

**COMMENTS ON BEHALF OF THE CITIES OF ANAHEIM, AZUSA, BANNING,
COLTON, PASADENA, AND RIVERSIDE, CALIFORNIA
ON THE THIRD RELIABILITY SERVICES WORKING GROUP MEETING**

In response to the ISO's request, the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (collectively, the "Six Cities") submit the following comments on the discussion at the third Reliability Services Working Group meeting on April 23, 2014:

The Six Cities Support Deferral of Further Efforts at Development of a Residual or Backstop Capacity Auction.

Consistent with their previous comments in the Reliability Services Initiative stakeholder process, the Six Cities strongly support deferral of further efforts to develop a residual or backstop capacity auction design until the ISO and market participants have the opportunity to observe how the major revisions to market structures and processes anticipated over the next eighteen months, *i.e.*, the 15-Minute Market, the Full Network Model Expansion, the Energy Imbalance Market, and Flexible Resource Adequacy requirements, affect both RA requirements and the operational availability of RA resources. The Cities recommend that further consideration of a residual or backstop auction mechanism be deferred until at least the first quarter of 2016, which should allow a full year's experience with the market design changes to be implemented later this year and in early 2015.

The Opportunity Cost Methodology Applicable to Use-Limited Resources Must Consider Local Reliability Requirements That Are Not Addressed in the ISO's Optimization Process.

Although the Six Cities support the concept of allowing use-limited resources to reflect use limitations through bids that recognize opportunity costs, the opportunity cost methodology described in the ISO's presentation at the April 23rd meeting is incomplete. Two of the Cities (Pasadena and Riverside) must utilize internal resources that are subject to use limitations to maintain reliability of service to their customers during peak load conditions. The ISO's optimization algorithm currently does not include these must-run requirements for the Cities' internal resources. Any determination of opportunity costs for the Cities' resources must include recognition of must-run needs to maintain local reliability.

Develop or Adapt Energy and Ancillary Services Products and RA Replacement/Substitution Rules to Maximize Availability and Use of Existing and Anticipated Capacity Resources Rather Than Imposing More Stringent Must-Offer Requirements and Availability Penalties.

The limited application of the Capacity Procurement Mechanism to date to address episodic and unsystematic capacity needs confirms that the existing RA framework effectively satisfies needs for System and Local RA resources. Because Flexible RA requirements are not yet in place, there is no direct market experience on which to draw. The information at page 26 of the ISO's presentation for the February 4th workshop, however, indicates that the existing RA resource fleet contains approximately 25,000 MW of flexible capacity that has been operationally available to the ISO through economic bids and more than 20,000 MW of additional RA capacity with flexible attributes that could be made operationally available to the ISO. Measures to encourage economic bidding by RA resources (as well as non-RA resources) appear to offer access to low-hanging fruit and ought to be the focus of near-term efforts by the ISO and stakeholders.

Although the ISO's proposed Must-Offer requirements will compel economic bidding by resources capable of meeting the Category 1 eligibility requirements and designated as Category 1 Flexible RA resources, there are additional resources with flexible attributes that will not be able to satisfy the demanding Category 1 criteria and, therefore, will not be subject to the associated Must-Offer requirements. The ISO should seek to identify and develop measures that will encourage System and Local RA and non-RA resources with flexible attributes to participate through economic bidding on a spot market or shorter-term basis. One such measure is the Flexible Ramping Product, which the Cities again urge the ISO to develop promptly and to craft in a way to invite participation by as broad an array of resources as possible.

In addition, replacement and substitution rules for RA resources should not impose eligibility requirements more stringent than necessary for the replacement or substitution period or more onerous than the eligibility requirements for the capacity subject to replacement or substitution. The ISO's responses at pages 10 and 68 in the matrix of comments submitted after the February 4, 2014 Reliability Services Working Group meeting indicate that the ISO is re-considering a current practice (which does not seem to be reflected in the tariff) of requiring a resource that replaces or substitutes for a local resource designated for System RA capacity to satisfy Local capacity requirements as well. This practice unjustifiably expands Local RA obligations, and the Six Cities support a rule that allows replacement or substitution with like-for-like capacity (although "higher" quality capacity obviously should be eligible to replace or substitute for "lower" quality capacity if desired by the Scheduling Coordinator having the obligation to replace or substitute).

