

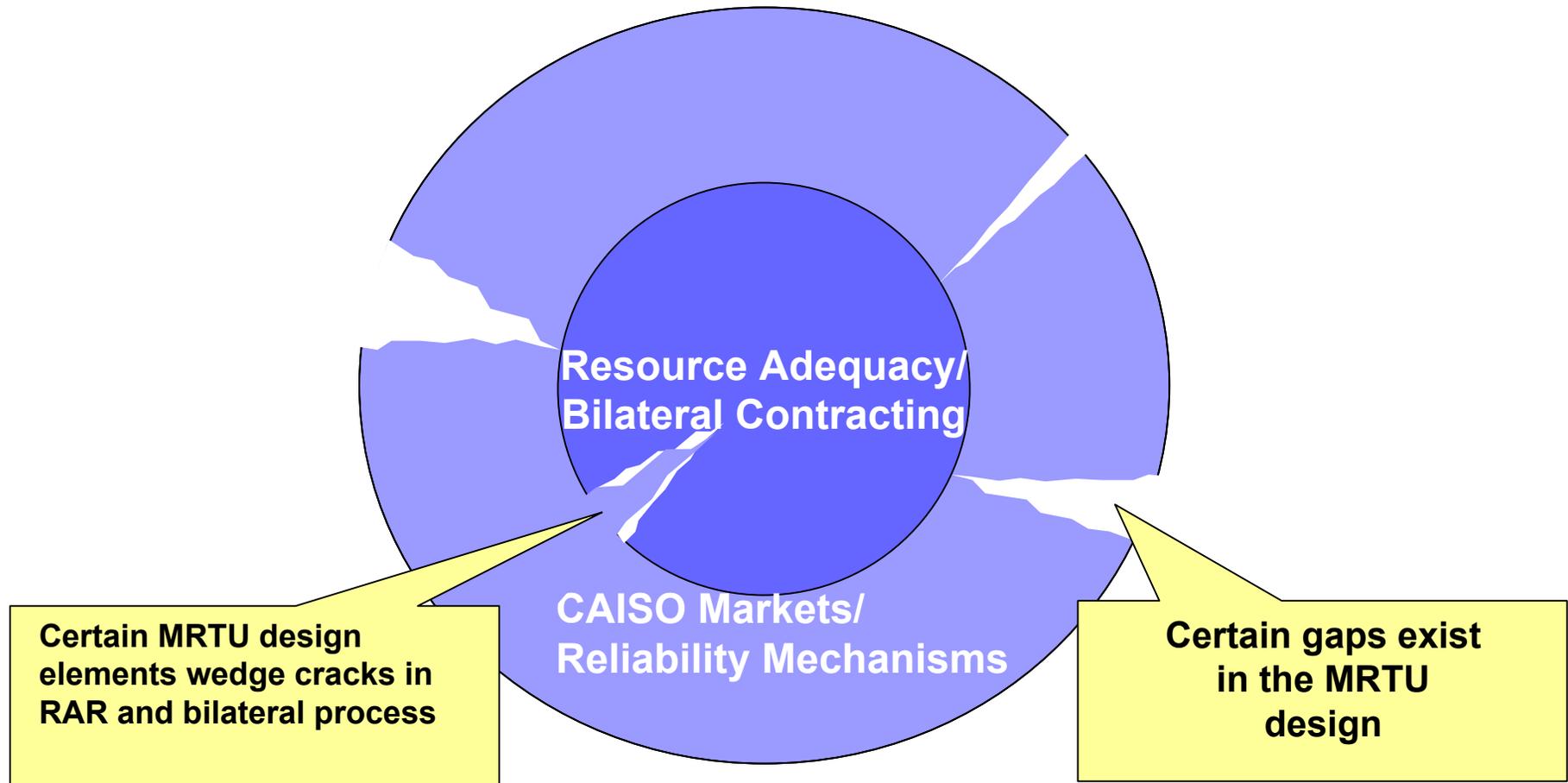
The End Game: Closing MRTU and RA Design Gaps

Western Power Trading
Forum Comments to MSC
September 22, 2005

WPTF Is Committed to Success of the MRTU

- WPTF has been encouraged in many areas by the significant progress toward market reforms
- A complete MRTU design and full integration with RA is vitally important to provide a stable investment climate for California's economic vitality

MRTU End Game design goal: free from critical gaps and free from imposing wedges in RAR – forward bilateral contracting structures



Now is the time to reveal any gaps in the MRTU design and integration

- FERC July Order
- Address gaps
- An unsuccessful course will require significant corrective action

Question: Will the design result in sufficient market mechanisms in place in California to ensure the delivery of energy and capacity to California?

