FEDERAL ENERGY REGULATORY COMMISSION

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NEWS RELEASE

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COMMISSION REAFFIRMS KEY CALIFORNIA RULINGS

In a broad rehearing order that addresses a number of wide-ranging issues related to California and the western energy markets, the Federal Energy Regulatory Commission today generally reaffirmed its key earlier decisions on pricing and price mitigation measures.

Amid volatile price fluctuations in the California electric markets last year, the Commission launched a series of strong initiatives designed to remedy the serious problems affecting the California markets.

In August 2000, the Commission ordered an investigation and hearing into rates for energy and ancillary services of sellers into the California Power Exchange (PX) and Independent System Operator (ISO) spot markets. The PX was the scheduling coordinator for California's investor-owned utilities as well as other market participants.

Following a staff investigation that found the market structure and rules for wholesale sales of electric energy in California to be "seriously flawed," the Commission issued a series of orders to bring stability to the markets. In December 2000, the Commission established guidelines to remedy the faltering markets, including ending the PX's buy/sell requirement and calling for the establishment of a prospective price mitigation plan. The Commission also cited the fundamental need to reduce the market participants' reliance on spot markets, which tend to be more volatile, and directed the participants to enter into longer-term contracts.

Today's order addresses rehearing and clarification requests for the Commission's August 23, November 1, December 8 and December 15, 2000 orders along with its March 9, June 19, and July 25, 2001 refund and price mitigation orders.

In its changes and clarifications, the Commission:

- states that governmental sellers (federal and municipal utilities) and Rural Utilities Service-financed cooperatives are excluded from price mitigation as it applies to bilateral transactions outside the ISO spot markets and also with the must-offer requirement outside California.
- eliminates the underscheduling penalty that was established in the December 15 order.
- provides an opportunity for marketers, load-serving entities and hydroelectric units selling in the California ISO and PX spot markets, to submit evidence that the refund methodology results in a total revenue shortfall for their transactions; this applies during the refund period, after the refund hearing is concluded.
- clarifies that generators subject to the must-offer requirement should be able to recover their costs for complying with the ISO's instructions to keep their units at minimum load status and directs the ISO to pay these costs, regardless of whether the ISO buys the power.
- clarifies that units operating outside California may set the mitigated market clearing price.
- clarifies that the mitigated market clearing price is to be set by the proxy price of the last unit dispatched, rather than the lower of the proxy price or the actual bid of the marginal unit.

In a related but separate order, the Commission altered the price mitigation methodology for spot market transactions for the west-wide market for the winter season (Docket No. EL01-68-000). This recalculation, designed to help the west through the winter season, will bring continued price stability and balance to the western markets, the Commission said, since the area the ISO serves is a summer peaking system and a large area of the 11-state Western Systems Coordinating Council (WSCC), especially the Northwest, consists of winter peaking systems. The change, which extends from the date of this order through April 30, 2002, is triggered when the average of three gas indices increases 10 percent from the level last used to calculate the mitigated price. Today's order addresses issues raised as a result of a June order in which the Commission adopted a mitigation plan for the California ISO's organized spot market sales, as well as for bilateral spot market sales throughout the WSSC region.

QUESTIONS AND ANSWERS

Q. What comprises the price mitigation in effect in the ISO spot markets in California under the Commission’s previous orders?

A. Current price mitigation measures use a single market clearing price derived from must-offer and marginal cost bidding requirements for hours of reserve deficiency (when reserves are below 7 percent) in California's organized spot markets. Generators submit bids that are no higher than their marginal costs, including the cost to replace gas used for generation, and marketers bid as price takers. The mitigated market clearing price is based on the marginal cost of the least efficient unit dispatched in the ISO's real-time market, using that unit's heat rate, the average of the mid-point of the monthly bid-week prices reported for SoCal Gas (large packages), Malin, and PG&E city-gate, and a $6/MWh O&M adder. Bidders invoice the ISO directly for the cost to comply with emissions requirements and for start-up fuel costs. For sales during non-reserve deficiency hours (when reserves exceed 7 percent), the market may clear at no higher than 85 percent of the highest ISO hourly market clearing price established during the hours when the last reserve deficiency was in effect. Sellers other than marketers may seek to justify bids above the mitigated prices. A 10 percent creditworthiness adder is included as a surcharge on market clearing prices.

