

**Panelist Opening Comments by Sean Gallagher  
(Director, California Public Utilities Commission)  
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**Thanks for the Opportunity to Be Here**

Good morning. I'd like to start by thanking you for the opportunity to address the FERC MRTU Seams Technical Conference. I am pleased that all five Commissioners, Cal ISO and stakeholder community have made this an important priority as demonstrated by your presence here today. We want to thank FERC staff for the tremendous effort put into reaching the September 21 order and acknowledging the unique character of Western markets.

Before I get too far I want to apologize that I won't be able to stay for the full session today. I've got to head back to the airport within the hour so that I can get back to host a large CPUC holiday party today.

One thing that I'm not going to do today is address any particular SEAMS issue in any detailed way. Instead, the message that I want to convey today is three (four?)-fold: First, we're pleased that the debate about *whether* to go forward with the ISO's market re-design is over. It's been a long time coming. We're now in the implementation stage, and as with any large project, there are some implementation issues that have to be worked out.

Second, California, intends to be a good neighbor. The fact is, we depend on our neighbors a good deal, so we have to.

Third, to the extent that parties identify legitimate SEAMS issue that really affect the ability of market participants to conduct and complete commercial transactions, I have a great deal of confidence that we'll be able to work those issues out in a manner that will allow commercial transactions to go forward. The ISO has shown its willingness and ability to work with our neighbors in the past and we expect that to continue. Does that mean that every party's issue will get resolved to their satisfaction? No it doesn't – particularly where parties are seeking an opportunity to re-litigate issues that have been resolved in one of the numerous orders addressing MRTU. And I do think that there's a lot of noise and hype involved in some of the claims

that have been advanced about MRTU. We are going to have to separate the wheat from the chaff when it comes to addressing purported seams issues.

Fourth – it does seem to me that there are some differences in issues raised by control areas outside of California as opposed to those inside of California. In particular, the newest control areas in California are entities that on their own volition left the ISO. I’ve frankly got very little sympathy for claims asserted by these entities. Their issues traditionally have focused on cost allocation – in our view they’ve often sought subsidies from IOU ratepayers for their activities. Their claims must be viewed through this prism. It is NOT the role of the ISO to subsidize others, particularly those who have seceded from the ISO.

MRTU is designed to bring increased efficiencies and transparency to the markets and to transmission utilization. I am confident that these aims can be achieved, and that this will meaningfully support California’s energy policy goals, some of which I will briefly mention today.

### **CPUC Supports MRTU and its Goals/Seams Issues Have Been Around a Long Time And Are Not Created by Cal ISO’s Market Design**

At the outset, I would like to say that the California Public Utilities Commission (CPUC) has been very involved in the development of MRTU. Like many of you, we remember when it was called MD02, and even earlier, when it was called “Market Redesign 2000.” There’s no doubt that moving to an LMP market brings with it some uncertainties. Our commission was able to support MRTU because we recognized that the reform of the Cal ISO’s problematic zonal congestion management system and its replacement by the more accurate, efficient and transparent MRTU design needs to proceed.

And, importantly, we were able to work with the ISO and with FERC to incorporate a number of mitigation and other measures intended to narrow uncertainties and protect consumers. Those protections include, for example, local market power mitigation and resolution of the “Sellers Choice” issues, which explored whether treatment of delivery points will be just and reasonable under an LMP market regime.

As the CPUC stated in a press release in late September, “The CPUC supports MRTU’s goals to promote reliability, provide more accurate price

signals, and provide better signals for generation investment in California. Successfully realizing these goals is important for California's energy future." So, we're committed to going forward.

It's important to note that "seams" issues exist today under the current market design, and seams issues will exist tomorrow under the new market design. A number of the issues identified in recent filings as seams issues have been around for a long time and are just not created by the Cal ISO's market redesign. While such issues may be deserving of attention, we must be careful to separate out those that are not specifically MRTU-related and focus on our immediate effort on those that are demonstrably created or exacerbated by the change of the Cal ISO's market design. Moreover, It's not enough to say, "hey, there's a difference here." Differences exist today, and in most cases, those differences can be managed. What's important is to address issues that would otherwise impede beneficial commerce.

### **CPUC Has a Strong Interest in the CAL ISO's Collaborative Process and Acknowledges that Many Issues Need to Be (And Can Be) Worked Out**

The CPUC has a strong interest in seeing that the CAL ISO's markets and operations work together within and outside the ISO Control area. As I said earlier, I strongly believe that parties both within and outside the ISO have sufficient incentives to ensure that this happens – there's too much money at stake not to.

As we move forward with the implementation of MRTU, we agree that there's a need for the CAL ISO and neighboring control areas to sit down together to resolve MRTU seams issues.

