Organization of MISO States

ORGANIZATION OF MISO STATES, INC.
Special Board of Directors Meeting
Conference Call Minutes
March 24, 2008

Approved April 10, 2008

Dan Ebert, Vice President of the Organization of MISO States, Inc. (OMS), called the March 24, 2008 Meeting of the OMS Board of Directors to order via conference call at approximately 1:00 p.m. (CDT). The following board members or their proxies participated in the meeting:

Randy Rismiller, Proxy for Bob Lieberman, Illinois
Greg Server, Indiana
Jeff Kaman, proxy for John Norris, Iowa
Rick Bertelson, proxy for Mark David Goss, Kentucky
Monica Martinez, Michigan
Burl Haar, proxy for Tom Pugh, Minnesota
Mike Proctor, proxy for Jeff Davis, Missouri
Greg Jergeson, Montana
Tim Texel, proxy for Eugene Bade, Nebraska
Susan Wefald, North Dakota
Kim Wissman, proxy for Valerie Lemmie, Ohio
Dan Ebert, Wisconsin

Absent
Manitoba
Pennsylvania
South Dakota

Agency members participating
Jack Dwyer – Iowa
Robb Mork – Indiana
Bill Bokram - Michigan
Mark Johnson – Minnesota
Brian Dekiep, Bryan Baldwin - Montana
Dorothea Hives – Ohio
Jerry Lein – North Dakota
Randel Pilo, Jim Wottreng – Wisconsin

Others on the call
Bill Smith, Julie Mitchell – OMS Staff

The directors and proxies listed above established the necessary quorum for the meeting of at least eight directors being present.

BUSINESS

1. **Comments approved on MISO's Real-Time RSG Redesign –** Bill Bokram

Bill Bokram, OMS Market WG co-chair, offered the following introduction and background on the draft comments prepared by Jim Wottreng of the Markets Work Group and distributed to the OMS directors for consideration today.

- The draft OMS comments address MISO's proposed alternative mechanism for allocating real-time Revenue Sufficiency Guarantee (RSG) charges and costs.
- The comments summarize RSG history since 2005, then comment on four issues: 1. The potential for the current proposal to provide the wrong incentives, 2. The current proposal is unfinished and will require too much time to implement to address immediate problems, 3. The need for a less complex and less costly method to be used now while continuing to develop the current proposal, and 4. The need for a timeframe that MISO will use to develop long-term solutions towards reducing RSG charges.
- The comments also state that the assumption that FERC will fix the rate and charge volume mismatch discussed in OMS' protest filed with the FERC on December 19th, 2007.
- Wisconsin Staffer Jim Wottreng, the OMS RSG expert was also on the phone to help answer any questions the directors may have had. The comments are due to be filed at FERC on March 24th.

After some discussion, and with clarifying language offered by Mike Proctor and a footnote by Susan Wefald inserted, a motion was made by Monica Martinez to accept the comments as amended. Greg Server seconded the motion.

Vice President Ebert asked for a roll call vote to be taken concerning the motion to adopt the comments and file with FERC:

Illinois - Abstain
Indiana - Yes
Iowa - Yes
Kentucky - Abstain
Manitoba - ABSENT
Michigan - Yes
Minnesota - Yes
Missouri - Yes
Montana - Yes
Nebraska - Yes
North Dakota - Yes
Ohio - Yes
Pennsylvania - ABSENT
South Dakota - ABSENT
Wisconsin – Yes

Yes, file comment= 10
No, do not file = 0
Abstain = 2
Absent = 3

The motion carried by a majority of the directors present. Associate members present on the conference call asking to be cited in support of the comments included: Indiana Office of Utility Consumer Counselor, Minnesota Office of Energy Security, Iowa Office of Consumer Advocate.

2. **Request for rehearing of FERC's February 25, 2008 Order on MISO's ASM proposal –** Bill Bokram – Market WG Co-Chair
   Bill Bokram, credited the Market WG, and co-chair Christine Ericson for their work effort on this document and the previous one. The following is the overview of the OMS request for rehearing Bill presented to the OMS directors:
   - The draft OMS request for rehearing addressed the single issue of determining generating unit reference levels and their oversight by the independent market monitor. The pleading recalls OMS concern about the need for effective mitigation to address the exercise of market power in MISO's Ancillary Services Markets, and OMS' concern about the lack of a formalized approach for setting the reference prices used in mitigation. The pleading notes that FERC's February 25th order did not address these concerns, but instead approved a process that gives the Independent Market Monitor too much discretion and produces reference prices that suffer from lack transparency, vagueness, and lack of oversight. The pleading urges FERC to grant rehearing and require a formalized reference price process that includes states in the review process.
   - The pleading is consistent with the OMS comments filed previously on ASM.
   - This pleading MUST be filed within 30 days of FERC's February 25th over, so it must be filed by Wednesday, March 26th.

A motion was made by Susan Wefald to accept the request for rehearing order as distributed. Kim Wissman seconded the motion.

Vice President Ebert asked for a roll call vote to be taken concerning the motion to adopt the request for rehearing on MISO's ASM order and file with FERC:

Illinois - Abstain
Indiana - Yes
Iowa - Yes
Kentucky - Yes
Manitoba - ABSENT
Michigan - Yes
Minnesota - Yes
Missouri - Yes
Montana - Yes
Nebraska - Abstain
North Dakota - Yes
Ohio - Yes
Pennsylvania - ABSENT
South Dakota - ABSENT
Wisconsin – Yes

Yes, file comment= 10
No, do not file = 0
Abstain = 2
Absent =3

The motion carried by a majority of the directors present. Associate members present on the conference call asking to be cited in support of the comments included: Indiana Office of Utility Consumer Counselor, Minnesota Office of Energy Security, Iowa Office of Consumer Advocate.

The meeting adjourned at 1:40 p.m. CDT

OMS Special BOD meeting Monday, 3/24/08

1. Comments on MISO's Real-Time RSG Redesign, EL07-86 et al filed 3/3/08

The draft OMS comments before you address MISO's proposed alternative mechanism for allocating real-time Revenue Sufficiency Guarantee (RSG) charges and costs.

