will also require the CAISO to revise its proposed section 37.8.2 to clarify that it is Market Violations that the DMM is to refer to the Commission, not Rules of Conduct (as modified per the preceding directive). The proposed draft of this section inappropriately conflates Rules of Conduct with Market Violations and leaves it to the DMM to determine whether a given activity is objectively identifiable and thus subject to sanction by the CAISO. However, that determination should be made by the Commission, and only objectively identifiable activity should be included in the tariff as a Rule of Conduct for which a CAISO sanction is permitted.

**d. Mitigation and Operations**

102. In Order No. 719, the Commission expressed concern that the unfettered conduct of mitigation by MMUs makes them subordinate to RTOs and ISOs and raises conflict of

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<sup>78</sup> 18 C.F.R. § 35.41(b)(2009).

interest concerns. However, it also acknowledged that there were a number of advantages, such as expertise and impartiality, in retaining MMU input in the mitigation process. The Commission adopted a balanced approach that allows modified participation by the MMUs in mitigation, while protecting against the conflict of interest and subordination concerns inherent in their unfettered participation. Specifically, the Commission drew a distinction between prospective and retrospective mitigation, and directed that a sole internal or sole external MMU may only conduct retrospective mitigation, not prospective mitigation.<sup>79</sup> However, in the event an RTO or ISO employs a hybrid MMU structure, it may authorize its internal MMU to conduct either or both types of mitigation, but only if it also assigns to its external MMU the responsibility, and gives it adequate tools, to monitor the quality and appropriateness of that mitigation.<sup>80</sup>

103. Order No. 719 also provided that an MMU may be permitted to provide inputs to its respective RTO or ISO to assist the latter in conducting prospective mitigation, including determining reference levels, identifying system constraints, and cost calculations.<sup>81</sup> Further, Order No. 719 provided that purely administrative matters, such as enforcement of late fees, should be conducted by the RTO or ISO, not by the MMU, regardless of the MMU structure.<sup>82</sup>

104. Finally, Order No. 719 directed RTOs and ISOs to specify in their tariffs which functions are to be performed by MMUs, and which by RTOs and ISOs. Also, it required RTOs and ISOs to review their mitigation tariff provisions (whether performed by the MMU or by the RTO or ISO) with a view to making them as non-discretionary as possible, and to reflect any needed changes in their compliance filing.<sup>83</sup>

#### **i. CAISO's Filing**

105. The CAISO avers that current CAISO practice follows the requirements spelled out in Order No. 719 to a large degree. The CAISO states it has made a “conscious decision to maintain its hybrid market monitoring structure comprised of a Department of Market Monitoring and the Market Surveillance Committee”.<sup>84</sup> The CAISO states that

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<sup>79</sup> Order No. 719, FERC Stats. & Regs. ¶ 31,281 at P 375.

<sup>80</sup> *Id.* P 374-375.

<sup>81</sup> *Id.* P 375.

<sup>82</sup> *Id.* P 377.

<sup>83</sup> *Id.* P 379.

<sup>84</sup> CAISO Filing, Transmittal Letter at 55.

this decision is reflected in Appendices O and P of the proposed tariff revisions, which indicate two separate market monitoring bodies and spells out their respective responsibilities.

106. The CAISO explains that the DMM will be prohibited from engaging in tariff administration or prospective mitigation. The CAISO explains that Order No. 719 permits, but does not require, the internal market monitoring unit within a hybrid structure to engage in prospective market mitigation, and since the CAISO's prospective mitigation is largely an automated process not currently administered by the DMM, the CAISO has not chosen to give the DMM that responsibility going forward. The CAISO finally states that the DMM may conduct retrospective mitigation and provide inputs to prospective mitigation.

**ii. Comments and Protests**

107. No adverse comments were filed.

**iii. Commission Determination**

108. The Commission will accept the CAISO's filing as it relates to Order No. 719's directives related to mitigation and operations.

**e. Ethics**

109. In Order No. 719, the Commission adopted minimum ethical standards for MMUs and its employees that RTOs and ISOs must include in their tariffs.<sup>85</sup> Under these standards, the MMU and its employees: (1) must have no material affiliation with any market participant; (2) must not serve as an officer, employee, or partner of a market participant; (3) must have no material financial interest in any market participant or affiliate, with potential exceptions for mutual funds and non-directed investments; (4) must not engage in any market transactions other than the performance of their duties under the tariff; (5) must not be compensated, other than by the Commission-approved RTO or ISO that retains or employs the MMU, for any expert witness testimony or other commercial services, either to the Commission-approved RTO or ISO or to any other party, in connection with any legal or regulatory proceeding or commercial transaction relating to the RTO or ISO or to its markets; (6) may not accept anything of value from a market participant in excess of a *de minimis* amount; and (7) must advise a supervisor in the event they seek employment with a market participant, and must disqualify themselves from participating in any matter that would have an effect on the financial

