UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	**)** **)**	**Docket Nos. ER08-1178-000 and EL08-88-000**

COMMENTS OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION REGARDING TECHNICAL CONFERENCE

Pursuant to the procedures established at the November 6, 2008 Technical Conference convened by the Staff of the Federal Energy Regulatory Commission ("Commission"), the California Independent System Operator Corporation ("CAISO")[1] hereby submits its Comments regarding the matters discussed at the Technical Conference in the captioned proceeding.

The Technical Conference addressed issues raised by the CAISO's Exceptional Dispatch proposal that was filed in the captioned dockets on June 27, 2008 ("June 27 Filing"). Specifically, the Technical Conference addressed the following issues: (1) the CAISO Exceptional Dispatch pricing proposal and the Commission's alternative proposal; (2) the frequency of Exceptional Dispatch; modeling, and software limitations; and (3) the scope of the CAISO's Exceptional Dispatch Bid mitigation proposal.

The instant Comments set forth the CAISO's positions on these issues. In addition, the CAISO discusses its authority to issue Exceptional Dispatches in the event of a Market Disruption and explains how the CAISO's proposal to

[1] Capitalized terms not otherwise defined herein are defined in Appendix A to the CAISO's Market Redesign and Technology ("MRTU") Tariff.

utilize a $24/MWh bid adder approach proposed for the first four months of MRTU, can be utilized with the revised Exceptional Dispatch pricing proposal.

Significantly, the CAISO's Comments present a revised Exceptional Dispatch pricing proposal that takes into account statements contained in the Commission's October 16, 2008 Order on the CAISO's proposal,[2] and Commission Staff comments and parties' comments at the Technical Conference. The CAISO submits that its revised Exceptional Dispatch pricing proposal is just and reasonable and consistent with the principles set forth in the October 16 Order. As such, the Commission should approve it expeditiously so that it can be implemented simultaneously with the implementation of MRTU.

I. THE CAISO'S REVISED EXCEPTIONAL DISPATCH PRICING PROPOSAL

A. Summary of the CAISO's Filed Exceptional Dispatch Pricing Proposal

In its Exceptional Dispatch proposal submitted in the June 27 Filing, the CAISO proposed to mitigate bids on behalf of resources that are issued Exceptional Dispatches for the following reasons: (1) to address reliability requirements related to non-competitive transmission constraints; (2) to ramp units up from minimum operating levels to minimum dispatchable levels to protect against contingencies that are not directly incorporated or sufficiently met by the MRTU software; or (3) to address other special unit-specific operating or environmental constraints not incorporated into the MRTU model. The CAISO proposed to mitigate all resources issued these types of Exceptional Dispatches

[2] *California Independent System Operator Corp.*, 125 FERC ¶ 61,055 (2008) ("October 16 Order").

so that they receive the higher of (1) their Default Energy Bid, or (2) the Locational Marginal Price ("LMP"). Under the proposed mitigation, resources with capacity contracts, *i.e.*, resource adequacy ("RA") resources, Reliability Must-Run ("RMR:") resources and Interim Capacity Procurement Mechanism ("ICPM") resources, would not earn any additional capacity-related revenues through Exceptional Dispatch but would be subject to bid mitigation. However, non-RA resources may receive no guaranteed fixed cost recovery for providing capacity through Exceptional Dispatch.[3] The CAISO already provides several market-based mechanisms to provide such resources with contributions to fixed cost recovery, including the ability to bid in to the Reliability Unit Commitment ("RUC") market. Nevertheless, the CAISO and stakeholders agreed that at least some cases of Exceptional Dispatch warranted additional such mechanisms, in particular if Bids are mitigated and also because LMPs will likely be suppressed when Exceptional Dispatch instructions are issued, Thus, the CAISO proposed a general pricing rule that non-RA resources that receive Exceptional Dispatch instructions and were subject to Bid mitigation would be eligible to receive a supplemental revenue payment to provide a contribution to fixed cost recovery. The mechanism for accruing those revenues was to pay such resources the higher of (1) the LMP, or (2) their actual bid. The CAISO proposed to cap the amount of the supplemental revenue payment that a non-RA resource can accrue in a 30-day period at $41/kW-year, *i.e.*, the same as a capacity payment

[3] For ease of reference, in these Comments the phrase "non-RA resource" or "non-RA unit" is used to mean a resource or unit that is non-RA, non-RMR, and non-ICPM.

associated with an ICPM designation.[4] When the cap is reached, the non-RA resource would be subject to Bid mitigation in the same fashion as other resources.

B. The October 16 Order

In its October 16 Order, the Commission expressed concern that the proposed Exceptional Dispatch pricing proposal failed to provide non-resource adequacy resources with sufficient compensation for the reliability services they provide under Exceptional Dispatch. The Commission stated that non-resource adequacy resources that provide reliability services should be paid in a similar manner—and be subject to the similar obligations—as resource adequacy resources, which receive fixed cost recovery. The Commission expressed concern that some non-resource adequacy resources may be unable to recover their fixed costs in certain circumstances because a non-resource adequacy resource that has no bid in the market will be paid the higher of its Default Energy Bid or the LMP. The Commission concluded that, given the intertwined nature of Exceptional Dispatch and the ICPM and the Commission's goal of encouraging participation in the RA program and the voluntary nature of the ICPM, a reasonable and efficient solution would be to provide non-resource adequacy resources with an offer of an ICPM designation upon receipt of their first Exceptional Dispatch instruction.

Accordingly, the Commission proposed the following remedy to address its concerns regarding the pricing of Exceptional Dispatches: (1) provide non-

[4] For the first four months, supplemental revenues are calculated based on the higher of (1) the LMP minus the Default Energy Bid or (2) the Default Energy Bid plus $24/MWh minus the Default Energy Bid.

resource adequacy resources with the offer of an ICPM designation upon receiving their first Exceptional Dispatch; and (2) cap the amount a non-resource adequacy resource may receive in a 30-day period under the ICPM or Exceptional Dispatch, or both mechanisms together, at the ICPM price of $41/kW-year. The Commission stated that this approach should ensure that non-RA resources are appropriately compensated for their backstop capacity services, regardless of which tariff mechanism authorized their service. The Commission also proposed this price so as not to undercut the voluntary ICPM program. Further, the Commission stated that requiring the CAISO to incorporate a provision that limits the amount of revenue a non-RA resource receives under Exceptional Dispatch or ICPM or both to $41/kW-year would negate the possibility of double payments under the CAISO's proposed market design.[5] The Commission sought comments on its proposed remedy at the Technical Conference.

C. The CAISO's Revised Exceptional Dispatch Pricing Proposal

Based on the Commission's statements in the October 16 Order and input received at the Technical Conference, the CAISO is proposing to revise its Exceptional Dispatch Pricing Proposal. The elements of the revised pricing proposal are as follows:

(1) Eligible resources would have two options to receive compensation when they are Exceptionally Dispatched by the CAISO:

[5] The Commission noted that, under the as-filed proposal, a non-resource adequacy resource that is likely to be Exceptionally Dispatched for an extended period of time could decline an ICPM designation, earn supplemental revenues equal to the cap in as little as eight hours, and then accept the still outstanding ICPM designation offer, effectively being paid twice.