The comments summarize RSG history since 2005, then comment on four issues: 1. The potential for the current proposal to provide the wrong incentives, 2. The current proposal is unfinished and will require too much time to implement to address immediate problems, 3. The need for a less complex and less costly method to be used now while continuing to develop the current proposal, and 4. The need for a timeframe that MISO will use to develop long-term solutions towards reducing RSG charges. The comments also state that the assumption that FERC will fix the rate and charge volume mismatch discussed in OMS' protest filed with the FERC on December 19th, 2007.

Wisconsin Staffer Jim Wottreng, the OMS RSG expert that you have heard from in prior OMS Board meeting, is also on the phone to help answer any questions that you may have. The comments are due to be filed at FERC on the 24th, today.

2. Request for rehearing of FERC's 2/25/08 Order on MISO's ASM proposal

The draft OMS request for rehearing before you addresses the single issue of determining generating unit reference levels and their oversight by the independent market monitor. The pleading recalls OMS concern about the need for effective mitigation to address the exercise of market power in MISO's Ancillary Services Markets, and OMS' concern about the lack of a formalized approach for setting the reference prices used in mitigation. The pleading notes that FERC's February 25th order did not address these concerns, but instead approved a process that gives the Independent Market Monitor too much discretion and produces reference prices that suffer from lack transparency, vagueness, and lack of oversight. The pleading urges FERC to grant rehearing and require a formalized reference price process that includes states in the review process.
The pleading is consistent with the OMS comments filed previously on ASM.

This pleading MUST be filed within 30 days of FERC's February 25th over, so it must be filed by this Wednesday, March 26th.

W. Bokram
3/21/08

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Midwest Independent	**)**	**Docket No. ER07-1372-000**
System Operator	**)**	**Docket No. ER07-1372-001**

REQUEST FOR REHEARING
OF THE ORGANIZATION OF MISO STATES

Pursuant to Rule 713 of the rules and regulations of the Federal Energy Regulatory Commission (Commission), 18 C.F.R. § 385.713, the Organization of MISO States (OMS) respectfully submits this Request for Rehearing of the Commission's February 25, 2008 Order on Ancillary Services Filing in the above captioned docket.[1]

I. SPECIFICATION OF COMMISSION ERROR

The Commission erred in: (1) not establishing a more transparent and more rigorous process for determining generating unit reference levels; and (2) not establishing a mechanism for oversight of both the reference price-setting process and the review of reference price levels accepted by the Midwest ISO independent market monitor (IMM).[2] The reference price-setting process accepted by the Commission in the February 25 Order provides undue discretion to the IMM in establishing the reference level, which is the key element in assessing whether sellers exercise market power in the Midwest ISO ancillary services market. Accordingly, mechanisms should be developed whereby the Commission would have a significant role in overseeing the reference price-setting process and whereby the Commission and state commissions would have an opportunity to review the reference prices determined by the IMM.

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[1] *Midwest Independent Transmission System Operator, Inc.* 122 FERC ¶ 61,172 (2008) (February 25 Order)
[2] *See e.g.*, February 25 Order at PP 124-155.

II. LIST OF ISSUES

Do the weaknesses in the reference price-setting process contained in Section 64.1.4 of the Midwest ISO's tariff render the resulting reference prices unjust, unreasonable, or unduly discriminatory under Section 205 of the Federal Power Act?

III. ARGUMENT

A. Review of the OMS Comments in this Proceeding.

In each of its various Comments to the Commission in this proceeding, the OMS expressed concerns about the Midwest ISO proposed reference price determination process and urged the Commission to require "effective mitigation to address the exercise of market power."[3] Specifically, the OMS stated,

> In this regard, the OMS has three concerns. The first concern is related to the accuracy of establishing a reference price for each generating unit. Dr. Patton's Affidavit does not include a comprehensive discussion as to how he intends to assess the accuracy and reliability of a submitted reference price. The OMS recommends that Dr. Patton develop a formalized approach for evaluating the accuracy and appropriateness of a submitted reference price and report the results to the Commission and the OMS.[4]

and,

> …the reference levels must reflect true marginal cost of service, so the Commission should in this docket make clear to the Midwest ISO and the IMM the proper way to calculate the reference levels and put that method in the tariff.[5]

With respect to uncertainty in the factors affecting marginal cost and the acceptable threshold over the reference price, the OMS observed that,

> Dr. Patton and Dr. Lawrence Kirsch, an economist who appeared on behalf of the Midwest TDUs, concurred that in standard microeconomic theory, if there were

[3] Comments of the Organization of Midwest ISO States and Notice of Intervention (October 15, 2007), at 2.
[4] Comments of the Organization of Midwest ISO States and Notice of Intervention (October 15, 2007), at 8.
[5] Reply Comments of the Organization of Midwest ISO States Following Technical Conference, (January 11, 2008) at 2.

> no uncertainty over the factors affecting marginal costs, the adder over reference levels for market power monitoring purposes would in fact be zero.[6]

and,

> …the very start up of a new market, given the market power measures identified forth [sic] by the IMM, implies a certainty that, without effective market monitoring, the whole ASM, in its design and operation, could lead to non-competitive outcomes.[7]

The above statements clearly illustrate that the OMS holds strong concerns about the possible exercise of market power in the Midwest ISO's new ancillary services market. The OMS expressed particular concern about the absence of a formalized approach for evaluating the accuracy and appropriateness of the accepted reference prices and a concern that, under the Midwest ISO proposed process, the accepted reference prices might not reflect the true marginal cost for generating units. In light of those concerns, the OMS recommended action by the Commission in overseeing the reference price-setting process and an opportunity for the Commission and state commissions to review the reference prices established by the IMM.[8]

The Commission did not address the OMS concerns and recommendations in this regard in the February 25 Order.