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<sup>85</sup> 18 C.F.R. § 35.28(g)(3)(vi) (2008).

interest of the market participants. RTOs and ISOs are free to propose more stringent ethics standards in their compliance filings.<sup>86</sup>

110. Order No. 719 clarified that the minimum ethics standards do not prohibit employees of MMUs from performing independent monitoring for entities other than RTOs and ISOs. However, if the employing entity is a market participant in the RTO or ISO for whom the MMU performs market monitoring, the proposed work would entail the same conflict of interest as would any other consulting services. The Commission directed RTOs and ISOs to notify the Commission of such engagements in its compliance filing, and to propose a transition plan for dealing with conflicts in a manner consistent with Order No. 719.<sup>87</sup>

**i. CAISO's Filing**

111. The CAISO states that it has incorporated the seven ethics provisions directly into Appendix O and Appendix P. The CAISO explains that it has also added two provisions. The CAISO states that in section 9.7.1 of both appendices, the CAISO defined the term "seeking employment" with reference to the provision in the Code of Federal Regulations applicable to all employees of the Federal government. The CAISO argues that this provides an objective standard for enforcing the restriction in section 9.7, which limits an employee's activities while seeking employment with a market participant.

112. Additionally, the CAISO notes that section 9.8 of Appendix P provides that the DMM employees will still be subject to the CAISO's generally applicable employee code of conduct. The CAISO states that the ethics provisions of the CAISO's proposed tariff appendices apply only to individual employees and members of the DMM and the MSC. The CAISO asserts that although Order No. 719 states that the "ethics standards apply to the MMU itself as well as to its employees,"<sup>88</sup> the DMM is merely a division of the CAISO, and has no ability to enter into the kinds of commercial relationships that are relevant under the ethics restrictions. The CAISO states that the same holds true for the MSC, which acts solely as an advisory committee to the CAISO Governing Board. The CAISO therefore states that to the extent the Order requires that the ethics provisions apply to the DMM and the MSC themselves, as opposed to individual members, the CAISO requests a waiver of this requirement.

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<sup>86</sup> Order No. 719 at P 384.

<sup>87</sup> *Id.* P 385.

<sup>88</sup> CAISO Filing, Transmittal Letter at 64 (citing Order No. 719 at 384).

**ii. Comments and Protests**

113. No adverse comments were filed.

**iii. Commission Determination**

114. We accept the CAISO's proposed revisions to section 9 of Appendix P and Appendix O, with some modifications. The CAISO must define what a "material affiliation" is, as that term is used in the ethical standard in section 9.1 of Appendix P, as required in Order No. 719.<sup>89</sup> The CAISO must also define what it considers a *de minimis* amount in the ethical standard in section 9.6 of Appendix P.<sup>90</sup> We find the proposed language specifying that the ethical standards in the CAISO's Appendix P will control in the event of a conflict between section 9 of Appendix P and CAISO's Employee Code of Conduct to be helpful in avoiding unnecessary uncertainty. We also will not require the CAISO to make any tariff changes related to the applicability of the ethics provisions to the DMM and MSC themselves as distinct entities. The ethics provisions will apply to all DMM and MSC employees, thus ensuring the entirety of the CAISO and its employees will be subject to ethics provisions. However, because neither the DMM nor the MSC are distinct legal entities with any ability to engage in restricted commercial activity, we find that the CAISO does not need to add any further language to its tariff related to the ethics provisions to the DMM and the MSC. We direct the CAISO to submit a compliance filing within 30 days of the date of issuance of this order consistent with these requirements.

115. In Order No. 719-A, the Commission revisited the issue of potentially conflicting engagements of the MMU with entities that are market participants in the RTO or ISO monitored by the MMU. We make no determination here as to the instant filing's compliance on this issue, and instead will defer the matter to the compliance filing on Order No. 719-A.

**f. Tariff Provisions**

116. Order No. 719 directed RTOs and ISOs to place all of their MMU provisions in one centralized location of their tariffs, and to include, in the introductory portion of that section, a mission statement setting forth the goals to be achieved by the MMU, including the protection of both consumers and market participants by the identification and reporting of market design flaws and market power abuses.<sup>91</sup> Under Order No. 719,

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<sup>89</sup> Order No. 719 at P 380.

<sup>90</sup> *Id.* P 380.