(a) An ICPM designation for 30 days, either for a partial or full unit depending on the amount of capacity subject to Exceptional Dispatch within the 30-day period, pursuant to the compensation rules discussed below which would obligate the resource in the same manner as a designation triggered under the tariff rules for ICPM[6]; or

(b) A bid-based supplemental revenue payment (referred to hereinafter as "supplemental revenues"), calculated according to the pricing rules contained in the CAISO's filed pricing proposal (including the supplemental revenue cap).[7]

The CAISO is also proposing a new "double payment" rule to prevent the double payment scenario identified by the Commission in the October 16 Order.

(2) To avoid adverse market incentives and minimize the administrative burden, eligible resources (*i.e.,* non-RA and partial RA units) would be required to indicate by the first day of each calendar month which method they prefer for Exceptional Dispatch compensation.[8] If no election is made, the resource will be

[6] See MRTU Tariff, Section 43, *et seq.*

[7] As discussed below, for the first four months of MRTU, the CAISO is proposing the $24/MWh bid adder approach for determining supplemental revenues.

[8] As discussed at the Technical Conference, most Exceptional Dispatches are not likely to occur in a time-frame that will allow simultaneous acceptance of an ICPM designation as many Exceptional Dispatches will occur in real-time. Thus, a resource's acceptance of an ICPM designation will have to take place either before the Exceptional Dispatch (*ex ante*) or after the Exceptional Dispatch (*ex post*). For the reasons discussed below, an *ex ante* approach is preferable.

treated as having selected the ICPM designation option. Once that election has been made, the following rules would apply:

(a) If a resource elects an ICPM designation for a particular month, once an Exceptional Dispatch is triggered, the resource would not be eligible to choose the supplemental revenues option for any subsequent Exceptional Dispatches during the 30-day period. The resource would have an ICPM designation for the entirety of the 30-day period even if that period extends into the next calendar month;

(b) If a resource elects supplemental revenues for a particular month, once an Exceptional Dispatch is triggered, the resource will not be eligible to choose the ICPM option for any additional Exceptional Dispatches during the subsequent 30 days.

For example, if an Exceptional Dispatch occurs on June 15, and the resource selected the supplemental revenue approach for June, the supplemental revenue approach would apply for the period June 15-July 15. The resource would not, for example, be able to select the supplemental revenue approach for the period June 15-30 and an ICPM designation for the period July 1-15. However, under the above example, if a second Exceptional Dispatch occurs on July 20, and the resource selected the ICPM option for the month of

July, the resource would receive an ICPM designation effective July 20 and remaining in effect for the next 30-day period. However, the resource can accept an ICPM designation if the CAISO offers it such a designation under the ICPM tariff provisions already accepted by the Commission during the 30-day period.[9] Under these circumstances, the "double payment" rule would apply, and any supplemental revenues earned by the resource during the 30-day period would be subtracted from the applicable ICPM payment to ensure that, during the 30-day period, the resource does not earn more than it otherwise would from an ICPM designation.

(3) The following types of Exceptional Dispatches would trigger a unit's eligibility for an ICPM designation (or, if elected, supplemental revenue compensation):

(a) Any Exceptional Dispatch **commitment** of a non-RA unit would result in the unit being eligible for an ICPM designation. The ICPM designation would be for the **commitment** amount, generally the unit's PMin. However, a resource that has elected supplemental revenues would not accrue any such revenues for a commitment to PMin, because supplemental revenues require a dispatch for incremental energy. Any resource committed through Exceptional Dispatch would also recover its Start-Up and Minimum Load Costs.

[9] *See* MRTU Tariff, Section 43, *et seq.*

Under MRTU, resources can receive up to 200% of their actual Start-Up and Minimum Load Costs, if located in a local capacity requirement area, or 400% if the resource is not located in a local capacity requirement area.[10]

(b) Any Exceptional Dispatch for incremental energy (*i.e.*, a **dispatch** of energy above PMin) that moves a non-RA resource (with no partial capacity contracts or designations) beyond its Self-Schedule amount or market-based commitment/dispatch level is eligible for either an ICPM designation or supplemental revenue compensation for the incremental amount that is Exceptionally Dispatched, minus any Self-Schedule or market-based commitment or dispatch level. The ICPM designation will be the higher of PMin or the quantity under Exceptional Dispatch.

For example, assume a non-RA unit with a PMin of 50 MW that has a Self-Schedule for 50 MW and a market bid for 25 MW; further assume that the CAISO directs the unit to move to 100 MW through an Exceptional Dispatch. Under this example, the unit would be eligible to receive an ICPM designation for 25 MW. However, because the CAISO cannot access a unit's capacity below PMin, the CAISO proposes to adopt a rule for these types of circumstances whereby the quantity eligible for an ICPM

[10] See MRTU Tariff, Sections 30.4 and 39.6.1.6.

designation will be the higher of a unit's PMin or the Exceptional Dispatch quantity. Hence, the ICPM designation in this example would be for 50 MW to PMin (and would establish an obligation to Bid the resource's PMin into the Day-Ahead Market).

(c) Any Exceptional Dispatch for incremental energy (*i.e.*, a **dispatch** of energy above PMin) that moves a partial RA or partial ICPM resource to a point that is beyond its Self-Schedule amount or market-based commitment or dispatch level, and beyond its RA or ICPM capacity amount, is eligible for an ICPM designation to the extent the Exceptionally Dispatched incremental quantity exceeds the RA/ICPM capacity amount minus the Self-Schedule or market-based commitment/dispatch Level. If, however, a unit were to elect to receive supplemental revenues under this scenario, it would be paid according to the submitted Bid. The CAISO would not distinguish between partial and non-RA capacity, consistent with the CAISO's original pricing proposal,

For example, assume a partial RA unit with RA capacity of 60 MW, a PMin of 50 MW, and a Self-Schedule for 55 MW and an accepted market bid for 25 MW and further assume that the CAISO directs the unit to move to 100 MW. Under this example, the unit would be eligible to receive an ICPM designation for 20 MW of capacity.

Because the unit is already an RA unit, there is no need to apply the aforementioned rule that the ICPM quantity must be the greater of PMin or the Exceptional Dispatch quantity. There should not be any double capacity payments for capacity that is already designated as ICPM or under an RA contract. In the above example, the PMin capacity is already under an RA contract and it should not also be eligible for an ICPM designation.[11]

(d) Resources that have been subject to an Exceptional Dispatch ICPM designation in a 30-day period in which their RA contract or otherwise obtained ICPM designation decreases in quantity may have their ICPM designation quantity changed accordingly for the remainder of the 30-day period. For example, with regard to the example described in (3)(c), above, if the partial RA resource becomes a non-RA resource in day 15 of the 30-day period, the ICPM designation would have to be adjusted to reflect the minimum MW associated with PMin for that resource. Hence, the 30 MW ICPM designation would have to be raised to a minimum of 50 MW to reflect PMin.