B. Review of the Commission's February 25 Decision.

In the February 25 Order, the Commission did not address the OMS concerns on this issue and accepted the Midwest ISO proposed method of determining reference levels with only minor changes not relevant to the issue here.[9]

The Commission observed that, under the Midwest ISO proposal, reference levels will be based upon estimates of a generator's marginal costs, including legitimate risks and opportunity

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[6] Comments of the Organization of Midwest ISO States Following Technical Conference (December 19, 2007), at 2.
[7] Comments of the Organization of Midwest ISO States Following Technical Conference (December 19, 2007), at 3.
[8] Comments of the Organization of Midwest ISO States and Notice of Intervention (October 15, 2007), at 8.
[9] February 25 Order at P 137.

costs.[10] The Commission noted that the tariff sets forth three methods (in order of application) for calculating a unit's reference levels: (1) offer-based, (2) price-based, and (3) consultative.[11] The Commission noted that, when the Midwest ISO ancillary services market begins, "there will be no history of accepted offers or market clearing prices."[12] Therefore, for at least the first ninety days of operation of the new Midwest ISO ancillary services market, the "consultative" process will be used to establish each generating unit's reference price.

C. Review of the Consultative Process for Establishing Reference Prices.

The consultative process by which the reference price will be established between the generators and the IMM is set forth in its entirety in Section 64.1.4.iii of the Midwest ISO tariff which describes the process as follows:

> **iii.** A level determined in consultation with the Market Participant submitting the Offer or Offers at issue and intended to reflect a unit's marginal costs, including legitimate risks and opportunity costs, or justifiable technical characteristics for physical Offer parameters, provided such consultation has occurred prior to the occurrence of the conduct being examined. Such consultation may be initiated by either the IMM or the Market Participant.[13]

Section 64.1.4.e of the Midwest ISO tariff provides a mechanism that a generator may use to get its IMM-determined reference price modified when it is not satisfied. Section 64.1.4.e states,

> **e.** Upon request by a Market Participant or at the initiative of the IMM, the IMM shall consult with a Market Participant with respect to the Reference Levels determined for that Market Participant. If cost data or other information submitted by a Market Participant indicates to the satisfaction of the IMM that the Reference Levels for that Market Participant should be changed, revised Reference Levels shall be determined, communicated to the Market Participant, and implemented, as soon as practicable. The IMM shall provide a written explanation of its determination to the Market Participant upon request.[14]

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[10] February 25 Order at P 124.
[11] February 25 Order at P 124.
[12] February 25 Order at P 125.
[13] Midwest ISO tariff Section 64.1.4.iii.
[14] Midwest ISO tariff Section 64.1.4.e.

D. Lack of Transparency, Vagueness, and Lack of Oversight in the Reference Price-Setting Process Add Up to Undue Discretion for the IMM.

These quoted sections of the Midwest ISO tariff show that the consultative process for establishing generating units' reference prices will be a non-transparent process available only to the generating company and the IMM. There are no constraints or instructions in the tariff on what information a generating company can submit to the IMM in support of the company's proposed reference level. Furthermore, there are no specified benchmarks in the tariff for the IMM to use in assessing whether the generator's proposed reference price is an accurate representation of each generating unit's marginal cost—other than the general admonition that the IMM must allow "legitimate risks and opportunity costs."

The lack of specified benchmarks in the Midwest ISO tariff concerning the information submitted by generators in support of their proposed reference levels causes concern, as there are no established mechanisms for the Commission to oversee the reference price-setting process or opportunities for a state commission to review the IMM's decisions concerning the setting of generator reference prices.

Not only does the Midwest ISO tariff not contain any specified benchmarks to guide the consultative process for determining reference prices, the Midwest ISO tariff does not even define the terms that might create a framework and establish boundaries necessary for the process to work properly. For example, while the Midwest ISO tariff requires the IMM to include "legitimate risks and opportunity costs" in the determination of reference prices, the tariff does not define those terms.[15] Indeed, the tariff definition of the term "Reference Levels" is so general as to provide

[15] "Lost Opportunity Cost" is defined in Section 1.176a of the Tariff as: "The LMP revenues that were not realized relative to a theoretical future operating point." However, that does not seem particularly relevant to the way that the term "opportunity cost" is used in Section 64.1.4.iii.

no additional illumination to the process. Specifically, Section 1.259 of the Midwest ISO tariff defines "Reference Levels" as follows:

> **1.259 Reference Levels:** In the context of Module D, calculations intended to reflect a Resource's marginal costs, including legitimate risk and opportunity costs.

In other contexts, the Commission has expressed great concern for transparency of regional transmission organization operations. For example, in the February 25 Order, the Commission expressed concern with the lack of transparency in the Midwest ISO proposed process for the auditing of physical withholding by generating companies and took steps to remedy that lack of transparency.[16] However, the consultative process set forth in Section 64.1.4.iii of the Midwest ISO tariff that the IMM and the generating companies will use to establish critically important reference price levels is entirely non-transparent. The Commission stated in the February 25 Order that "transparency is important to build market participants' confidence in the fairness of the [ ] process and prevent undue discretion by the IMM."[17] Yet, the Commission took no steps to improve transparency in the reference price-setting process.

The lack of transparency, vagueness, and lack of oversight in the Midwest ISO's proposed reference price-setting process allows too much leeway for generating companies and could result in the IMM exercising undue discretion. Why the Commission took no action to address undue IMM discretion in this critical area is especially puzzling, as in other contexts, the Commission has expressed great concern that the IMM not be permitted to exercise too much discretion. Indeed, elsewhere in the February 25 Order, the Commission concluded that the Midwest ISO proposal

[16] February 25 Order at P 151.
[17] February 25 Order at P 151.

allowed the IMM too much discretion and took steps to reduce the IMM's discretion.[18] Preventing undue IMM discretion in the process for determining generating unit reference levels is no less important, and is arguably much more important, than preventing undue IMM discretion in the "fair game" assessment process or the process of auditing generating companies for physical withholding.

The lack of transparency, vagueness, and lack of oversight in the reference price-setting process, all of which together create an environment in which the generating companies may not be properly restrained and the IMM may exercise undue discretion, is very troubling. It is especially troubling given that, for at least the first ninety days of operation of the new Midwest ISO ancillary services market, the "consultative" process will be the only process that is used to establish each generating unit's reference price. Because the reference price is the base on which the IMM will apply the conduct and impact tests to assess whether a generator is exercising market power, the reference price-setting process must be improved. The Commission should not permit vagueness, lack of transparency and lack of oversight in a process as important as the reference price-setting process.