<sup>91</sup> Order No. 719 at P 392.

MMU provisions may be duplicated elsewhere in the tariff if needed for clarity, but must contain a note that the provision in question is also found in the centralized MMU section. Also, Order No. 719 required RTOs and ISOs to include in their tariffs a provision stating that in the event of any inconsistency between provisions in the centralized MMU section and provisions set forth elsewhere, the provisions in the centralized MMU section control.<sup>92</sup>

**i. CAISO's Filing**

117. The CAISO states that, at the time of filing, nearly all of the market monitoring provisions in the CAISO Tariff are located in section 38, Appendix P, Appendix P1, and Appendix P2 of the CAISO Tariff. The CAISO states that section 38 applies to both the DMM and the MSC, Appendices P and P1 apply to the DMM, and Appendix P2 applies to the MSC. The CAISO stated that in centralizing the market monitoring provisions in one section, it faced two questions: (1) where to centralize the market monitoring provisions – in section 38, Appendix P, or some other part of the tariff; and (2) whether to include the DMM and MSC provisions in one section or create separate sections for the DMM and the MSC. The CAISO states that because of its hybrid market monitoring structure, which includes both an internal market monitor, i.e., the DMM, and an external market monitor, i.e., the MSC, Order No. 719 did not provide a complete answer on the latter matter.

118. The CAISO states that because the bulk of the DMM's responsibilities presently are located in Appendix P, the CAISO elected to make Appendix P the centralized section for the DMM provisions. At the same time, the CAISO determined that placing the MSC provisions in a separate section from the DMM would more accurately represent the distinct nature of the DMM and the MSC. Thus, the CAISO chose to centralize the MSC provisions in Appendix O, which previously was vacant. The CAISO notes that section 38 now contains a short explanation of this reorganization and a statement that in the event that there is conflict between either Appendix O or Appendix P and a cross-referenced provision in another part of the CAISO Tariff, the language in the appendices will control.

119. The CAISO states that it is following the Commission's suggested organization. The CAISO claims that, by doing so, the CAISO will better allow the Commission and market participants to compare market monitoring provisions among different ISOs. The CAISO notes that some of the new sections are blank (e.g., sections 2 and 10 of Appendices O and P) because the CAISO decided that for reasons of continuity, provisions that conceivably could have gone in those sections were best placed elsewhere.

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<sup>92</sup> *Id.* P 393.

**ii. Comments and Protests**

120. No adverse comments were filed.

**iii. Commission Determination**

121. The Commission accepts the CAISO's compliance filing as it relates to Order No. 719's directives related to market monitoring tariff provision organization.<sup>93</sup> However, if CAISO chooses to designate the MSC as an external Market Monitoring Unit that is responsible to perform, in whole or in part, one or more of the core functions, we will require CAISO to revise Appendix P and Appendix O to: (1) define clearly the relationship between the internal and external market monitors, (2) delineate clearly the responsibilities of the external Market Monitoring Unit.

**g. Enhanced Information Dissemination**

122. Order No. 719 required each RTO or ISO to include in its tariff a requirement that the MMU prepare an annual state of the market report on market trends and the performance of the wholesale market, as well as less extensive quarterly reports. These reports must be disseminated to Commission staff, staff of interested state commissions, the management and board of the RTO or ISO, and market participants, with the understanding that dissemination may be accomplished by posting on the RTO's or ISO's website.<sup>94</sup> Also, Order No. 719 directed that MMUs be available for regular conference calls, which may be attended by the Commission, state commissions, representatives of the RTO or ISO, and market participants. The information to be provided in the MMU reports and in the conference calls may be developed on a case-by-case basis, but is generally to consist of market data and analyses of the type regularly gathered and prepared by the MMU in the course of its business, subject to appropriate confidentiality restrictions.<sup>95</sup>

123. Additionally, Order No. 719 required RTOs and ISOs to release offer and bid data on a three-month lag. An RTO or ISO may propose a shorter lag time for the release of offer and bid data and provide accompanying justification. If the RTO or ISO demonstrates a potential collusion concern, it may propose a four-month lag period or

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<sup>93</sup> Clarifying the role of the MSC as ordered in the Commission Determination for the "Structure and Tools Section" (Order No. 719 at P 161) should make clear the separate roles of the MSC and the DMM.

<sup>94</sup> Order No. 719 at P 424.