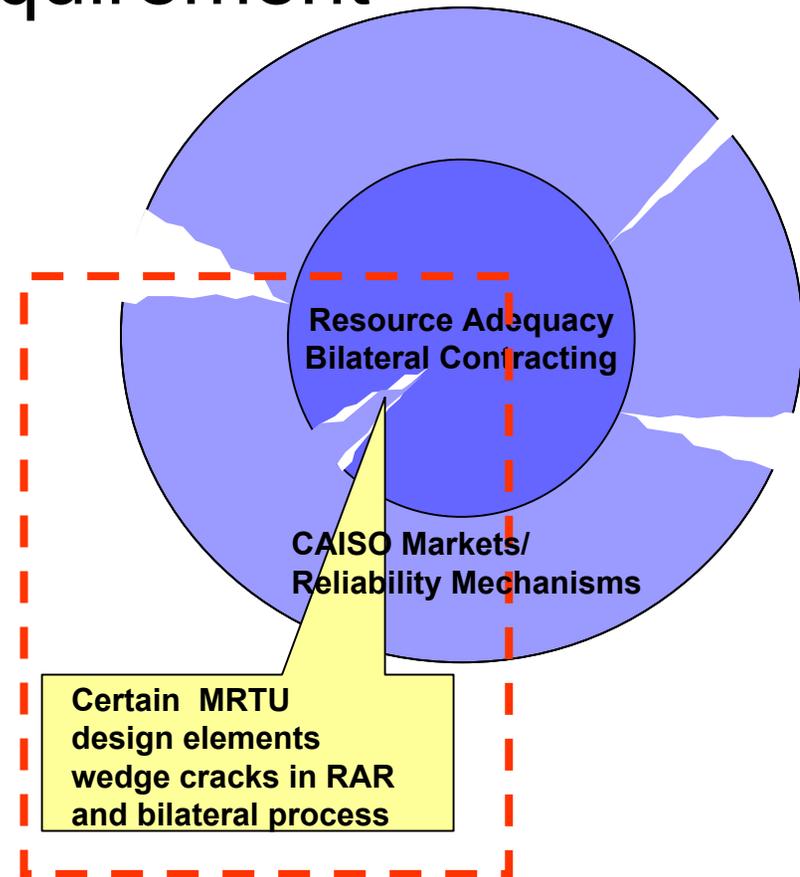
There are four areas requiring corrective action

1. RAR/MRTU interface
2. PJM-style mitigation
3. Details of ISO backstop procurement
4. Absence of certain critical functionality (such as convergence bidding)