I actually think that the ISO has a pretty good track record on this kind of thing. Over the past eight years there have been a number of occasions where an ISO proposal has caused concern among our neighbors. My experience is that on such occasions, one of two things has happened. On the one hand, neighboring control areas have often found, after further study, that they could manage or accommodate ISO proposals that initially appeared troublesome. I believe that the introduction of 10 minute markets is one example of issues that fall into this bucket. On the other hand, where experience demonstrates that an ISO proposal truly is having a negative impact on the ability to conduct transactions, the ISO has changed.

Amendment 52, for instance, involved a situation in the early days of market redesign when the CAL ISO changed the rules for bidding by imports. This change facilitated the participation of importers in CAL ISO markets to the benefits of both California, which often relies on imports, and our neighbors, for whom California is an important market.

We're confident that the various interests represented here today will be open minded and constructive (maybe even creative!) regarding the implementation of MRTU and its coordination with neighboring areas, and to respond quickly to ensure that consumers in the West benefit as much, and soon, as possible.

One instance in which I think the ISO has responded positively already to the recent filings is by requesting cooperation in exchange of scheduling data. More transparency through exchange of scheduling data should mean more accurate transmission availability and monitoring of unscheduled flows. This efficiency should translate into more region wide cost savings and benefits to consumers on either side of the interties.

Another point that is worth making in this regard is that reciprocity among neighbors is essential. To the extent the operation of the Cal ISO is claimed to have impacts on its neighbors, we must also examine whether there are analogous impacts on the Cal ISO by the operation of other control areas, and solve such problems in a balanced fashion.

### **The CPUC Strongly Believes that Resolving Seams Issues Needs to be Accomplished Within the Context of California State Legislative and Policy Goals**

CPUC is interested in ensuring integration of MRTU issues in such a way that it facilitates the implementation of the loading order established in the Energy Action Plan that has been adopted by the CPUC and California Energy Commission. The loading order places a priority on the development of energy efficiency, demand side, and renewable resource development. Consistent with this policy, the California State Legislature recently passed legislation that would accelerate the state's Renewables Portfolio Standard ("RPS") to achieve a 20 percent penetration of qualifying renewable energy by 2010. As stated in our recent comments, the CPUC is concerned that the resolution of MRTU-related seams issues not *interfere* in any way with the achievement of this goal. Instead, we anticipate that the

resolution of seams issues and the resulting increased market efficiencies will actually *foster* the achievement of this RPS goal as well as the other high priority objectives highlighted in California's Energy Action Plan.

### **The CPUC's Resource Adequacy Program in California Is Designed as a Complement to MRTU**

I do want to address the concern that's been articulated that MRTU is problematic for bilateral contracts. Our Commission's Resource Adequacy program and today's California market are explicitly premised on bilateral contracts and that will remain so after MRTU is implemented. Resource Adequacy supports reliability, and helps to maintain wholesale prices at just and reasonable levels. Resource Adequacy supports the MRTU market design, and we've worked hard with the ISO and the parties, in both its design and the implementation, to ensure that Resource Adequacy works hand in hand with MRTU. FERC's September 21 Order acknowledges and supports California's progress in developing and implementing Resource Adequacy.

Our utilities have engaged in several rounds of procurement over the last several years procuring, thousands or perhaps tens of thousands of MW of capacity and energy over the long, short, and medium term - as long as 20 years in some cases. All of this procurement activity, all of this bilateral contracting, took place with MRTU firmly in mind. It is simply not the case that MRTU does or will inhibit bilateral contracting.

To the contrary, we expect that bilateral contracts and associated hedging activity will utilize the new flexibility and transparency, of MRTU. Our resource adequacy requirements implemented in an MRTU environment will enhance reliability, protect against price volatility, and reduce the likelihood of market manipulation that exists when demand outstrips supply.

### **Resolving Seams via a Collaborative Process Realizes Economic Benefits for Consumers**

One reason to have some confidence that real seams issues will get resolved through mutual dialogue is that resolving seams issues between control areas will lower transaction costs. Breaking down barriers to sell power between control areas will provide consumers access to the most economic power and provide sellers with expanded markets.

In closing, I don't want to give the impression that the CPUC believes that everything is perfect with MRTU (or with our own RA program, for that matter). The state didn't get everything we wanted in the MRTU design, any more than anyone else got everything that they wanted. But I am not going to offer our critique of the market design today any more than I am going to offer a point by point rebuttal of the many errors and omissions in the filings of the parties expressing concerns about MRTU seams issues.

This is not the time to re-litigate what any of us won and lost in the MRTU design. We do believe that MRTU will improve known deficiencies in the existing market design, that it is likely to be an effective and efficient market design, and that there are build-in protections to prevent it from spinning out of control as our markets did several years ago.

Now *is* the time for the ISO to work closely with all interested parties to make implementation of MRTU as smooth, and as equitable, as possible. I thank FERC for its attention to this matter, I'm confident that the ISO and the parties have the right incentives to work out real issues that might otherwise impede commerce, and I can assure you that our Commission will work closely with the ISO and all of the parties to make this happen.

Thanks again.