This concern about the reference setting process is not limited to the consultative method. The offer-based method and the price-based method of setting the reference price also exhibit vagueness, lack of transparency and lack of oversight. However, the weaknesses in the consultative process are particularly notable and those weaknesses will be magnified because the consultative process will be in place for the critical first ninety days of operation of the Midwest ISO ancillary services market.

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[18] *See, e.g.*, February 25 Order at P 122 concerning the IMM's assessment of "fair game" behavior, and February 25 Order at P 151 concerning the IMM's audits of physical withholding.

E. State Regulators, and Their Regional State Committee--the OMS--Can Serve a Useful Role in Reviewing the Reference Price-Setting Process and the IMM's Reference Price Level Determinations.

In its Comments in this proceeding, the OMS advocated the development of "a formalized approach for evaluating the accuracy and appropriateness of a submitted reference price."[19] The OMS recommended that the IMM be required to report the results of the reference price determination process to "the Commission and the OMS."[20] Those recommendations were sound, but were not addressed or acted on in the Commission's February 25 Order. We reiterate those recommendations here and urge the Commission to promptly implement them.

State regulators have extensive historical experience and considerable expertise in assessing and determining energy companies' prudent costs. The Commission would do well to make use of state regulators' extensive historical experience and considerable expertise in reviewing the reference price-setting process which involves many of the same skill-sets as are involved in the more traditional cost determination processes that state regulators know well. State regulators also have a significant interest in the establishment of accurate reference prices, as improperly inflated reference prices can lead to improperly inflated locational marginal prices that are paid by retail customers and improperly deflated reference prices could affect generator revenues that could lead to resource adequacy issues. State regulators are unbiased and act in pursuit of the public interest. Thus, state regulators are particularly well-suited to play a role in reviewing the reference price-setting process and the reference prices established by the IMM. This role should be designed to constitute the "formalized approach for evaluating the accuracy

[19] Comments of the Organization of Midwest ISO States and Notice of Intervention (October 15, 2007), at 8
[20] Comments of the Organization of Midwest ISO States and Notice of Intervention (October 15, 2007), at 8

and appropriateness of a submitted reference price" which was previously recommended in OMS Comments.[21]

The OMS also previously recommended that the IMM be required to report the results of the reference price determination process to "the Commission and the OMS."[22] Since the data involved in the reference price-setting process will be both commercially sensitive and market sensitive, the utmost care must be taken in handling such data. State regulators have long experience in properly handling such highly confidential data. However, the currently-effective data access provisions of the Midwest ISO's tariff effectively limit the ability of many state commissions to receive or view data such as that underlying generating unit reference price levels or even the IMM-determined reference price. In order to improve the current absence of oversight over the IMM's reference price setting decisions and to reduce the undue discretion of the IMM in that process, the Midwest ISO's policy that limits state regulators' access to confidential IMM data must be modified.[23]

IV. CONCLUSION

Wherefore, for all of the reasons explained above, the OMS recommends and requests that the Commission rehear its decisions in the February 25 Order regarding establishment of generator reference prices. As explained above, the Midwest ISO's proposed process for establishing reference prices suffers from lack of transparency, vagueness, and lack of oversight. The Commission must address the unrestrained flexibility that the Midwest ISO tariff provides to the generating companies and the undue discretion that the Midwest ISO tariff provides to the IMM regarding the reference price-setting process. To remedy these flaws, more specificity

[21] Comments of the Organization of Midwest ISO States and Notice of Intervention (October 15, 2007), at 8.
[22] Comments of the Organization of Midwest ISO States and Notice of Intervention (October 15, 2007), at 8 .
[23] Without needed data, state commissions are unable to effectively exercise their legitimate Federal Power Act Section 206 complaint rights regarding IMM-determined reference prices.

must be injected into the process of establishing reference prices and a role should be created for state regulators in reviewing the reference price-setting process and the reference prices established by the IMM. The OMS further requests any and all other appropriate relief.

The OMS submits these comments because a majority of the members have agreed to generally support them. The following members generally support these comments. Individual OMS members reserve the right to file separate comments regarding the issues discussed in these comments:

Illinois Commerce Commission
Indiana Utility Regulatory Commission
Iowa Utilities Board
Kentucky Public Service Commission
Michigan Public Service Commission
Minnesota Public Utilities Commission
Missouri Public Service Commission
Montana Public Service Commission
North Dakota Public Service Commission
Public Utilities Commission of Ohio
Wisconsin Public Service Commission

The Manitoba Public Utilities Board, the Pennsylvania Public Utility Commission, and the South Dakota Public Utilities Commission did not participate in this pleading. The Nebraska Power Review Board abstained from this pleading.

The Indiana Office of Utility Consumer Counselor, the Iowa Office of Consumer Advocate and the Minnesota Office of Energy Security,[24] as associate members of the OMS, participated in these comments and generally support these comments.

Respectfully Submitted,
William H. Smith, Jr.
William H. Smith, Jr.
Executive Director

[24] The Minnesota Office of Energy Security now exercises the consumer advocacy functions previously performed by the Minnesota Department of Commerce.

Organization of Midwest ISO States
100 Court Avenue, Suite 218
Des Moines, Iowa 50309
Tel: 515-243-0742

Dated: March 24, 2008

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Des Moines, Iowa, this 24th day of March, 2008.

William H. Smith, Jr.

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Ameren Services Company and Northern Indiana Public Service Company Complainant v. Midwest Independent System Operator, Inc., Respondent	Docket Nos.	EL07-86-003
Great Lakes Utilities, et al. Complainant v. Midwest Independent System Operator, Inc., Respondent		EL07-88-003
Wabash Valley Power Assoc., Inc. Complainant v. Midwest Independent System Operator, Inc., Respondent		EL07-92-003
E.ON. U.S. LLC Complainant v. Midwest Independent System Operator, Inc., Respondent		EL07-100-002

COMMENTS OF THE ORGANIZATION OF MISO STATES
AND NOTICE OF INTERVENTION

I. Introduction

On March 3, 2008, the Midwest Independent System Operator, Inc. ("Midwest ISO" or "MISO") filed revisions to its Open Access Transmission, Energy and Operating Reserve Markets Tariff reflecting an alternative mechanism for allocating real-time Revenue Sufficiency Guarantee ("RSG") charges and costs.

