

# Comments on Issue Paper and Straw Proposal Requirements for Import Bids Greater than \$1,000 under FERC Order 831

Department of Market Monitoring  
May 30, 2019

The California ISO Department of Market Monitoring (DMM) appreciates the opportunity to comment on the CAISO's May 10, 2019 issue paper and straw proposal on *Requirements for Import Bids Greater Than \$1,000/MWh* under FERC Order 831.<sup>1</sup> CAISO describes the objective of this new 2019 initiative as being "to ensure energy prices continue to reflect the marginal cost of supply when those prices exceed \$1,000/MWh, and to ensure intertie offer rules are consistent with ISO's internal bidding rules by developing reasonable cost-verification measures for intertie offers above \$1,000/MWh."<sup>2</sup>

## Summary

In June 2018, DMM recommended that CAISO prepare a filing with FERC pursuant to Order 831 to include imports in the CAISO's proposed process for *ex ante* cost review and to allow import bids over \$1,000/MWh to set market energy prices only if bids have been cost-verified prior to being dispatched by CAISO.<sup>3</sup>

In this initiative, CAISO is proposing to address this recommendation by adding a rule to the tariff explicitly stating that "suppliers may only submit import bids above \$1,000/MWh that reflect their actual or expected short-run marginal costs (i.e., fuel or fuel-equivalent cost.)" However, the CAISO is proposing to only perform any verification of this rule on an *ex post* case-by-case basis. With this approach, if any import bid over \$1,000/MWh is dispatched by the CAISO, the bid is not subject to review prior to market operations and may set the market clearing price in excess of \$1,000/MWh for the entire CAISO system. Even if it is later determined that the bid did not reflect the supplier's actual or expected short-run marginal costs, the overall market impact of the bid will not be mitigated since LMPs will not be reset.

Thus, DMM does not support the CAISO's proposal and continues to recommend the CAISO establish a process for *ex ante* cost-review of import bids over \$1,000/MWh and only allow imports bids over \$1,000/MWh to set market wide prices if these bids have been cost verified.

## Background

In 2016, FERC's Order 831 raised the energy offer cap for ISO/RTOs from \$1,000/MWh to \$2,000/MWh and generally required suppliers to submit offers above \$1,000/MWh based on verifiable costs. Order 831 required that each ISO/RTO must verify the costs underlying these cost-based offers above \$1,000/MWh before that offer can be used to calculate energy prices.<sup>4</sup>

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<sup>1</sup> *Requirements for Import Bids Greater Than \$1,000/MWh*, Issue Paper and Straw Proposal, May 10, California ISO. <http://www.caiso.com/Documents/IssuePaper-StrawProposal-ImportBidCostVerification.pdf>

<sup>2</sup> *New Initiative: Import Bid Cost Verification*, May 9, 2019. <http://www.caiso.com/Documents/NewInitiative-ImportBidCostVerification-IssuePaper-StrawProposal-Call051619.html>

<sup>3</sup> *Comments on FERC Order 831 Compliance Filing*, Department of Market Monitoring, June 27, 2018. <http://www.caiso.com/Documents/DMMComments-FERCOrderNo831ComplianceFiling-DraftTariffLanguage.pdf>

<sup>4</sup> CAISO Issue Paper and Straw Proposal, p. 5.

FERC further required that if a supplier submits an energy offer above \$1,000/MWh and the RTO/ISO cannot verify the costs underlying the offer before the market clearing process begins, that offer may not be used to calculate energy prices. However, if an offer exceeding \$1,000/MWh is dispatched and the resource's costs are verified after-the-fact, suppliers are eligible for make whole payments based on verified costs.

FERC's final order does not require that this same cost-verification process be applied to import offers greater than \$1,000/MWh, but allowed each ISO/RTO to develop its own requirements for import offers above \$1,000/MWh. As FERC explained:

.. we will not require import offers above \$1,000/MWh be cost-verified and find that imports are not similarly situated to internal generation resources. Unlike incremental energy offers from internal resources, import offers are often not resource-specific and, thus, it is difficult – some commenters say impossible – to ascertain the underlying costs of most import offers.<sup>5</sup>

However, FERC went on to add that:

Though it is not required, the Commission would consider proposals by RTOs/ISOs to verify or otherwise review the costs of imports or exports and/or develop additional mitigation provisions for import and export transactions above \$1,000/MWh. Such proposals should be submitted in a separate filing under section 205 of the Federal Power Act.<sup>6</sup>

In June 2018, the CAISO posted draft tariff language for its FERC Order 831 compliance filing. The CAISO's draft tariff language would allow bids from imports to set market prices at \$2,000/MWh without subjecting these bids to any *ex ante* cost verification process such as the process that will be applied to resources within the CAISO.