(4) The following Exceptional Dispatches are *not* eligible for ICPM designations or supplemental revenue payments:

[11] While the CAISO has spent considerable time considering different examples of how these rules will operate in practice, the CAISO has not considered every facet of implementation.

(a) The Exceptional Dispatch is for decommitment or decremental energy. There is no reasonable basis to support providing additional compensation to resources under these circumstances. There was general agreement at the Technical Conference that these types of Exceptional Dispatches do not warrant additional payments to resources. Moreover, the CAISO has not proposed to mitigate suppliers in these circumstances.

(b) The CAISO believes that there should be a category for Exceptional Dispatches that are not eligible for either an ICPM designation or supplemental revenues but would still be subject to mitigation. This would be a modification to the CAISO's original proposed Exceptional Dispatch payment rule which allowed resources to collect supplemental revenues whenever their bids would be subject to mitigation. At a high level, the principle is that, when the CAISO issues Exceptional Dispatches in circumstances where the resource has to be moved for reasons unrelated to the CAISO's needs, it should not be obligated to pay for the capacity. As discussed at the Technical Conference, the CAISO will have to utilize Exceptional Dispatch in Real-Time to move a unit through its Forbidden Operating Region and, at times, to hold a unit either below or above its Forbidden Operating Region. As also discussed at the Technical Conference, the Forbidden Operating Region

functionality will be in place in the Day-Ahead Market and therefore will be reflected in the Day-Ahead Schedule. The functionality will not be in place in the Real-Time Market. Accordingly, operators will have to issue Exceptional Dispatches to move, and possibly hold, a resource either above or below a Forbidden Operating Region when the Real-Time Market software is trying to move the unit to a point within the resource's Forbidden Operating Region. The CAISO believes that such Exceptional Dispatches should be mitigated, as the resource owner would be able to submit high Bids during subsequent periods knowing that the resource is being held at a certain level, for example. The CAISO does not believe that the resource should be eligible for an ICPM designation or to receive supplemental revenues in this circumstance. The CAISO also believes there may be other instances where the exception should apply for similar reasons. However, due to time constraints in preparation of these comments, the CAISO was unable to conduct a complete analysis of this issue. Accordingly, the CAISO reserves its right to offer additional comments on this topic.

(5) If a resource with an existing ICPM designation at PMin (or a partial RA contract at PMin) is subsequently Exceptionally Dispatched by CAISO above PMin, whether on the same day or on a subsequent day during the 30-day period, the CAISO will calculate the MW corresponding to that Exceptional

Dispatch and provide an incremental ICPM designation for that amount. If the unit is Exceptionally Dispatched multiple times during the 30-day period, the "incremental" ICPM designation will be for largest quantity for which the resource was Exceptionally Dispatched.

A simple example can demonstrate the CAISO's proposal: A resource is committed on Day 1 and dispatched to its minimum operating level (PMin) of 50 MW. It is then eligible for an ICPM designation to PMin. On Day 2, that same resource is committed again and given an Exceptional Dispatch instruction to increase its output by 100 MW. It will now be eligible for an ICPM designation of 150 MW. If on Day 3 the unit is Exceptionally Dispatched to an output level of 175 MW, the unit would be eligible for an ICPM designation of 175 MW. To the extent a unit has accepted market bids "sandwiched" between RA/ICPM Commitments and/or Exceptional Dispatches, those accepted bid quantities or Self-Schedules would not count for toward and ICPM designation.

Thus, for settlement purposes, the CAISO will consider the final incremental designation in each calendar month during the 30-day period as the monthly settlement quantity. Thus, in the example above, the ICPM monthly payment if all three days fall into one month will be for 175 MW if there are no further incremental ICPM designations. However, if days 1 and 2 are in one calendar month and day 3 in the next month, the payment in month 1 will be based on 150 MW while the payment in month 2 will be based on the 175 MW. In addition, the payments will be prorated. If the first Exceptional Dispatch occurs on the 15th day of the month, the ICPM payments will be prorated.

(6) A special minimum designation rule is needed for an Exceptional Dispatch for incremental energy that moves a non-RA resource beyond its market-based or self-scheduled commitment or dispatch level. The possibility exists that the incremental energy Exceptional Dispatch amount may not be greater than the resource's PMin, and thus would provide no operational value to the CAISO. In this instance, CAISO proposes that under these circumstances the unit would be eligible for a designation to its PMin. For example, a non-RA resource has a minimum operating level (PMin) of 50 MW. It is self-scheduled for 270 MW and CAISO issues it an Exceptional Dispatch instruction to increase its output by 30 MW. Since the incremental dispatch of 30 MW is lower than its PMin, the CAISO will offer it an ICPM designation to PMin.

(7) A rule is also need for resources with RA capacity less than PMin. The CAISO believes that any RA resource that has entered into a contract to provide RA capacity less than its PMin has an obligation to make that RA capacity available to the CAISO and, therefore, must offer its PMin to the CAISO and should not be eligible for an ICPM for the difference between PMin and its contracted RA capacity less than PMin.

(8) As indicated above, a rule is needed to prevent any double payment to resources during a 30-day period. Consistent with the principle set forth in the October 16 Order, in any 30-day period, a resource committed through

Exceptional Dispatch would not be permitted to earn, through the sum of ICPM capacity payments and supplemental revenues, payments greater than the applicable monthly ICPM payment (which shall be based on the higher of $41/kW-year or a resource's Commission-approved ICPM rate above $41/kW-year, whichever is applicable). This means that a resource that elects and receives supplemental revenues upon the first Exceptional Dispatch and is then offered an ICPM designation due to a Significant Event on a subsequent day in the 30-day period cannot earn more than the applicable monthly ICPM payment for the 30-day period triggered by the Exceptional Dispatch. Under these circumstances, the CAISO would subtract any applicable supplemental revenues from the ICPM payment.

D. The CAISO's Revised Pricing Proposal Is Just And Reasonable And Consistent With The Principles Set Forth In The October 16 Order

The revised Exceptional Dispatch pricing proposal satisfies the principles enunciated in the October 16 Order. First and foremost, by giving Exceptionally Dispatched units the option to earn a monthly ICPM capacity payment, the revised proposal satisfies the Commission's overarching objective that non-resource adequacy resources that provide reliability services be paid in a similar manner – and be subject to similar obligations as resource adequacy resources.

Second, the revised proposal respects the voluntary nature of the ICPM program. Resources that are Exceptionally Dispatched can choose to earn supplemental revenues during the 30-day period following an Exceptional

Dispatch or they can opt for a 30-day ICPM designation. They are not required to accept an ICPM designation.