On March 10, 2008, the Commission issued a notice of the March 3 filing and set March 24, 2008, as the deadline for comment and protest.

As discussed in greater detail below, the Organization of MISO States ("OMS") respectfully offers the following comments for Commission consideration:

1. The proposed alternative RSG cost allocation methodology contains flaws that could send the wrong incentives.
2. As proposed, the alternative RSG cost allocation methodology is a work product that is unfinished and that will require too much time to implement to address immediate problems.
3. A less complex and less costly method for allocating RSG costs may be warranted initially and immediately, but the proposed methodology should continue to be developed with the stakeholders.
4. A definitive ordered timeframe on the long term RSG solutions that the Midwest ISO is currently studying is useful and necessary to communicate its commitment.

An underlying assumption of the OMS comments is that the RSG rate and charge volume mismatch will be rectified in conformity with the Commission's recent determinations, specifically, that the volumes used to determine the RSG rate be the same volumes that will be charged that RSG rate and that to the extent the Midwest ISO has been in error in its interpretation of the currently effective RSG charge and rate, refunds will be required.[1, 2]

II. Notice of Intervention

Pursuant to Rule 214(a)(2) of the Federal Energy Regulatory Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214(a)(2), the Organization of MISO States ("OMS")

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[1] *Midwest Independent Transmission System Operator, Inc*., 121 ¶ 61,132 (2007) at P 26, and *Ameren, et al. v. Midwest Independent Transmission System Operator, Inc*., 121 ¶ 61,205 (2007) at P 86.
[2] The North Dakota PSC and the Montana PSC do not support refunds or resettlements for periods prior to the potential refund effective date of August 10, 2007, established by the Commission in Docket Nos. EL07-86-000, EL07-88-000 and EL07-92-000.

files its Notice of Intervention in the above-captioned proceedings. Service of all pleadings, documents, and communications in this matter should be made on the following:

> William H. Smith, Jr., Executive Director
> Organization of MISO States
> 100 Court Avenue, Suite 218
> Des Moines, Iowa 50309
> e-mail: bill@misostates.org

III. Background

To ensure that adequate supply is available to meet real-time demand, resources that are made available as a result of the Reliability Assessment Commitment ("RAC") process receive compensation at least equal to their start-up offers, no-load offers, and incremental energy costs, even if the resources are not dispatched. When real-time Locational Marginal Prices ("LMP") are not sufficient to fully compensate resources to this minimum reimbursement level, they receive a real-time Revenue Sufficiency Guarantee ("RSG") make whole payment for the shortfall.

The real-time RSG make whole payments are funded primarily by RSG charges for real-time deviations from day-ahead schedules. Section 40.3.3.a.ii of the Midwest ISO Transmission and Energy Markets Tariff (TEMT) describes the calculation of the RSG charges:

> On any Day when a Market Participant actually withdraws any Energy the Market Participant shall be charged a Real-Time revenue sufficiency guarantee charge. The Market Participant's Real-Time revenue sufficiency guarantee charge for that Hour shall equal the product of: (i) the Market Participant's total Load purchased in the Real-Time Energy Market during the Operating Day (in MWh), all Virtual Supply for the Market Participant in the Day-Ahead Energy Market, and Resource Uninstructed Deviation quantities (MWh), and (ii) the per unit Real-Time revenue sufficiency guarantee charge. The per unit Real-Time revenue sufficiency guarantee charge for any given Day shall equal:(i) the aggregate Real-Time revenue sufficiency guarantee charge in that Hour attributed to Resources committed in any RAC processes conducted in the Operating Day divided by (ii) the sum of the total uncovered Load withdrawn in the Operating Day (in MWh), all Virtual Supply for that Market Participant in the Day-Ahead Energy Market,

> and for deviations from Dispatch Instructions, of all Market Participants withdrawing during that Hour for the Operating Day.[3]

To the extent that the RSG make whole payments are not fully funded by RSG charges, they are uplifted to market participants based on load ratio share.

On October 27, 2005, the Midwest ISO submitted proposed revisions to the TEMT. One of the proposed revisions was to remove references to virtual supply from the provisions related to the calculation of RSG charges in section 40.3.3 of the TEMT.[4] (Virtual supply is an offer to sell energy in the day-ahead market that is not supported by a physical injection or reduction in withdrawals or commitment by a resource). In the RSG Order issued on April 25, 2006, the Commission determined that virtual supply can cause RSG costs and rejected the Midwest ISO's proposal to eliminate entirely virtual supply transactions from real-time RSG charges.[5]

In the RSG Rehearing Order issued on October 26, 2006, the Commission reaffirmed its determination that virtual supply offers accepted in the day-ahead market can require the commitment of physical resources in the RAC process, which may cause RSG costs to be incurred.[6] To ensure that cost responsibility follows cost incurrence, the Commission required the Midwest ISO to propose a charge that assesses RSG costs to virtual supply offers based on the RSG costs they cause.[7]

The Midwest ISO then proposed in its compliance filing to allocate RSG costs in each hour to two buckets; a net virtual bucket (netting virtual demand bids against virtual supply offers) and a net deviations bucket.[8] In the Compliance Order issued on March 15, 2007, the Commission noted that the Midwest ISO failed to provide the requested analysis and provided no

[3] Midwest ISO Transmission and Energy Markets Tariff, Module C, section 40.3.3.a.ii, Second Revised Sheet Nos. 577-578.
[4] *Midwest Independent Transmission System Operator, Inc*., 115 ¶ 61,108 (2006) (RSG Order) at P 3-4.
[5] RSG Order at P 48.
[6] *Midwest Independent Transmission System Operator, Inc*., 117 ¶ 61,113 (2006) (RSG Rehearing Order) at P 108.
[7] RSG Rehearing Order at P. 117.
[8] *Midwest Independent Transmission System Operator, Inc*., 118 ¶ 61,213 (2007) (Compliance Order) at P 43.