<sup>95</sup> *Id.*

some other mechanism to delay release of the data if it were otherwise to occur in the same season as reflected in the data.<sup>96</sup> The identity of market participants must remain masked, although the RTO or ISO may propose a time period for eventual unmasking. Order No. 719 requires RTOs and ISOs to include in their compliance filings a justification of their policies on the aggregation (or lack of same) of offer and cost data, discussing participant harm, collusion and transparency.<sup>97</sup>

**i. CAISO's Filing**

124. The CAISO states that to comply with this directive, it proposes to revise section 20.4(a) of the CAISO Tariff to indicate that masked offer and bid data shall be released in 90 days. The CAISO explains that such information may include items such as the bids that market participants submit, the bids that are sent to the CAISO's market optimization software following application of prospective market mitigation procedures, and Residual Unit Commitment (RUC) availability bids. The CAISO also explains that it will consider amending section 20.4(a) to cover virtual bids once the CAISO implements the virtual bidding feature into its markets. Regarding Order No. 719's requirement relating to the aggregation of offer and cost data, the CAISO states that it understands this requirement to refer to a practice at other ISOs of providing certain services, e.g., ancillary services, through an offer and price for individual transactions. The CAISO explains that its service model is different in that it procures such services through the market, and thus believes that this requirement is inapplicable to it. The CAISO therefore requests waiver, if necessary, of the requirement.

**ii. Protests and Comments**

125. SoCal Edison supports the CAISO revised tariff language in section 20.4 (a) to release individual bid data 90 days after the trading day with respect to which the bid was submitted. SoCal Edison emphasizes that releasing only the bids submitted by stakeholders is insufficient for understanding market prices and schedules determined by the MRTU optimization software. SoCal Edison states that after the CAISO receives bids submitted by market participants CAISO software has the potential to further modify those bids for such reasons as market mitigation procedures and bids adjusted for Resource Adequacy bidding rules. SoCal Edison additionally states that the revised language allows for the release of RUC availability bids which are also a critical component of understanding market outcomes. SoCal Edison urges the Commission to accept the CAISO compliance language in section 20.4(a) and require the CAISO to

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<sup>96</sup> *Id.*

<sup>97</sup> *Id.*

make necessary system changes to provide market participants all relevant bid information as soon as practical.

**iii. Commission Determination**

126. The Commission accepts the CAISO's Tariff revisions as it relates to the release of individual bid and offer data. The Commission agrees with the CAISO that its service model was not the focus of Order No. 719's requirement regarding the aggregation of offer and cost data; however, the directive to discuss aggregation was not limited to ancillary services. Order No. 719 stated: "The RTO or ISO is to include in its compliance filing a justification of its policy regarding the aggregation or lack thereof of offer data and of cost data..."<sup>98</sup> However, the Commission has recently found that the CAISO's proposed post-MRTU OASIS will provide sufficient data in many categories, thereby providing adequate market transparency. For that reason, the Commission finds it unnecessary for CAISO to discuss the aggregation of data in this filing.<sup>99</sup>

**h. Tailored Requests for Information**

127. In Order No. 719, the Commission stated that MMUs are to entertain state commissions' tailored requests for information regarding general market trends and performance of wholesale market, but not requests for information designed to aid state enforcement actions. The Commission noted that granting or refusing such requests is at the MMU's discretion, based on its agreements with the RTO or ISO and the states, or otherwise based on time and resource availability.<sup>100</sup> Order No. 719 also directs RTOs and ISOs to develop confidentiality provisions to protect commercially sensitive material that may be included in responses to tailored requests for information.<sup>101</sup>

**i. CAISO's Filing**

128. The CAISO states that section 8.1 of Appendix P, and its related sub-parts, reflects CAISO's implementation of the balance the Commission struck between providing state commissions with more useful information and recognizing the need to protect market monitors from being overrun by requests for information from state commissions. The CAISO states that the first sentence of section 8.1 establishes the general rule that the DMM must consider tailored requests from the CPUC for information or data on general

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<sup>98</sup> Order No. 719 at P 424.

<sup>99</sup> *Cal. Indep. Sys. Operator Corp.*, 126 FERC ¶ 61,260 (2009).

<sup>100</sup> *Id.* P 424, 459.

<sup>101</sup> *Id.* P 459.

market trends and the performance of the wholesale markets. The CAISO states that the second sentence of section 8.1, as well as the sub-parts of section 8.1, reflects the limits on the CPUC's right to obtain the information or data. The CAISO notes that the second sentence of section 8.1 allows the DMM to deny a request where complying with it would be unreasonably burdensome or otherwise would interfere with the DMM's ability to carry out its core market monitoring responsibilities.