DMM's comments on the CAISO's June 2018 draft tariff language recommended that CAISO make a filing with the Commission so that import bids are subjected to the same cost verification process that will be applied to resources within the CAISO. As explained in DMM's June 2018 comments:

DMM recognizes that verifying import cost may be more difficult than verifying cost for gas and other resources within the ISO system. However, in the event that the ISO determines that import bid prices over \$1,000/MWh cannot be justified by prevailing bilateral market prices and conditions, the ISO should be able to utilize information submitted by suppliers as the basis for reviewing and verifying import bids. The fact that cost verification of imports may be difficult in some cases should not lead to adoption of a market design in which import bids over \$1,000 up to \$2,000/MWh are simply accepted and allowed to set market prices without any review, verification or other form of mitigation.<sup>7</sup>

After receiving stakeholder comments on the June 2018 draft tariff language for FERC Order 831 compliance, CAISO deferred this filing and requested an extension from the Commission.<sup>8</sup>

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<sup>5</sup> FERC Order 831, ¶195 at pp.122-123.

<sup>6</sup> FERC Order 831, ¶197 at p.123.

<sup>7</sup> Comments on FERC Order 831 Compliance Filing, Department of Market Monitoring, June 27, 2018, p.1

<sup>8</sup> *Motion for Extension of Time of the California Independent System Operator Corporation*, CAISO, FERC Docket No. RM16-5, June 29, 2019.

[http://www.caiso.com/Documents/Jun29\\_2018\\_Motion\\_Extension\\_Time\\_Comply\\_FERCOrderNo831\\_RM16-5.pdf#search=831](http://www.caiso.com/Documents/Jun29_2018_Motion_Extension_Time_Comply_FERCOrderNo831_RM16-5.pdf#search=831)

## CAISO Straw Proposal

In its straw proposal, the CAISO is proposing to add a rule to the tariff explicitly stating that “suppliers may only submit import bids above \$1,000/MWh that reflect their actual or expected short-run marginal costs (i.e., fuel or fuel-equivalent costs.)” However, the ISO is proposing to only verify and enforce this rule on an *ex post* case-by-case basis. With this approach, if an import bid over \$1,000/MWh is dispatched by the CAISO, this bid may set the market clearing price for the entire CAISO system, even if it is later determined that the bid did not reflect the supplier’s actual or expected short-run marginal costs. In this situation, the overall market impact of the bid will not be reversed since LMPs will not be reset.

Moreover, under the approach proposed by the CAISO, there would be a significant lag between the time import bids over \$1,000/MWh may begin setting prices and the time that any action is actually taken to mitigate bids that could not be cost justified. The CAISO proposes that import bids over \$1,000/MWh be subject to cost justification only if the CAISO initiates an audit. Once CAISO initiates an audit and requests supporting cost information, the participant has five business days to provide the requested information.

After receiving any supporting documentation, the CAISO would then need to evaluate this information before deciding whether or not the supplier’s documentation supported cost expectations above \$1,000/MWh. The CAISO will be allowed up to 10 business days to review the information and determine if it supports the bid price above \$1,000/MWh. Only after making this determination could the CAISO prohibit the scheduling coordinator from bidding at or above \$1,000/MWh for a specified amount of time (i.e., 60 days for the first instance, 180 days for subsequent instances).

Thus, even if the CAISO initiated an audit immediately after bids were submitted and decided very quickly that the supplier’s documentation did not support cost expectations above \$1,000/MWh, there would be a lag of at least five business days before the Scheduling Coordinator would be prohibited from bidding over \$1,000/MWh. In practice, this process may take at least one to two weeks (e.g. allowing some time for the CAISO to review the information provided). During this period, significant irreversible market impacts could occur before the CAISO could temporarily prohibit the participants from submitting imports bids over \$1,000/MWh.

## DMM Recommendation

DMM recommends that the CAISO implement the same approach for verifying and accepting import bids over the \$1,000/MWh that the CAISO is proposing for resources within the CAISO under its CCDEBE initiative.<sup>9</sup> With this approach the CAISO would screen import bids over \$1,000/MWh relative to a predetermined level (referred to as a “reasonableness threshold”) set at or above the \$1,000/MWh cap. If the submitted energy bid is within the reasonableness thresholds calculated by the CAISO for imports, the bid would be passed on to the market software and the bid would be allowed to set the market clearing price.