1. RA/MRTU Interface: Bidding, Settlement, Must-offer requirement

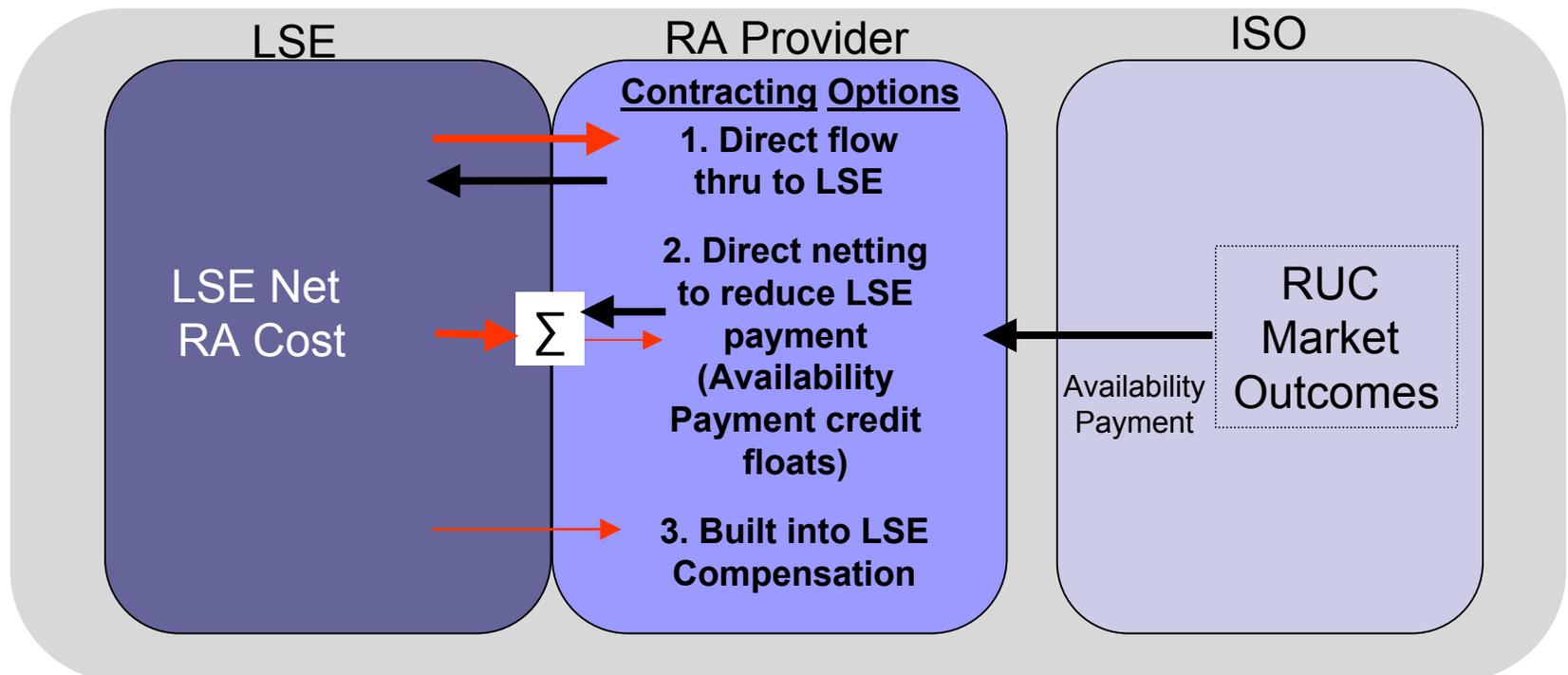
What translates RAR provisions into operations through market-based capacity mechanisms?

- CPUC RA design – flexible bilateral
- ISO RUC mechanism – structured market
- ISO treatment of RA capacity – challenging interface



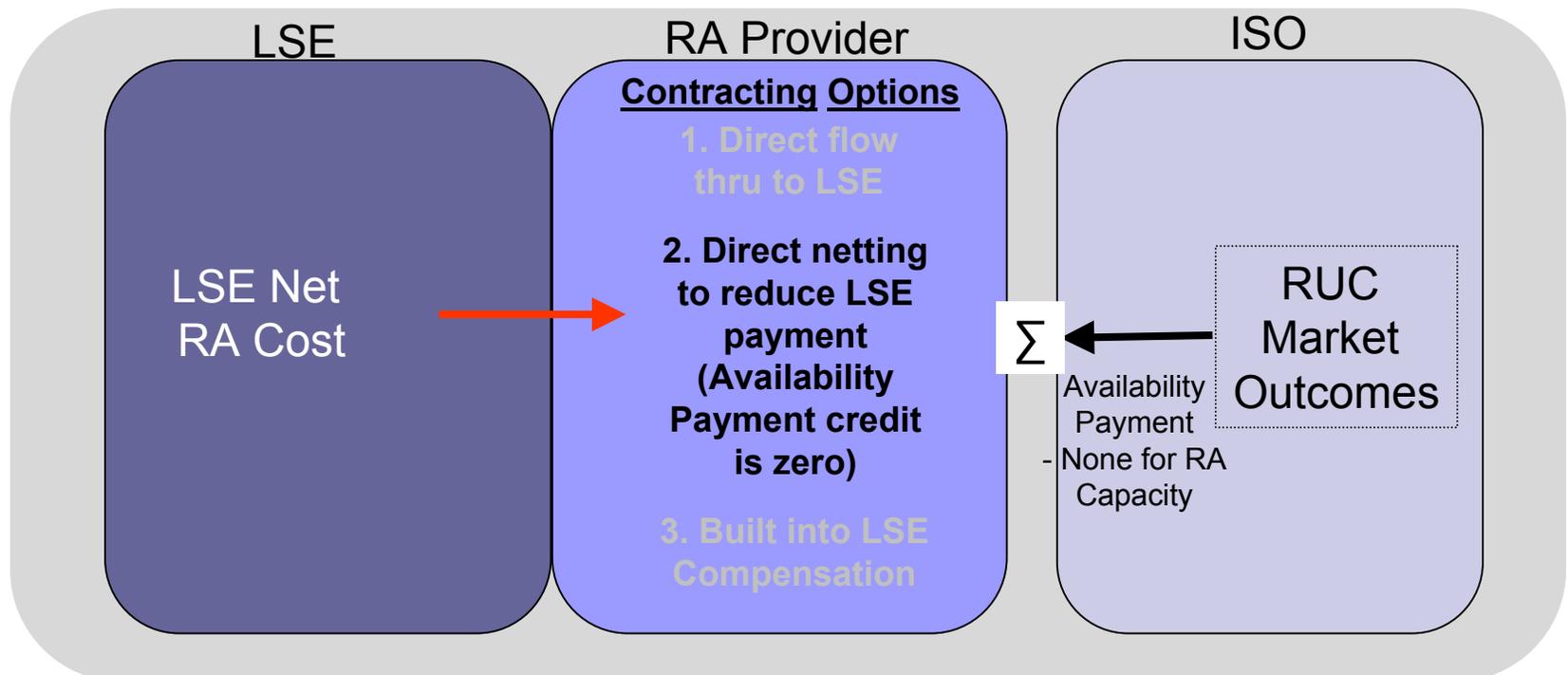
Availability Payment \neq “Double” Payment