Third, the revised pricing proposal recognizes the intertwined nature of Exceptional Dispatch and ICPM and the need to encourage participation in the RA program. In particular, the revised proposal allows for partial-unit ICPM designations in instances where the CAISO does not need the entire capacity of a unit to meet reliability needs. This is consistent with the ICPM and RA programs, both of which allow the procurement of partial units if the full output of the unit is not needed for the CAISO to meet reliability needs (ICPM) or a Load Serving Entity ("LSE") to satisfy its RA obligations (RA). The Commission has previously recognized that the procurement of partial units under the ICPM is consistent with procurement under the RA program.[12] By allowing resources to be partially designated as ICPM resources, the revised Exceptional Dispatch proposal accomplishes the Commission's comparable treatment objective. On the other hand, requiring full-unit ICPM designations upon issuance of an Exceptional Dispatch instruction – even if the CAISO does not need or use the entire capacity of the unit – would result in resources that are Exceptionally Dispatched being treated more favorably than they otherwise would be under RA or ICPM. For example, a Significant Event could occur that only requires the CAISO to commit a non-RA resource to PMin. Under the ICPM program the CAISO could offer a resource a partial-unit designation to PMin, which the resource could choose to accept or decline. If the CAISO subsequently had to Exceptionally Dispatch the unit by committing it to PMin, it should not be required

[12] *California Independent System Operator Corp.*, 125 FERC ¶ 61,053, at P 94 (2008).

to designate the entire capacity of the unit. Not only would such a result undermine the ICPM program, it would be inconsistent with the goal that Exceptionally Dispatched resources be treated in a comparable manner to RA and ICPM resources. A resource should not be able to "get a better deal" from Exceptional Dispatch than it would from accepting an ICPM designation. Further, requiring full-unit designations could result in unnecessary over-procurement if the entire capacity of the unit is not needed to meet reliability needs, address a Significant Event, or cure an RA deficiency. The CAISO submits that its revised pricing proposal is just and reasonable because the CAISO will make a monthly ICPM payment based on the highest quantity for which a unit was Exceptionally Dispatched during the first calendar month within the 30-day period. Moreover, the CAISO will make the monthly ICPM payment in the second month of a 30-day period based on the highest quantify for which a unit was Exceptionally Dispatched during the 30-day period even when the highest quantity occurred during the first month.

Fourth, the CAISO's revised proposal eliminates the possibility of "double payment" that existed under the CAISO's filed proposal. In that regard, the CAISO will cap the amount a non-resource adequacy resource may receive in a 30-day period under ICPM and Exceptional Dispatch to the higher of $41/kW-year or a unit's (higher) cost-justified, Commission-approved ICPM capacity payment, whichever is applicable.

Fifth, the CAISO's proposal allows a partial RA (or partial ICPM) unit to receive an ICPM designation for capacity in excess of its RA capacity (or ICPM

capacity) to the extent the CAISO Exceptionally Dispatches capacity above the RA (or ICPM) amount, and such capacity was not self-scheduled or bid-in by the resource. Thus, the revised proposal addresses any concerns about partial RA units being eligible for capacity payments for their non-RA capacity.

E. The CAISO's Department of Market Monitoring Alternative Proposal

The CAISO believes the ICPM designation proposal discussed above fairly responds to the concerns articulated by the Commission in its October 16 Order as well as concerns raised by Commission Staff at the Technical Conference and should go a long way towards addressing concerns raised by other parties attending the Technical Conference. However, the CAISO's Department of Market Monitoring ("DMM") has raised concerns about any proposal, including the proposal discussed above, that would create incentives to withhold Bids. The DMM is concerned that this rule will create an incentive for resources to withhold capacity in anticipation of an Exceptional Dispatch or to force the CAISO to issue an Exceptional Dispatch that will provide the resource with the option of an ICPM designation or of receiving supplemental revenues. DMM believes that it would be more appropriate to require units to submit a Bid in order to be eligible for an ICPM designation or supplemental revenues, because such a requirement would encourage a resource to continue to participate in the market while ensuring that if the resource chooses otherwise, it will still be compensated at the higher of the Default Energy Bid price or the Resource-Specific Settlement Interval LMP, per the CAISO's Exceptional Dispatch mitigation proposal.

The CAISO recognizes that based on the Commission's October 16 Order and comments from Commission Staff, the Commission may be unwilling to adopt a strict requirement that a resource submit a Bid into the applicable market in order to be eligible to receive an ICPM designation or supplemental revenues. As a further alternative and as a compromise between the CAISO's proposal described above and DMM's preferred approach, the CAISO could offer an ICPM designation (or supplemental revenues) in the event the CAISO used Exceptional Dispatch to commit a resource regardless of whether the resource has submitted a Bid, but make any incremental designations contingent upon the resource submitting Bids into the CAISO's markets.

II. DISCUSSION OF OTHER ISSUES RAISED AT THE TECHNICAL CONFERENCE

A. The CAISO Acknowledges that It May Need to Employ Exceptional Dispatch More Frequently than Previously Expected

The CAISO's goal under MRTU is for Exceptional Dispatch to be a rare and infrequent event. As the CAISO explained in the June 27 Filing, however, as the MRTU software has been developed, and in light of experience gained with MRTU market simulations, the CAISO has become aware that it will likely need to utilize Exceptional Dispatches more often during the initial stages of MRTU operations than previously anticipated.

It is important, however, to place this assessment in the proper context. Although the CAISO anticipates that it will likely have to issue more Exceptional Dispatches than previously expected, it nevertheless expects that the total number of such Exceptional Dispatches will still constitute only a very small

percentage of the total number of dispatches under MRTU. Specifically, the CAISO anticipates that Exceptional Dispatches will amount to one percent or less of the several thousand automated dispatches that will occur daily under MRTU. Significantly, the CAISO expects that most Exceptional Dispatches under MRTU will be not for the purpose of committing resources – equivalent to today's must-offer waiver denials – but rather for reasons akin to the reasons that the CAISO issues Out-of-Sequence ("OOS") dispatches[13] under its current market design – that is, in order to manage energy output for a variety of reasons in Real-Time. Specific reasons under the current market design and under MRTU include managing Forbidden Operating Regions and other ramping and resource-specific constraints, as well as to manage unscheduled loop flows.[14]

Moreover, because there is usually sufficient capacity available from local RA resources to handle local area constraints, only a small portion of those Exceptional Dispatches that do involve resource commitments is likely to involve non-RA resources. Very few non-RA resources have been committed under the existing must-offer process in recent months, and the CAISO expects that this trend will continue under MRTU. The CAISO notes, however, that it may see increased commitments of non-RA resources in "shoulder" months, *i.e.*, those months on either side of the peak season, due to higher levels of scheduled

[13] As the CAISO has explained, Exceptional Dispatches are fundamentally no different from the Out-of-Market ("OOM") and OOS dispatches that the CAISO has the authority to perform under its current market design. *See California Independent System Operator Corp.*, 116 FERC ¶ 61,274, at P 254 (2006).

[14] See also the discussion regarding Forbidden Operating Regions in Section II.D.2.b, below.

transmission maintenance outages during the months and a lesser quantity of available RA capacity.