All non-hydropower generators selling through the ISO's markets must offer all of their capacity in real-time if it is available and not already scheduled to run. The price mitigation and must-offer obligations apply to all public utilities as well as to governmental entities and cooperatives not otherwise subject to Commission rate regulation.

Q. What comprises the price mitigation in effect in the rest of the Western Systems Coordinating Council (WSCC) under the Commission's previous orders?

A. For spot sales outside the ISO's single price auctions, the mitigated prices apply as a maximum price and sellers can receive the prices they negotiate up to those maximum prices. All sellers with the exception of marketers and hydroelectric resources must offer their capacity that is available and not already scheduled to run in WSCC spot markets. The creditworthiness adder is not paid for these transactions.

Q. Does the refund methodology being used in the hearing proceeding before Administrative Law Judge Birchman differ from the price mitigation method?

A. Yes, in these respects: (1) The Commission held in the July 25 refund Order that gas costs for past periods should be determined by using the daily spot market price for gas, rather than the monthly bid-week prices used for prospective mitigation in the June 19 Order. The Commission also separated the state's gas market into northern and southern zones, applying a northern and southern gas cost depending on whether the marginal unit is located in northern or southern California; and (2) suppliers may net their demonstrable emissions costs from their refund liability (as opposed to invoicing the ISO for them).

Q. How does this rehearing order modify the existing price mitigation and refund formula?

A. The rehearing order grants rehearing of the previous orders in four respects:
1) it departs from the June 19 Order to exclude governmental entities and cooperatives (referred to as "non-public utilities" in that order) from price mitigation with respect to bilateral transactions outside of the ISO spot markets, and with respect to the must-offer requirement outside of California. See section E.10. It retains price mitigation and potential refunds for governmental entities and cooperatives that sell through the ISO.

2) it eliminates the underscheduling penalty that was instituted in the December 15 Order. See section C.2.

3) it grants rehearing to modify the way the mitigated market clearing price is calculated to apply the "North" gas cost index to the unit in the North with the highest heat rate, and apply the "South" gas cost index to the unit in the South with the highest heat rate; whichever unit has the highest total costs will then serve as the system-wide marginal, market clearing unit. See section B.2.a.

4) it provides an opportunity for marketers, load serving entities, and hydro units to submit evidence after the conclusion of the refund hearing that the refund methodology results in a total revenue shortfall in the California ISO and PX spot markets for their transactions during the refund period. See sections B.1.c. and F.

Also, the rehearing order reflects two modifications discussed in the related

compliance order, to be issued concurrently with the rehearing order (E-35). First, the compliance order clarifies that generators subject to the must-offer requirement should be able to recover their costs for complying with the ISO's instructions to keep their units at minimum load status, and directs the ISO to pay these costs. See section E.2.a. of the rehearing order. Second, the compliance order clarifies that a system emergency should be triggered by reaching a 7 percent reserve deficiency, not when the ISO calls a Stage 1 emergency. See section E.8.

In addition, the rehearing order clarifies several significant aspects of existing price mitigation. First, it clarifies that the mitigated market clearing price is to be set by the proxy price of the last unit dispatched, rather than the lower of the proxy price or the actual bid of the marginal unit. See section B.2.a. Second, it clarifies that units operating outside of California may set the mitigated market clearing price. See section B.2.a. Third, it clarifies that subsequent changes in the mitigated market clearing prices will not impact prices settled the day or hour ahead in Ancillary Services markets. See section B.2.g. (This is also discussed in the related compliance order that is being issued concurrently with the rehearing order. See section E.3. of the compliance order.) Fourth, the rehearing order clarifies that, as price takers, marketers and load serving entities that choose to participate in the real-time spot market must bid at $0/MWh. See section B.1.c.

Q. What action does the rehearing order take with respect to governance of the ISO and the independence of the organization?

A. The rehearing order does not act on governance issues. See sections C.4. and E.8.

Q. How does the rehearing order resolve related issues for the Pacific Northwest raised in Puget Sound's complaint?

A. The rehearing order does not act at this time on the Pacific Northwest complaint (Docket No. EL01-10-000). See section G.