

California Department of Water Resources State Water Project Comments On Cost Allocation Guiding Principles Straw Proposal

February 29, 2012

On February 14, 2012, CAISO posted the Cost Allocation Guiding Principles straw proposal. On February 21, 2012, CAISO hosted a conference call with stakeholders to discuss the straw proposal. California Department of Water Resources State Water Project (SWP) appreciates the opportunity to provide comments.

CAISO developed this straw proposal on Cost Allocation Guiding Principles has seven elements, which are: 1) Causation, 2) Comparable Treatment, 3) Policy Alignment, 4) Incentivize Behavior, 5) Manageable, 6) Synchronized, and 7) Rational. CAISO proposes to apply these principles to Flexible Ramping Product, and then to review existing cost allocations to ensure these cost allocations are consistent with these principles. The Cost Allocation Principles guide how to determine the cause of a cost, who benefits, and other cost relations in the CAISO market.

In general, SWP supports CAISO in developing these cost allocation principles to allocate costs in the market, if these principles are just and reasonable. SWP also supports CAISO to establish a series of standards for the Cost Allocation Principles, and to use these standards as a significant basis to allocate various costs.

SWP strongly urges CAISO establish cost causation as the primary Cost Allocation Principle when developing all allocation methodologies. Following the application of the causation principle, a cost calculation standard could be developed to determine the percentage of each remaining Cost Allocation Principle that should be considered, the total costs to be allocated, whether the settlement interval price should be based on a weighted or simple average, or if a netting cost method is appropriate. The result should be accurate, just, and reasonable.

1. Causation

The principle of cost causation has been missing from CAISO initiatives and products for many years. This principle has been continuously pushed aside in deference to ease of implementation or perceived complexity, and as a result costs have typically been socialized to Measured Demand. SWP considers this principle as utmost going forward, in addition to the possibility of reexamining past or existing cost allocation methodologies.

2. Comparable Treatment

The CAISO Tariff contains many exceptions to this principle that SWP would like to see addressed. SWP has requested comparable treatment of such resources as Participating Load to that of Generators. Additionally, SWP has made the investment to install revenue quality meters which should allow equal or comparable treatment of SWP resources under many circumstances due to the improved granularity at which CAISO can monitor similar resources.

3. Policy Alignment

SWP feels that the Rational principle should be considered as an added requirement for the Policy Alignment principle, that both are mutually inclusive. SWP is concerned that without careful management, a Policy Alignment principle concerning Federal and State policy mandates could unintentionally drive changes that result in unreasonable and unjust rates to ratepayers and produce unintended consequences in which inefficiency is rewarded.

4. Incentivize Behavior

Incentivizing behavior involves not only maximizing profit, as described in the straw proposal. Cost allocation based on cost causation should also enable loads to alter their behavior in order reduce the need for—and the CAISO incurrence of—costs for various services. For instance, allocation of reliability costs to meet peak loads based on a load's contribution to system peak has the effect of encouraging off-peak usage and diminishing the need for capacity and resources to meet spiky peak usage. More granular allocation not merely between generation and loads, but also as among cost causers is necessary to gain greater efficiency.

5. Manageable

Being able to manage exposure to costs is key and relates to the point above. Socializing costs uniformly to all loads across all geographic areas and all time frames eliminates useful price signals and precludes demand response that can reduce the need for CAISO acquisition of certain services. Similarly, generation whose variability or other limitations requires additional CAISO services should receive price signals that reward better performance.

6. Synchronized

Synchronizing cost allocation with incurrence of costs based on the expected conditions driving the costs, as opposed to actual outcomes, may be necessary given the CAISO's role in balancing and anticipating reliability needs. Nonetheless, other objectives, such as incenting behavior and allocation based

on actual cost causation may be defeated if CAISO cost incurrence is based on consistently and significantly erroneous forecasts. For this reason, it is even more important that the CAISO continue its efforts to refine its forecasting and dispatch, with continual evaluation of accuracy and effectiveness in this arena.

7. Rational

While this category should be included, it should not be paramount. In particular, cost allocation that sends meaningful price signals to load should not be rejected without consideration of the benefits of potential altered behavior/demand response resulting from more accurate cost allocation. Additionally, inferior metering should not be a rote excuse for cost socialization. Demand resources that have invested in and high quality telemetering should benefit from more precise cost allocation, and others should be encouraged to improve their metering.

SWP would like to know if these principles or a subset of these principles are adopted and found to be applicable to existing cost allocations, what would be the timeline or process to remedy a non-abiding allocation.