- Bilateral Choice vs. “fixing” options (e.g. no CAISO payments to RA Provider) impacts who bears risks and risk premiums



Availability Payment ≠ “Double” Payment

- ISO predetermination, removes bilateral flexibility

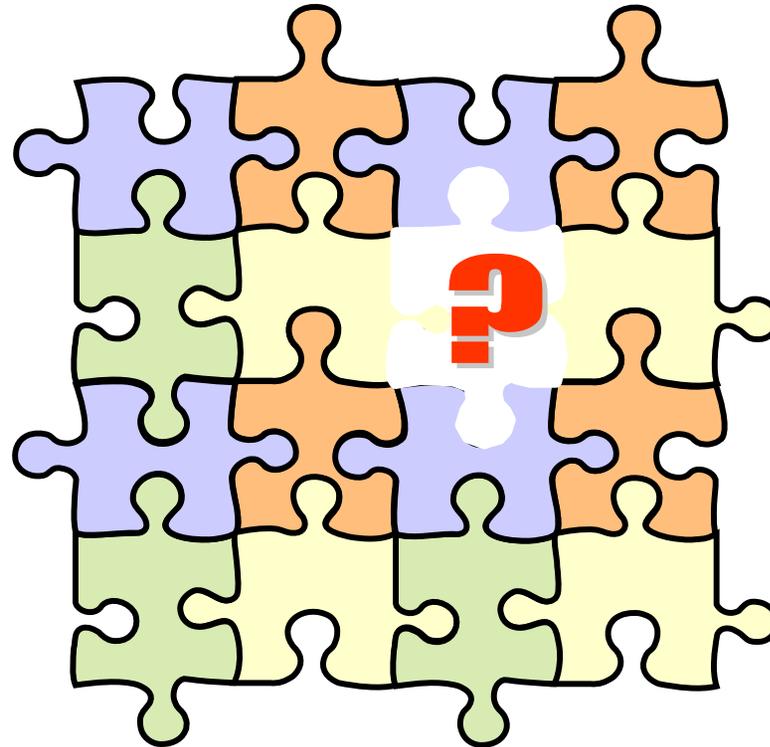


2. Is application of PJM-style mitigation to CAISO situation creating fatal MPM gaps and mismatches?

Need integrated workable mitigation package

- a) FMU bid adder – designed for specific outcome in PJM for units coincident with resource de-activation protocols – will not apply to any market units in CA
- b) Local Backstop Mechanism – needs careful treatment to not undermine RAR incentives
- c) Competitive Path Screen – target of “best estimate” of competitive paths versus overly conservative

2. MPM (cont.) Bottom line: MRTU design elements and MPM *as a set of provisions* have to result in complete and workable markets



3. Perpetuation of critical functional gaps in MRTU

- The Release 2 list
- Lack of virtual bidding
 - Virtual bidding in other FERC ISO/RTO markets

What needs to be done to fill gaps such as these?

Need fresh broad review on such issues:

- RAR and RUC payment mechanisms
- Ask the hard question:

Will RAR and MRTU produce sufficient incentives such that developers will send turbines to new development sites in California versus elsewhere?

- Reliability capacity service tariff rate type “backstop”
- Critical functionality

Why is this so important?

- Risk of Failure
- Implementation – not sufficient
- Success judged by long-run outcome
- End Game is here

Additionally: WPTF offers its position on CRR Auction

- Day 1 auction and allocation of auction revenue rights
- Complexity and uncertainty adversely impact both options
- Liquidity, efficiency benefits
- LSEs and non-LSE bidding rules as needed