evidence to support its proposal.[9] Unable to determine that the proposal was based on cost causation and would not result in unjust and unreasonable rates, the Commission rejected the proposal and directed the Midwest ISO to submit a new compliance filing. [10]

In the Order on Rehearing, also issued on March 15, 2007, the Commission, in its discussion of the Section 40.3.3.a.ii TEMT phrase "actually withdraws any Energy" stated:

> We do not find the calculation of the charge to be arbitrary or unduly discriminatory, since the end-result of the charge does not result in any harm. We agree that the charge is assessed only on market participants withdrawing energy in real-time and payment of the charge may result in less than full recovery of RSG costs since the divisor to the charge includes all virtual supply – not just virtual supply offered by market participants withdrawing energy -- and therefore may result in under-recovery of RSG costs. However, to the extent that RSG costs are not fully recovered in the RSG charge, the unrecovered costs are recovered through uplift charges assessed to all market participants. While the assignment of costs to all market participants differs from the assignment of costs to only those entities causing the costs, the Commission is not, here in this section 205 proceeding, determining which of several possible allocations to implement. Rather, the currently-effective tariff provision – which was not challenged by any parties when accepted – cannot be revised in this proceeding and remains in effect until a section 206 investigation determines the current provision is unjust and unreasonable.[11]

Based on paragraph 58 of the Order on Rehearing, the Midwest ISO determined that "the real-time RSG rate calculation includes all Virtual Supply Offers that clear in the Day-Ahead Energy Market in the divisor to the charge."[12] On April 17, 2007, the Midwest ISO made its RSG compliance filing.

Subsequently, the Midwest ISO determined and published its estimate of the cost shift that would result from developing an RSG rate based on volumes that would not then be subject to the RSG charge. As a result of that volume mismatch, the Midwest ISO estimated that approximately 57 percent, and for some months more than 70 percent, of the real-time RSG cost

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[9] Compliance Order at P. 84.
[10] Compliance Order at P. 88 and order point (B).
[11] *Midwest Independent Transmission System Operator, Inc*., 118 ¶ 61,212 (2007) (Order on Rehearing) at P 58.
[12] "11a RSG Discussion Presentation - Final" presentation by the Midwest ISO to the Market Subcommittee on April 10, 2007, at http://www.midwestiso.org/publish/Document/4ad10b_1114b6b848b_-7f7e0a48324a?rev=9

would likely cross over to Revenue Neutrality Uplift and be collected from market participants based on load ratio share.[13] The estimated real-time RSG cost from market start through February 2007 totaled almost three quarters of a billion dollars.[14]

On August 10, 17 and 24, 2007, three Complaints were filed in Docket Nos. EL07-86-000, EL07-88-000, and EL07-92-000, respectively, requesting the Commission to find that Section 40.3.3.a.ii of the EMT is unjust and unreasonable to the extent it is construed to impose RSG charges only on Market Participants physically withdrawing energy from the Real-Time Energy Market. [15]

On November 5, 2007, the Commission issued an Order on Compliance Filing and provided clarification with respect to the RSG rate and charge calculations and stated:

> Based on our review of the Midwest ISO RSG charge and rate tariff provision, we provide the following clarification on the meaning of these provisions, to address Ameren's concerns. Per the terms of the tariff in the April 17 Filing, the denominator in the RSG rate in section 40.3.3.a.iii is based on the sum of the absolute values of the amounts in section 40.3.3.a.ii(a) – (d). We interpret this formulation to mean that the RSG rate denominator is the aggregate of the amounts for market participants withdrawing energy on that day, since they are entities being assessed the RSG charge in section 40.3.3.a.ii. Therefore, the amounts in the individual RSG charges in section 40.3.3.a.ii should sum to the same summed and aggregate number in the denominator of section 40.3.3.a.iii, thereby eliminating the possibility of developing the RSG charge and RSG rate on different bases and resulting in a shortfall in recovery of RSG costs.[16]

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[13] "RSG AWE Resettlement Results.xls" at http://www.midwestiso.org/publish/Document/193f68_1118e81057f_-7c540a48324a?rev=1

[14] *Id.*

[15] The three RSG complaints were filed on: (1) August 10, 2007, by Ameren Services Company, on behalf of certain of its affiliates (Ameren Energy Marketing Company, Union Electric Company d/b/a AmerenUE, Central Illinois Public Service Company d/b/a AmerenCIPS, Central Illinois Light Company d/b/a AmerenCILCO, and Illinois Power Company d/b/a AmerenIP – collectively, "Ameren"), and Northern Indiana Public Service Company ("NIPSCo"); (2) August 17, 2007, by Great Lakes Utilities ("GLU"), Indiana Municipal Power Agency ("IMPA"), Missouri Joint Municipal Electric Utility Commission ("MJMEUC"), Missouri River Energy Services ("MRES"), Prairie Power, Inc. ("PPI"), Southern Minnesota Municipal Power Agency ("SMMPA"), and Wisconsin Public Power Inc. ("WPPI") (collectively, "Midwest TDUs"); and (3) August 24, 2007, by Wabash Valley Power Association, Inc. ("Wabash Valley").

[16] *Midwest Independent Transmission System Operator, Inc*., 121 ¶ 61,132 (2007) at P 26.