Finally, the CAISO has committed to exploring a number of potential improvements to MRTU functionality after go-live, some of which should reduce the need for Exceptional Dispatches. For instance, the CAISO has already initiated a stakeholder process to develop the capability to model multi-stage generating units. Once developed and implemented, this software enhancement will provide improved performance superior to the Forbidden Operating Region functionality originally designed and now deferred, and will also improve the modeling of combined cycle units and other resource-specific operating constraints. The CAISO anticipates that this new functionality alone will dramatically reduce the number of Exceptional Dispatches.

In addition, as discussed below, the CAISO is exploring options for future enhancements to the Full Network Model to incorporate modeling of such constraints as the Pacific DC Intertie.[15] The CAISO has also proposed to post monthly reports on the CAISO Website, 30 days after the end of each month, indicating the reasons for the Exceptional Dispatches.[16] The CAISO will use this information to direct allocation of resources to improved modeling in areas that are most likely to reduce reliance on Exceptional Dispatch.

[15] See also the discussion below regarding the Pacific DC Intertie.

[16] In its September 21, 2006, order on MRTU, the Commission required posting of information on Exceptional Dispatch. *California Independent System Operator Corp.*, 116 FERC ¶ 61,274, at P 267 (2006).

B. The CAISO's Authority to Issue Exceptional Dispatches to Avoid Market Disruptions Will Reduce the Need for More Significant Interventions[17]

Under Section 7.7.15 of the MRTU Tariff, the CAISO can issue an Exceptional Dispatch in the event of, or to prevent or minimize, a Market Disruption. A Market Disruption is defined as "[a]n action or event that causes a failure of the normal operation of any of the CAISO Markets." Thus, the CAISO cannot use Exception Dispatch for this purpose as long as the CAISO Market at issue is functioning properly. The intended use of Exceptional Dispatch in connection with this authority is to resolve situations in which the MRTU software is unable to reach a solution through its automated processes. In such situations, the use of Exceptional Dispatch is appropriate because it allows the CAISO to take limited and targeted manual action in order to avoid results that would likely involve serious harm to Market Participants, and would almost certainly require a much greater level of manual intervention, including extensive use of Exceptional Dispatch, in order to address the ensuing market failure.

C. The CAISO's Modeling-Related Limitations Are Reasonable

The CAISO's Full Network Model and MRTU software represent a significant advance compared to today's market design. No market model, however, can be perfect and no market model – no matter how accurate – can account for all possible contingencies.

The most common modeling limitation will involve transmission outages – both anticipated and unanticipated. Even with planned outages, the CAISO may

[17] At the Technical Conference, counsel for the California Department of Water Resources requested an explanation of the CAISO's authority to issue Exceptional Dispatches to avoid a Market Disruption

not be able to adjust the Full Network Model to reflect the de-rate. As discussed at the Technical Conference, there may not be enough time to incorporate the configuration in the production model, because of the timing of the model update process, the timing of the outage, or the need to perform studies before certain outages can be modeled. In addition, some outages cause capacity requirements that, as discussed below, are not modeled. In the case of emergency outages, the same considerations apply generally, but in addition there is no advance notice and thus even less time to incorporate an alternative configuration. Finally, some outages – planned or unplanned – are of such short duration that it is impracticable to model them.

As discussed at the Technical Conference, some other conditions are simply not modeled in the Full Network Model and MRTU software and, therefore, may require manual intervention. One of these is voltage support on the CAISO Controlled Grid. As the Commission explicitly recognized "the CAISO uses market dispatch software that relies on a DC model of the grid, which does not include reactive power constraints. As a result, the CAISO may need to rely on Exceptional Dispatches to adjust the amount of voltage support on the grid in real time."[18] The CAISO may also need to issue Exceptional Dispatches to commit resources in defined local areas to ensure adequate voltage support and to ensure that the MRTU software is able to reach a solution. The CAISO understands that voltage support requirements are generally not modeled in the systems of other Independent System Operators ("ISOs") and Regional Transmission Organizations ("RTOs"). The use of a manual system such as

[18] *California Independent System Operator Corp.*, 119 FERC ¶ 61,313, at P 444 (2007).

Exceptional Dispatch to address this shared modeling limitation is necessary to preserve just and reasonable market conditions.

Another condition that is not modeled is capacity-based constraints, such as requirements for capacity in the area south of Path 26 (Southern California) to protect that area against loss of the Pacific DC Intertie.[19] To be more specific, because the Pacific DC Intertie is a direct current line, the current MRTU software lacks the capability automatically to dispatch resources to address a contingency on this line.

The Pacific DC Intertie, being a direct current line, is modeled under MRTU as a single, radial line into which injections of power are made into the CAISO Controlled Grid directly from NOB to Sylmar, without the possibility of any parallel flows on other lines. By contrast, alternating current lines that are internal to the CAISO are modeled under MRTU in a way that reflects the fact that they are part of an interconnected network of transmission lines on which parallel flows occur. The current MRTU software performs Security Constrained Unit Commitment ("SCUC") and Security Constrained Economic Dispatch ("SCED"), which ensure that parallel transmission lines do not exceed their emergency ratings in the event of transmission contingencies. In this manner, the current MRTU software is able to use automated dispatch to address

[19] The Pacific DC Intertie (also known as Path 65) is a high-voltage direct current transmission line that has a capacity of approximately 3100 MW and is used to transmit a significant amount of power between the Pacific Northwest and Southern California. Specifically, power is injected at the Celico Converter Station in northern Oregon ("Celico") and transmitted on the Pacific DC Intertie to the Sylmar Converter Station ("Sylmar") located north of Los Angeles, California (or, alternatively, power could be injected at Sylmar and transmitted to Celico, though this rarely or never happens). The portion of the Pacific DC Intertie that is located north of the California border is known as "NOB" (short for "north of border"). The CAISO is responsible for a portion of the Pacific DC Intertie between Sylmar and NOB.

contingencies on internal alternating current lines. However, the current MRTU software is not able to automatically address contingencies that result in supply of power or demand for power being removed from the system, *i.e.*, supply/demand contingencies. Addressing a supply/demand contingency is a more complex than addressing a transmission contingency involving AC lines: a transmission contingency simply shifts flows of power on the system to other transmission lines; in contrast, a supply/demand contingency alters the balance between supply for power and demand for power at the same time that the MRTU software is working out the automated commitment of resources that may themselves be part of the supply/demand contingency. A contingency on the Pacific DC Intertie, as currently modeled, represents a supply/demand contingency because an outage of the Pacific DC Intertie would simple terminate the flow of power to Sylmar, thus altering the balance between supply and demand.

The CAISO has had discussions with the MRTU software vendor about expanding the capability of the MRTU software to address supply/demand contingencies, but realistically this issue cannot be resolved within the next several months. Therefore, for the reasons explained above, the CAISO may be required to perform manual interventions (*i.e.*, Exceptional Dispatches) in order to address contingencies relating to the Pacific DC Intertie at MRTU go-live.