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<sup>9</sup> See proposed tariff changes currently posted as part of the CAISO’s CCDEBE initiative (Section 30.11 and 30.12) [http://www.caiso.com/informed/Pages/StakeholderProcesses/CommitmentCosts\\_DefaultEnergyBidEnhancements.aspx](http://www.caiso.com/informed/Pages/StakeholderProcesses/CommitmentCosts_DefaultEnergyBidEnhancements.aspx)

If the bid exceeded the reasonableness threshold, the bid could be dispatched but could not set the market clearing price above the reasonableness threshold. The supplier could then seek ex post cost recovery for the difference between the bid price and the reasonableness threshold.

The CAISO could set the reasonableness thresholds for imports based on prevailing market and system conditions observed by the CAISO and/or information provided by entities submitting import bids. Under normal conditions, this reasonableness threshold would presumably be set at the \$1,000/MWh level. The reasonableness threshold would be increased to levels between \$1,000 and \$2,000/MWh if warranted based on prevailing market and system conditions observed by the CAISO and/or information provided by entities submitting import bids. Reasonableness thresholds could be set at a uniform level for all imports or could vary based on information provided by suppliers for different resources or conditions in different supply regions.

### Implementation Issues

DMM's recommendation is based on the same basic process for *ex ante* review and verification of bids that the CAISO is proposing to apply to bids from resources within the CAISO. Thus, there should be not be any implementation issues preventing similar *ex ante* bid verification procedures for imports and resources within the CAISO. Moreover, for all of these resources, the frequency of bids in excess of \$1,000/MWh which could be cost justified should be extremely rare. As noted in CAISO comments to FERC on Order 831:

The CAISO does not believe that a soft cap on incremental energy bids is necessary in the CAISO markets at this time. As stated previously, there is no evidence indicating that incremental costs in the CAISO markets have approached the current \$1000/MWh cap. The final rule should allow ISOs or RTOs that do not share a seam with another organized market, such as the CAISO, to demonstrate that it is not necessary to implement the soft-cap requirement in their market at this time.<sup>10</sup>

However, if for some reason CAISO believes it cannot implement a process for *ex ante* review and verification of import bids over \$1,000/MWh concurrently with a process for *ex ante* verification of bids from resources within the CAISO, DMM recommends that the CAISO request deferment of rule changes allowing import bids in excess of \$1,000/MWh to set market clearing prices until such a process can also be implemented for import bids.

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<sup>10</sup> Comment of the California Independent System Operator on Offer Caps in Markets Operated by Regional Transmission Organizations and Independent System Operators, RM16-5-000, April 4, 2016. [http://www.caiso.com/Documents/Apr4\\_2016\\_CaliforniaISO\\_Comments\\_Notice\\_ProposedRulemaking\\_Pri ceCaps\\_ISO-RTOMarkets\\_RM16-5.pdf](http://www.caiso.com/Documents/Apr4_2016_CaliforniaISO_Comments_Notice_ProposedRulemaking_Pri ceCaps_ISO-RTOMarkets_RM16-5.pdf)

## Referrals to FERC

The CAISO's proposal states that:

If the CAISO determines the supplier's documentation does not support its submitted bid above \$1,000/MWh, the CAISO will prohibit the supplier from bidding at the interties for a specified amount of time and potentially refer the behavior to the Federal Energy Regulatory Commission.<sup>11</sup>

The CAISO should clarify the basis on which such a referral might be made (e.g. false information, etc). The CAISO should also clarify the respective roles it would expect CAISO and DMM staff to play in the process of cost review and potential referrals to FERC.

The straw proposal suggests that CAISO staff would be responsible for deciding whether to initiate an audit, to review supporting documentation, and to temporarily prohibit the scheduling coordinator from bidding above \$1000/MWh if the supporting documentation is insufficient. However, current CAISO policy is that all referrals to FERC for manipulation or provision of false or misleading information are to be done by DMM rather than CAISO staff. Given the reliance being placed on potential referrals as a deterrent mechanism under the CAISO's proposal, DMM recommends this CAISO policy be more formally clarified as part of this initiative.

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<sup>11</sup> CAISO Issue Paper and Straw Proposal, p. 8-9.