The Commission directed the Midwest ISO to submit a compliance filing, pursuant to the requirements specified in the body of the order.[17]

On November 28, 2007, the Commission issued an Order on Complaints that consolidated the complaints of Ameren, et al, in Docket Nos. EL07-86-000, EL07-88-000, and EL07-92-000. In addition, the Commission:

1. Found that the Midwest ISO's existing RSG cost allocation methodology may be unjust, unreasonable, unduly discriminatory or preferential,
2. Instituted paper hearing procedures to review evidence regarding what would be a just and reasonable RSG cost allocation methodology, but held this paper hearing in abeyance pending the earlier of either the conclusion of the ongoing stakeholder proceeding, or February 1, 2008;
3. Directed the Midwest ISO to make an informational filing by February 1, 2008, reporting the results of the stakeholder discussion of an alternative RSG cost allocation methodology, and
4. Established a potential refund effective date of August 10, 2007. [18]

On February 1, 2008, the Midwest ISO submitted an Informational Filing describing the alternative real-time RSG cost allocation methodology that was being developed in the stakeholder proceedings.[19]

On March 3, 2008, the Midwest ISO filed revisions to its Open Access Transmission, Energy and Operating Reserve Markets Tariff reflecting the alternative mechanism for allocating real-time RSG charges and costs.

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[17] *Id.* at order point (B).
[18] *Ameren, et al. v. Midwest Independent Transmission System Operator, Inc*., 121 ¶ 61,205 (2007) at Order Points C, D, E, and G.
[19] Informational Filing at 7 - 12.

IV. Comments

1. The proposed alternative RSG cost allocation methodology contains flaws that could send the wrong incentives.

As the Midwest ISO states, one principle underlying an RSG cost allocation methodology should be incentives compatible with the day-ahead and real-time markets.[20] To the extent that an RSG cost allocation methodology does not have incentives compatible with the day-ahead and real-time markets it may result in individual actions taken to minimize individual costs that run counter to market actions that would otherwise optimize the market solution for the entire footprint.

The new proposal envisions, among other things, the creation of a notification and netting process. A notification deadline of four hours prior to the operating hour will be established, since that is the minimum advance time required by the Midwest ISO to take into account and reflect the schedule changes in the unit commitment process, also known as the RAC process. Notification to the Midwest ISO of a day-ahead schedule change prior to the notification deadline will allow a market participant to net such a schedule deviation with another eligible transaction involving an offsetting day-ahead schedule change.[21]

An appropriate RSG cost allocation methodology would be one that preserves the incentive for demand and supply to bid and offer into the day-ahead market. However, it is not apparent that the proposed alternative RSG cost allocation methodology preserves that incentive with respect to the day-ahead market. The proposed methodology imposes a one-directional RSG cost allocation methodology (to deviations that can cause the commitment of units in the RAC process) in combination with a notification and netting process.[22]

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[20] Alternative Mechanism Filing at 9.
[21] Informational Filing at 8 - 11.
[22] *Id.* at 9 and 19 - 20.

For example, assuming no constraints and day-ahead and real-time price convergence, it appears that with respect to the RSG Day-Ahead Schedule Deviations Charge an offer from an import not required to submit offers into the MISO energy markets has incentives to avoid the day-ahead market and instead submit its offer into the real-time market. If the offer from an import is put into the day-ahead market but ends up being curtailed or cut after the notification deadline, it appears that it will get charged RSG costs (a positive deviation since the import is being decreased from the day-ahead schedule which is akin to additional load in the RAC process).[23] Instead, if the offer from an import is put into the real-time market and is taken, it will not be charged RSG costs (as it can only be a non-positive deviation whether scheduled or not scheduled in the real-time market).[24]

Summarizing with respect to the import schedule, it appears that the proposed RSG cost allocation methodology implies that only a decrease in an import offer taken in the day-ahead market can cause RSG costs and that an increase in an import taken in the day-ahead market can never cause RSG costs.

However, deviations in both directions from day-ahead schedules, such as deviations that cause increased resource commitments and dispatch and deviations that cause decreased dispatch of committed resources, can cause RSG costs. The Midwest ISO recognized this in 2005 when it argued that imports are appropriately assessed RSG because imports, which could be scheduled 30 minutes prior to the hour, could displace generation that was previously committed in the RAC process.[25]

[23] *Id.* at Indicative RSG Tariff Languages, Sections 40.3.3.a.v.(c)(5), and 40.3.3.a.v.(d).
[24] *Id.* at Indicative RSG Tariff Languages, Sections 40.3.3.a.v.(c)(5), and 40.3.3.a.v.(d).
[25] Answer of Midwest ISO, Docket No. ER04-691-065, December 2, 2005, at 7.

Because it appears that the proposed alternative RSG cost allocation methodology has flaws due to the incentives it sends, the OMS urges the Commission to direct the Midwest ISO to address this as part of further work with stakeholders.

2. As proposed, the alternative RSG cost allocation methodology is a work product that is unfinished and that will require too much time to implement to address immediate problems.

In its February 1, 2008, Informational Filing, the Midwest ISO indicated that certain components of the proposal would require seven months following the issuance of a Commission Order before they could be implemented, but noted that timetable was based on the assumptions of no substantial changes by the Commission to the methodology as proposed or to the Ancillary Services Market ("ASM") proposal. The Midwest ISO noted that any significant directives to revise the ASM provisions could increase the time needed to implement the proposed alternative RSG cost allocation methodology.[26]

In its March 3, 2008, Filing proposing an alternative RSG cost allocation methodology, the Midwest ISO indicated that the suggested Tariff revisions were indicative in nature as they did not yet reflect the ASM proposal design elements. The Midwest ISO indicated it would require approximately two (2) months following the issuance of a Commission Order on the alternative RSG cost allocation methodology before ASM-conformed Tariff provisions would be filed.[27]

On February 25, 2008, the Commission issued an Order on the Midwest ISO's ASM filing, which among other things, required the Midwest ISO to file, within 30 days, revised cost

[26] Informational Filing at 12.
[27] Alternative Mechanism Filing at 2.

allocations related to the cost of reserves in the zone and to the carved-out grandfathered agreements.[28]

On March 13, 2008, the Midwest ISO announced that the ASM launch date would be moved back, to September 9, 2008.[29]

Based on the filings, it appears that the alternative RSG cost allocation methodology can only be implemented concurrently with, or later than, the launch of the Energy and Ancillary Services Market.[30] However, the alternative RSG cost allocation methodology filed with the Commission is based on the pre-ASM market design and does not reflect the design elements of the proposed ASM. Further, as a result of the Commission determinations, the ASM proposal will require design changes which may in turn have implications for the alternative RSG cost allocation methodology. The alternative RSG cost allocation methodology that the Commission is being asked to make a just and reasonable determination on is an unfinished work product for the Energy and Ancillary Services.