The CAISO intends to explore options for modeling the Pacific DC Intertie and other capacity-based contingencies some time after MRTU go-live. One possible approach that may warrant further investigation would be to model the

Pacific DC Intertie as an injection that has two connections to the CAISO. Under normal conditions the Pacific DC Intertie would inject power into the CAISO Controlled Grid at Sylmar, but under a contingency on the Pacific DC Intertie the connection to the CAISO Grid at Sylmar could be opened and used to represent the immediate shift of flow to the alternating current interconnection that would occur when the Pacific DC Intertie trips. Such a model would result in no loss of supply, and thus would not result in a supply/demand contingency as explained above. The CAISO will, however, need to thoroughly review this potential approach to determine whether it could be feasibly implemented. In the meantime, the CAISO operators will need to review the results of the Day-Ahead Market to determine whether sufficient resources south of Path 26 are committed and, if not, utilize Exceptional Dispatch to commit additional resources.

D. The Commission Should Approve the Scope of the Exceptional Dispatch Mitigation Measures that the CAISO Proposed in the June 27 Filing to Address Market Power

The Commission should approve the CAISO's proposal to apply Mitigation Measures to Exceptional Dispatches issued in the circumstances specified in new Section 39.10 of the MRTU Tariff when the dispatched resources could exercise local market power. Specifically, as explained in the June 27 Filing, the CAISO should be permitted to apply Mitigation Measures to Exceptional Dispatches issued for any of the following three purposes: (1) to address reliability requirements related to non-competitive transmission constraints; (2) to ramp units from minimum operating levels to minimum dispatchable operating levels in order to protect against reliability contingencies that are not directly incorporated into the Full Network Model or sufficiently met by the MRTU

software; or (3) to address other special unit-specific operation or environmental constraints not incorporated into the Full Network Model or the MRTU software.[20]

The rationale for the CAISO's proposed approach is that Mitigation Measures should be applied to Exceptional Dispatches where a significant potential exists for market power to be exercised due to highly localized or unit-specific constraints and other reliability requirements that are not subject to the automated Local Market Power Mitigation ("LMPM") provisions incorporated in the MRTU software. Just as it is appropriate for the CAISO to apply the LMPM provisions to address the exercise of locational market power by resources that are dispatched through the MRTU software, it is also appropriate for the CAISO to apply Mitigation Measures to Exceptional Dispatches of resources that have the ability to exercise locational market power. Furthermore, it is the CAISO's understanding that all ISOs and RTOs issue manual dispatch instructions for reliability purposes and apply (or propose to apply) local market power mitigation rules to those dispatch instructions. The Commission should approve the CAISO's proposal to do the same.[21]

The potential for the exercise of locational market power is a concern whenever the Full Network Model and/or MRTU software is unable to address the condition and the Scheduling Coordinator is able to submit high bids knowing

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[20] Transmittal Letter for June 27 Filing at 6; proposed MRTU Tariff Section 39.10. However, the CAISO does not propose that its offer to an Exceptionally Dispatched resource of the option described in Section I.C, above, be made contingent upon the resource being Exceptionally Dispatched for any of these three purposes. Instead, the CAISO proposes to offer that option to every Exceptionally Dispatched resource that meets the criteria for receiving the offer, regardless of the purpose for which the Exceptional Dispatch was issued.

[21] *See* Transmittal Letter for June 27 Filing at 6-8. The CAISO will publicly post information that will provide a high level of transparency to Market Participants concerning the frequency, volume, costs, causes, and degree of mitigation of Exceptional Dispatches. *Id.* at 7.

that the CAISO requires the resource to operate at a level in excess of the level determined in the CAISO's markets. As requested by Commission Staff at the Technical Conference, the CAISO offers the following additional explanation concerning how market power can be exercised in circumstances requiring use of Exceptional Dispatch.

1. Forced Outages and De-rates

Ideally, the CAISO would be able to incorporate a transmission or generation outage or de-rate into the Full Network Model within one to twenty-four hours, thus allowing return to reliance on market mechanisms to establish schedules before a significant opportunity arises to adjust bidding practices. While this is the ideal, it will not always be possible to update the Full Network Model so quickly, particularly during the first two years of operations under MRTU. When these types of outages create a need for additional capacity, particularly in transmission-constrained areas of the grid, a Market Participant will know, after one Exceptional Dispatch, that its resource is needed but that the MRTU software is unable to dispatch the resource automatically. Under these circumstances, the Market Participant could exercise local market power by submitting extremely high Energy Bids and being paid as-bid.[22] Therefore, it is appropriate that such resources be subject to mitigation in the same manner as resources that are selected through the automatic dispatch software.

2. Reliability and Resource Constraints that Are Not Modeled or Not Fully Modeled in the Full Network Model and MRTU Software

[22] *Id.* at 19.

The second problematic situation, from a market power perspective, occurs when a reliability constraint or resource specific is not reflected, either fully or partially, in the Full Network Model or MRTU software. The Full Network Model and MRTU software work well when dealing with flow-based constraints and contingency analyses, but were not designed to handle on-line capacity-based constraints, resource constraints, environmental constraints, or voltage-related constraints. Four important examples of instances where the opportunity to exercise market power exists with respect to addressing conditions that are not modeled or are not fully modeled in the Full Network Model are the following: (1) capacity constraints caused by transmission outages of the Pacific DC intertie (2) Forbidden Operating Regions and other real-time operating constraints, which are resource constraints; (3) San Francisco Bay Area Delta Dispatch ("Delta Dispatch") and other environmental constraints; and (4) voltage stability constraints.

a. Responding to Outages on the Pacific DC Intertie

As discussed above, the MRTU software will not, at go-live, reflect contingencies that occur on the Pacific DC Intertie, which can lead to flow violations on other parallel transmission lines into Southern California. Reliability Standards implemented by the North American Electric Reliability Corporation ("NERC") require the CAISO, in the event of such an outage, to take actions to restore flows to regular ratings within 30 minutes. In order to meet this requirement, the CAISO currently takes two basic actions. First, on a Day-Ahead basis, the CAISO reviews Day-Ahead Schedules and determines if the amount of

capacity that is scheduled to be on-line and of quick start capacity that is expected to be available south of Path 26 would be sufficient to meet a 30-minute contingency such as the loss of the Pacific DC Intertie. If additional non-quick start capacity is needed and is available, the CAISO may commit additional capacity through the must-offer waiver denial process. Second, during the operating day, the CAISO may issue out-of sequence dispatches to some units in order get them from minimum operating levels (at which the units' ramp rates may be extremely low) to minimum dispatchable operating levels (from which the units could ramp much more quickly to their maximum available capacity).

Under MRTU, the CAISO expects that most capacity needed to meet capacity requirements in Southern California will be committed on a Day-Ahead basis through a combination of (1) capacity from units that are self-scheduled in the Day-Ahead Market, (2) capacity from units that are scheduled through the Day-Ahead Market (and are therefore eligible for Bid Cost Recovery guarantees), and (3) additional capacity that is committed at minimum operating levels through the RUC process. However, since the Day-Ahead and RUC process do not directly incorporate analysis of 30-minute contingency requirements, it is possible that the CAISO may need to use Exceptional Dispatch to commit additional capacity in order to address the 30-minute contingency. In making such unit commitments, CAISO operators will continue the current practice of selecting units to commit through Exceptional Dispatch based on a combination of reliability considerations and, to the extent practicable, projected unit

commitment costs based on the Start-Up Costs and Minimum Load operating costs of each unit.