With regard to implementation of Flexible RA requirements, the ISO proposes that a Category 1 Flexible RA resource must be able to start up at least twice a day to be designated for a month. But if a designated Category 1 Flexible RA resource is subject to an outage (either planned or forced) for a week during a month, a use-limited resource with 15 allowed start-ups (as well as sufficient energy availability) should be eligible to serve as a substitute or replacement resource for the seven-day outage. In general, the ISO should craft replacement and

substitution rules to allow the broadest possible array of resources to satisfy the replacement/substitution requirement consistent with maintaining reliability.

Instead of focusing on measures designed to expand the pool of resources able to contribute to meeting flexibility requirements, a number of the potential design changes discussed at the April 23rd workshop appear likely to restrict the ability of resources with flexible attributes, especially use-limited resources, to provide flexible capacity. Expanding must-offer obligations and modifying the availability standard to apply to expanded time periods and bid submission rather than operational capability will not encourage more resources with flexible attributes to make themselves available to the ISO but instead will have the opposite effect. Imposing ever more demanding obligations and expanding exposure to potential penalties will outright disqualify many resources that could contribute to operational flexibility and discourage others from doing so by increasing risks of penalties. With approximately 45,000 MW of existing capacity that is capable of flexible operation during some periods, it would be counter-productive for the ISO to expand obligations and exposure to penalties in ways that preclude or discourage resources from offering flexibility. Moreover, it is likely to force LSEs to procure additional capacity that is not necessary to maintain reliability and that simply will result in increased and unnecessary cost to ratepayers.

The Six Cities also oppose the ISO's proposal to rescind the exemption from SCP requirements for grandfathered resources subject to contracts entered into prior to the adoption of SCP requirements and penalties. Although the ISO's presentation for the 3rd Working Group Meeting quantified the MWs and numbers of resources eligible for all categories of SCP exemptions, there was no information regarding the megawatts or numbers of resources eligible for the grandfathered exemption or the relative availability of grandfathered resources. More importantly, there was no demonstration that the grandfathered exemption has resulted in any impairment of system reliability. The grandfathered exemption appropriately recognizes that contracts entered into prior to the adoption of SCP requirements may give rise to additional risks or challenges to avoiding SCP penalties. The ISO should continue to respect pre-existing contractual commitments and limitations and should keep the SCP exemption for grandfathered resources in place unless and until there is a compelling reason, based on a demonstrable reliability concern, to revoke the exemption. The ISO has not demonstrated that such a reason exists.

Increased Standardization Is Not Desirable at This Time.

For similar reasons, it is unjustified and potentially counter-productive to devote efforts to increasing standardization of capacity products at this time. The unsystematic residual capacity needs that are likely to arise on occasion may involve attributes that are specific to the situation and, hence, may not be resolved by procurement of a standardized capacity product. In addition, as discussed under the third topic above, short-term replacement or substitution resources should not be required to have all the attributes of the RA resources for which they are standing in - - only those required for the period of replacement/substitution. Increased standardization may impede cost-effective use of available capacity resources to meet non-standardized or short-term needs, which may end up being the only backstop needs that occur. And deferring development of a residual or backstop capacity auction postpones or eliminates

any need for increased standardization of capacity products in order to facilitate procurement through an auction process.

Cost Allocation for Backstop Procurement Should Track Cost Causation.

The Six Cities urge the ISO to focus more attention on cost allocation concerns. Whatever backstop procurement mechanism the ISO considers, allocation of the associated costs should be based strictly on cost causation principles. If resource performance characteristics lead to backstop procurement costs, the relevant resources should bear the associated costs, whether the resources in question are preferred or traditional in nature. To promote both transparency of market processes and fundamental fairness, the ISO should avoid socialization of backstop procurement costs to the maximum extent possible.

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