The timetables contained in the filings suggest that the earliest possible date that the alternative RSG cost allocation methodology could be implemented is sometime in December 2008.[31] The Commission directed ASM modifications and the Midwest ISO announcement that ASM launch will be moved back three (3) months suggest that the earliest likely date that it could be implemented is sometime in 2009.[32] Under both scenarios, the alternative RSG cost

[28] *Midwest Independent Transmission System Operator, Inc*., 122 ¶ 61,172 (2008) at P 421 and 440.
[29] Midwest ISO News Release at http://www.midwestiso.org/publish/Document/1e1401_118199304fa_-7ad00a48324a/2008-03-13%20ASM%20Launch%20Date%20Moved.pdf?action=download&_property=Attachment
[30] Alternative Mechanism Filing at 22.
[31] Assumes no modifications required by the Commission with respect to the filed alternative RSG cost allocation methodology or the yet-to-be filed revisions to reflect the ASM design and no delays from the Midwest ISO estimated development and implementation schedule.
[32] The OMS notes that the original timeline called for the alternative RSG cost allocation methodology to be filed in the fall of 2007.

allocation methodology, as conformed to the ASM, will require too much time to implement as the implementation date occurs subsequent to, and not concurrently with, the launch of the ASM.

While the OMS appreciates the Midwest ISO's hard work to date, fixing the RSG cost allocation issue sooner rather than later is required, especially given the Commission finding that the current RSG cost allocation may be unjust and unreasonable.

3. A less complex and less costly method for allocating RSG costs to deviations that can cause RSG costs may be warranted initially and immediately, but the proposed methodology should continue to be developed with the stakeholders.

In the March 3, 2008 Filing, the Midwest ISO included Data Analysis and Cost Allocations sections in support of the proposed alternative RSG cost allocation methodology.[33] It appears that this support is in the form of cost correlation rather than cost causation. The Midwest ISO believes the available RSG cost data remains insufficiently granular, and thus, incapable of supporting a conclusion that its RSG proposal matches cost causation and cost allocation with any degree of certainty.[34] However, according to the Midwest ISO, the cost data appropriately supports the alignment of the proposed tariff provisions with cost causation, as desired by the stakeholders.[35] For example, the Midwest ISO studies indicate that approximately 37% of RSG make whole payments needed are a result of constraint management.[36] So, while the OMS would encourage the Commission to immediately adopt a less complex allocation methodology that addresses the serious issue whereby millions of dollars are being shifted to the second pass uplift charge, the OMS strongly encourages the Commission to direct the Midwest ISO to continue to develop and provide support for its proposed four-bucket approach that better assigns the RSG costs to those activities driving the RSG costs, such as constraint management.

[33] Alternative Mechanism Filing, at end.
[34] Alternative Mechanism Filing at 15, footnote 28.
[35] Alternative Mechanism Filing at 14.
[36] Alternative Mechanism Filing at 12.

The OMS encourages the Commission to direct the Midwest ISO to implement, by year end 2008, an improved methodology, such as the four-bucket approach, to provide cost causation support, and to provide implementation cost analyses, as well as to address all questions and concerns the OMS has raised in its comments.

4. A definitive ordered timeframe on the long term RSG solutions that the Midwest ISO is currently studying is useful and necessary to communicate its commitment.

The Midwest ISO states that the alternative RSG cost allocation methodology is the result of numerous compromises and that it should be considered in the nature of a settlement proposal where modification could undermine the consensus achieved.[37] The Midwest ISO's statements regarding the compromises required in the development of the proposed methodology suggest that the alternative RSG cost allocation methodology might not be the optimal solution.

In the March 3, 2008, filing, the Midwest ISO discusses two compromises that were the result of time constraints. In that filing the Midwest ISO indicates two potential improvements for the RSG cost allocation issue that were not pursued at this time, (1) the possibility of reducing RSG costs by assuring that the LMP reflects the total cost of incremental energy and (2) the possibility of reducing RSG charges by redesigning the unit commitment process. These potential improvements, given the length of analysis and implementation time they required, were not incorporated into the proposal given the urgency for an alternative RSG cost allocation methodology. The Midwest ISO is studying them as "long-term" projects. The Midwest ISO does not explain when this will occur.[38]

The OMS strongly encourages the Commission to direct the Midwest ISO to study, develop and provide support for long-term RSG solutions. The development and communication

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[37] Informational Filing at 4 - 5.
[38] Alternative Mechanism Filing at 9, footnote 23.

of the timeframe with respect to the long-term RSG solutions are important to the extent that they reveal a commitment and plans to reduce RSG costs, and may be useful to the Commission and market participants. The OMS urges the Commission to direct the Midwest ISO to provide a timeline for providing the solutions.

VI. Conclusion

The OMS submits these comments because a majority of the members have agreed to generally support them. The following members generally support these comments. Individual OMS members reserve the right to file separate comments regarding the issues discussed in these comments:

Indiana Utility Regulatory Commission
Iowa Utilities Board
Michigan Public Service Commission
Minnesota Public Utilities Commission
Missouri Public Service Commission
Montana Public Service Commission
Nebraska Power Review Board
North Dakota Public Service Commission
Public Utilities Commission of Ohio
Wisconsin Public Service Commission

The Manitoba Public Utilities Board, the Pennsylvania Public Utility Commission, and the South Dakota Public Utilities Commission did not participate in this pleading. The Illinois Commerce Commission and the Kentucky Public Service Commission abstained from this pleading.

The Indiana Office of Utility Consumer Counselor, the Iowa Office of Consumer Advocate and the Minnesota Office of Energy Security,[39] as associate members of the OMS, participated in these comments and generally support these comments.

Respectfully Submitted,
William H. Smith, Jr.
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Dated: March 24, 2008

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Des Moines, Iowa, this 24th day of March, 2008.

William H. Smith, Jr.

[39] The Minnesota Office of Energy Security now exercises the consumer advocacy functions previously performed by the Minnesota Department of Commerce.