During this Day-Ahead Unit Commitment process under MRTU, the potential for market power in providing generation to meet major zonal contingencies such as the loss of the Pacific DC Intertie is limited by a variety of factors. Because the process is performed Day-Ahead, the amount of available supply includes all available capacity (except for forced and scheduled outages). Moreover, the potential exercise of market power in this Day-Ahead Unit Commitment process is mitigated by the fact that in this market all units are subject to caps on Bids for Start-Up Costs, Minimum Load Costs, and RUC capacity. Suppliers that may be in a position to exercise market power must weigh their potential gains, in light of these limitations, against the potential profits of selling increased output in the Day-Ahead Energy market.

However, once this Day-Ahead Unit Commitment process is completed, the potential to exercise market power by units needed to provide energy beyond that scheduled through Day-Ahead Schedules dramatically increases because (1) the Day-Ahead process is designed to ensure the availability of an amount of capacity and energy that meets, but does not exceed, system energy requirements; (2) units are selected through the RUC process based only on Start-Up, Minimum Load, and RUC capacity bid prices (excluding Energy Bid prices for any unloaded capacity of units committed through Self-Schedules, the Day-Ahead Energy market, or the RUC process); and (3) units that are Self-Scheduled or committed in the Day-Ahead process can modify their Bid prices

for Energy during the time period between the closing of the Day-Ahead Market and two hours prior to the actual Operating Hour.[23] Thus, the Real-Time Energy Bid prices of some of unscheduled capacity could be extremely high for units with a high expectation of being dispatched above Minimum Load under Exceptional Dispatch for any locational reliability needs or unit-specific operating constraints. This situation may be characterized as a form of "temporal market power," which is created by the increasingly limited amount of supply available in Real-Time by virtue of the fact that not all resources effective in addressing the contingency are available in Real-Time (*i.e.*, some of the long-start units were not committed Day-Ahead and therefore are not available to compete in Real-Time). Under these conditions, units that are needed to operate at minimum dispatchable operating levels could bid up to the $500 Energy Bid cap specified in the MRTU Tariff[24] regardless of their costs and still receive dispatches from the CAISO because other effective resources that could contest these bids were not committed Day-Ahead and are thus not available.[25]

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[23] The ability of units to change their Energy Bids prior to the Real-Time Market also limits the ability of the CAISO to minimize anticipated cost of any units committed through Exceptional Dispatch, since the CAISO cannot project actual Bid costs of dispatching a unit to minimum dispatchable operating levels during peak hours.

[24] For the twelve months following the implementation of MRTU, the maximum Energy Bid price will be $500/MWh. MRTU Tariff, § 39.6.1.1. After the twelfth month following MRTU implementation, the maximum Energy Bid price will be $750/MWh, and after the twenty-fourth month following MRTU implementation, the maximum Energy Bid price will be $1,000/MWh. *Id.*

[25] The discussion in this section focuses on capacity requirements south of Path 26 to protect against loss of the Pacific DC Intertie, the same concerns apply to capacity constraints generally. The Pacific DC Intertie is not the only capacity-based constraint. The CAISO maintains Operating Procedures that identify resources needed to be on-line to in specific geographical areas such as South of Lugo, San Diego, and Southern California Import Transmission ("SCIT").

b. Forbidden Operating Regions and other Real-Time Unit-Related Operating Constraints

The inability of the CAISO's Real-Time Market software to recognize Forbidden Operating Regions and other unit-related Real-Time operating constraints (such as minimum operating times after being dispatched below a certain Forbidden Operating Region) may also give rise to opportunities to exercise market power when a unit knows that it is needed by the CAISO. For example, assume that the CAISO's Day-Ahead Energy market and RUC process commit just enough capacity to meet all reliability requirements of the CAISO system. Thus, virtually all capacity that is on-line is needed to meet various specific reliability requirements. Under this scenario, temporarily dispatching below a Forbidden Operating Region (due to market prices and bids) could cause the unit's unloaded capacity to be unavailable for a period of time when it would be needed to meet reliability needs.[26] Under these conditions, the CAISO may utilize Exceptional Dispatch to keep the unit operating above this Forbidden Operating Regions through an Exceptional Dispatch. Without bid mitigation, a unit that knew that it was needed for reliability purposes could bid up to the $500 Energy Bid Cap recognizing that the CAISO would need to utilize Exceptional Dispatch in order to manage its unit-specific operating characteristics. This

[26] For example, this could occur if the unit bid capacity above a Forbidden Operating Region at a relatively low price during one hour (so it would get dispatched through the market software), while bidding capacity above this Forbidden Operating Region at a significantly higher price during subsequent hours (so it would not get dispatched through the market software). This would cause the MRTU software to dispatch the unit above this Forbidden Operating Region during one hour (when its bid price was lower than the LMP"), and then dispatch the unit below this level during subsequent hours (when its bid price was significantly high than the LMP). If the unit had a significant minimum down time below this Forbidden Operating Region (*e.g.*, one to four hours) and its capacity above this level was needed for any reliability needs during these future Operating Hours, the CAISO would need to constraint the unit on above this Forbidden Operating Region through an Exceptional Dispatch.

scenario is entirely plausible because generators will, of course, be aware of the operating characteristics of their own units and what actions CAISO operators need to take in order to manage those characteristics.

c. Delta Dispatch and Environmental Constraints Generally

Delta Dispatch is an environmental restriction that limits the use of specific Generating Units in the Sacramento Delta during several weeks in the spring and summer, which in turn requires the CAISO to dispatch different combinations of resources under certain circumstances.[27] Delta Dispatch is not modeled in the Full Network Model due to its temporary nature, its complexity, and the fact that it involves constraints that simply cannot be modeled, such as water temperature. Under the Delta Dispatch operating procedures, the CAISO must ramp up output from one unit prior to ramping up output from other units. Since this constraint is not included in either the Day-Ahead or the Real-Time dispatch software, Exceptional Dispatch of the first unit may be necessary to ensure that capacity from the other units is actually available in the Real-Time Market. This can lead to the opportunity to exercise market power by units that are called on during those periods in which resources are constrained by this environmental restriction. Such an opportunity exists because of the predictable nature of this phenomenon – that is, generators will know when these environmental restrictions apply, and therefore, that the CAISO will need to utilize Exceptional Dispatch in order to commit a different set of units than those that would be dispatched under the automated process.