129. The CAISO claims that section 8.1.1 reflects the non-disclosure approach that the CAISO and the CPUC have reached. The CAISO states that for nearly five years, the CAISO and the CPUC have operated successfully under a confidentiality agreement in which the CPUC promises to treat all information provided by the CAISO pursuant to a subpoena as confidential. Currently, when the CAISO receives a subpoena, the CAISO provides its response upon written confirmation that the information or data provided will be covered under the existing confidentiality agreement. The CAISO claims that this process has worked well for the past five years, and thus the CAISO proposes to extend it to cover information or data provided under section 8.1.1. The CAISO states that section 8.1.3 bars the DMM from complying with a request that "is designed to aid an enforcement action by an instrumentality or political subdivision of the State of California against a specific company." The CAISO states that, in developing this part of the proposed tariff language, it was concerned that if the limitation referred only to requests designed to aid a CPUC enforcement action, the CPUC could seek information and pass it along to another state agency for its enforcement action. Because Order No. 719 refers generally to "state enforcement actions," rather than "state utility commission enforcement actions," the proposed scope of section 8.1.3 should better fulfill the Commission's intent.

130. The CAISO also notes that during the stakeholder feedback process, the CPUC expressed concern that section 8.1.2 did not guarantee that the DMM would provide basic information needed to understand the raw data, such as the definitions of terms and the sources of data. The CAISO states that the DMM intends to provide such support unless it is unreasonably burdensome or is otherwise restricted by section 8.1. The CAISO explains, however, that because the DMM cannot guarantee that it will be able to provide the desired support in all circumstances, the CAISO did not incorporate a requirement to provide the support in section 8.1.2.

**ii. Comments and Protests**

131. No adverse comments were filed.

**iii. Commission Determination**

132. We will generally accept the CAISO filing relating to information sharing; however, we note that one of the goals in Order 719 is providing state commissions with more useful information and recognizing the need to protect market monitors from being

overrun by requests for information from state commissions. The CAISO proposal is tailored for information sharing between the CAISO and the CPUC. We direct the CAISO to revise section 8 of appendix P to also include a provision that addresses information sharing with other state commissions.

**i. Commission Referrals**

133. In Order No. 719, the Commission also adopted protocols for referrals by MMUs to the Commission of suspected market violations and perceived market design flaws to be included in RTO and ISO tariffs. These are set forth at 18 C.F.R. § 35.28(g)(iv)(v). By Commission rule, all information and documents obtained during the course of an investigation are non-public, and may not be released except to the extent the Commission directs or authorize in a given instance, unless the material is already made public during an adjudicatory proceeding or disclosure is required by the Freedom of Information Act.<sup>102</sup>

**i. CAISO's Filing**

134. The CAISO states that section 12 of Appendix P in the MRTU Tariff “adopts virtually verbatim”<sup>103</sup> from Order No. 719 the regulations governing a market monitoring unit’s obligation to refer perceived market rule flaws to the Commission. The CAISO states that these referrals are also addressed in section 5.1.7, which provides that the CAISO’s obligation to inform the Commission of disagreement between the DMM and the CAISO about identification of market flaws shall be carried out as part of a referral under section 12 of the MRTU Tariff.

135. With respect to suspected violations, the CAISO states that it will only handle objectively determinable violations. If DMM believes a market violation has occurred it will make a referral to the Commission according to Protocols in section 11 of Appendix P.

**ii. Commission Determination**

136. The Commission accepts the CAISO’s compliance filing as it relates to Order No. 719’s directives related to Commission referrals. However, as section 11 of Appendix P refers to referrals of Market Violations, it is critical that the CAISO’s definition of Market Violation conforms to the definition of Market Violation set forth in

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<sup>102</sup> *Id.* P 465 (*citing* 18 C.F.R. § 1b.9).

<sup>103</sup> CAISO Filing, Transmittal Letter at 61.

the Commission's regulations.<sup>104</sup> If the CAISO chooses to designate the MSC as an external Market Monitor Unit, then we will require the CAISO to revise Appendix O to either include language giving similar Commission referral powers to its external market monitor or to state that only the DMM is the entity assigned with the responsibility to make referrals.

The Commission orders:

(A) CAISO's compliance filing is hereby accepted, as modified, effective April 28, 2009, as discussed in the body of this order.

(B) CAISO is hereby directed to submit a compliance filing, within 30 days of the date of this order, as discussed in the body of this order.

(C) CAISO is hereby directed to submit an information report, within six months of the date of this order, as discussed in the body of this order.

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.

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<sup>104</sup> As we stated in Paragraph 97, *supra*: "We will require the CAISO to conform its proposed definition of Market Violation to that set forth in our regulations. The protocols for the referral of suspected violations to the Commission, which the CAISO includes in its tariff, use this term, and must therefore be consistent with the Commission's definition."

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