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[27] Transmittal Letter for June 27 Filing at 20 & n.54.

d. Voltage Stability Constraints

As discussed above in Section II.C, the MRTU software does not model voltage support conditions, and, as the Commission has recognized, the CAISO may need to rely on Exceptional Dispatches to commit resources or adjust the amount of voltage support on the grid in Real-Time. Historically, the CAISO has relied on units under RMR contracts to address voltage stability issues. However, the number of units under RMR contracts has decreased significantly over the past several years due to the success of the RA program and enhancements to the grid. In particular, since the inception of the RA program in 2006, more than 7800 MW of capacity has been released from RMR contracts. As of 2009, only 2242 MW of capacity will remain under RMR contracts.[28] The purpose of the RMR contracts is to limit the ability of units whose availability was necessary to ensure local reliability to exercise market power. RMR contracts have served as a form of local market power mitigation by limiting the payment that units received for services such as voltage support, including energy needed for voltage support, through compensation mechanisms set forth in the contracts. Most of the units that were formerly under RMR contracts are now RA units. However, the RA mechanism does not limit the compensation that units can receive for energy needed for voltage support. Thus, units that are needed by the CAISO to resolve voltage stability issues can submit very high bids knowing

[28] See the October 20, 2008, memorandum regarding "Briefing on Results of RMR Contract Process for 2009" provided by members of CAISO management to the CAISO Governing Board, which is available on the CAISO Website at http://www.caiso.com/2067/2067e65a26ea0.pdf. For purposes of historical comparison, 9820 MW of capacity was under RMR contracts for 2003. *See* http://www.caiso.com/docs/09003a6080/1c/53/09003a60801c53b3.pdf.

that the CAISO will have to call on them through Exceptional Dispatch. It is therefore appropriate that mitigation apply under such conditions.

E. The Commission Should Accept the CAISO's Two Proposed Methodologies for Determining the Amount of Exceptional Dispatch Supplemental Revenues that an Eligible Mitigated Resource Will Receive

As explained in the June 27 Filing, the CAISO anticipates that Exceptional Dispatches will need to be issued more frequently in the first two years of MRTU than during subsequent periods, especially during the first few months of implementation. During the first few weeks or months of market operations under MRTU, operators will be gaining experience with the new software, and any software design flaws that were not apparent during the months of testing prior to MRTU start-up will become manifest. The CAISO is concerned that, in the absence of especially strong initial Exceptional Dispatch Mitigation Measures during the first few months after MRTU start-up, some mitigated generators may be able to receive extraordinary payments not due to true reliability needs but rather due to temporary software issues.[29]

Because the need for Exceptional Dispatch is likely to be greater at the beginning of MRTU than during the remainder of the period, the CAISO has proposed two different methodologies for determining the amount of "Exceptional Dispatch supplemental revenues" that an "eligible mitigated resource" should receive.[30] The first of these methodologies will apply from the date that MRTU is

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[29] Transmittal Letter for June 27 Filing at 11-12; Attachment C to June 27 Filing at 19.

[30] As explained in the June 27 Filing, the term "mitigated resource" refers to a resource to which the CAISO applies Mitigation Measures for any of the three purposes described in proposed Section 39.10 of the MRTU Tariff. June 27 Filing at 6 n.14. A mitigated resource that

implemented until the end of the fourth month of MRTU operations, at which point it will be superseded by the second methodology. Under each of these methodologies, the amount of Exceptional Dispatch supplemental revenues that an eligible mitigated resource will be receive will be limited by a revenue cap. Once the cap is reached, the resource will be treated like other mitigated resources and be paid the higher of the LMP or its Default Energy Bid price.

The CAISO proposes that during the initial four months eligible mitigated resources will be settled at the higher of (a) the Default Energy Bid price plus a $24/MWh adder or (b) the Resource-Specific Settlement Interval LMP, up to the revenue cap. Supplemental revenue amounts will be defined as the higher of (a) the Resource-Specific Settlement Interval LMP minus the Default Energy Bid price for the resource or (b) the Default Energy Bid plus a $24/MWh adder, minus the Default Energy Bid price for the resource, multiplied by the amount of Energy provided by the resource under Exceptional Dispatch. The CAISO proposes to employ a $24/MWh adder because that is the level of the Bid Adder under the existing MRTU Tariff for Frequently Mitigated Units that are not designated under ICPM or as RA resources and to which the CAISO's market power Mitigation Measures apply. The Commission has approved this adder for Frequently Mitigated Units, recognizing that it provides the opportunity for recovery of going-forward fixed cost.[31] It is thus reasonable to use adder during the first four

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is eligible to receive supplemental revenues is referred to as an "eligible mitigated resource." *Id.* at 9.

[31] *California Independent System Operator Corp.*, 116 FERC ¶ 61,274, at P 1069 (2006) ("We accept the CAISO's proposed $24/MWh bid adder for FMUs [Frequently Mitigated Units] as reasonable."); *California Independent System Operator Corp.*, 112 FERC ¶ 61,013, at P 144 (2005) ("We find the CAISO's proposal to compensate FMUs through the use of a bid adder is a

months of MRTU operations to provide a contribution to units' fixed costs while ensuring that Exceptional Dispatch supplemental revenues will not accrue at an excessive rate.[32]

Beginning with the fifth month of MRTU operations, the CAISO proposes that mitigated resources eligible to receive supplemental revenues be settled at the higher of (a) the resource's Energy Bid price or (b) the Resource-Specific Settlement Interval LMP, up to the level of the revenue cap. The Energy Bid price will be bounded only by the "safety net" Bid cap, which will be $500/MWh in the first year of operations under MRTU and will increase thereafter.[33] For purposes of this methodology, supplemental revenue amounts are defined as the higher of (a) the Energy Bid price for the resource minus the Default Energy Bid price for the resource or (b) the Resource-Specific Settlement Interval LMP, minus the Default Energy Bid price for the resource, multiplied by the amount of Energy provided by the resource under Exceptional Dispatch. The advantage of this methodology is that it will allow eligible mitigated resources more flexibility to recover fixed costs by allowing supplemental revenues potentially to accrue in a fewer number of hours than the $24/MWh adder would allow.

The CAISO believes its proposal to offer resources a choice between an ICPM designation or supplemental revenues can be utilized with the $24/MWh bid adder approach as well. Thus, during the first four months of MRTU,

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reasonable approach that provides these units with certainty that they will have an opportunity to recover their fixed costs for serving a local reliability need under MRTU.").

[32] Transmittal Letter for June 27 Filing at 12-13; Attachment C to June 27 Filing at 19, 22 (citing MRTU Tariff, § 39.8.3). The CAISO notes that ICPM designations will be available in the first four months after MRTU implementation for any Significant Events that warrant backstop capacity procurement from non-RA and non-RMR resources. *See* Attachment C to June 27 Filing at 19.

[33] MRTU Tariff, § 39.6.1.1.

resources will have the option to accept a 30-day ICPM designation or receive a $24/MWh bid adder during the same 30-day period.

III. CONCLUSION

Wherefore for the foregoing reasons, the CAISO requests that the Commission act on the CAISO's Exceptional Dispatch proposal in a manner consistent with the discussion herein.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each party listed on the official service list for these proceedings, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure (18 C.F.R. § 385.2010).

Dated at Washington, D.C. on this 24th day of November, 2008.

/s/ Bradley R. Miliauskas
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