

# INDEPENDENT ENERGY PRODUCERS

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**To:** CAISO

**From:** Steven Kelly  
Policy Director

**Date:** April 23, 2012

**RE:** CAISO Flexible Ramping Product/Cost Allocation Draft Final Proposal

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The Independent Energy Producers Association (“IEP”) is pleased to provide the following comments regarding the CAISO’s Flexible Ramping Product/Cost Allocation Draft Final Proposal. IEP participated in the CAISO Stakeholder Meeting on April 17, 2012; and, those comments are incorporated herein. In response to the Stakeholder Meeting, we offer the following additional comments related to the proposal for cost allocation and product design.

**1) CAISO Decision-making and Stakeholder Processes.**

While the Stakeholder Meeting failed to address or clarify a lot of stakeholder questions, it did seem to address a number of process issues which raise questions and concerns.

- a) *The CAISO’s Cost Allocation Guiding Principles apparently don’t guide decision-making.* In response to stakeholder questions regarding cost allocation, IEP was surprised to learn from CAISO staff that “cost causation” was the sole principle governing CAISO’s approach to market design. When addressing recently the CAISO’s Cost Allocation Guiding Principles document, the CAISO had created the impression that market design and cost allocation would be governed by a more nuanced approach, including the balancing of such factors as (a) *causation*, (b) *comparable treatment*, (c) *accurate price signals*, (d) *incentivize behavior*, (e) *manageable* [“Market participants should have the ability to manage exposure to the allocation...Allocating unmanageable costs does not provide market participants with the opportunity to minimize the cost drivers the cost allocation is intended to incent...In addition, changes to cost allocation mechanisms should recognize that transitional measures may be needed to be assessed to allow sufficient time for market participants to implement within contractual arrangements”<sup>1</sup>]; and, (f) *synchronized*. Having now been informed that the sole principle guiding CAISO market design is cost causation, the question arises as to the purpose of the stakeholder process related to Cost Allocation Guiding Principles and, more fundamentally, what’s the effect of not balancing market design on a set of principles but rather relying solely on cost causation?

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<sup>1</sup> CAISO, “Cost Allocation Guiding Principles – Draft Final Proposal, March 15, 2012, p. 6.

- b) *The CAISO's Stakeholder Process is meaningless if stakeholder comments are not considered and subsequent CAISO actions explained.* As reported by CAISO staff, the Cost Allocation Guiding Principles Draft Final Proposal is now "final." Based on CAISO staff comments, the sole change was (or will be) to strike "Draft" from the title page. Since apparently no comments received by the CAISO warranted changes to the Draft Final, it would be helpful to know why individual stakeholder comments were (a) either not reviewed or (b) reviewed and rejected in their entirety.
  
- c) *The CAISO's angst against bilateral contracting if such contracts reduce participation in CAISO markets raises concerns regarding equitable treatment of existing contracts.* Since 2001, California's energy market, particularly the market for new generation development, has been characterized as a bilateral contract market. Thus, it was informative to hear from CAISO staff that bilateral contracts that reduce participation in CAISO markets (e.g. most existing contracts, self schedules, etc.) are not appreciated. Staff's position suggests that the primary role of maintaining grid reliability is supplemented with the goal of forcing generation into the CAISO markets irrespective of existing, bilateral contractual arrangements. It further suggests a lack of appreciation for these contractual arrangements and the commercial realities that have driven, and in some instance continue to drive, the operations and development of generation infrastructure.

## **2) Cost Allocation -- Flexible Ramping Products**

IEP has provided a series of comments in the CAISO stakeholder process raising concerns related to the allocation of costs incurred by the CAISO to maintain overall grid reliability, integrate renewables, and otherwise undertake its responsibilities. We also have proposed solutions. We will not repeat them here; rather, we will incorporate them by reference. Once again, we wish to remind the CAISO of some of the critical factors that govern the energy markets in California today. These factors apply equally in a scenario wherein cost-causation is the sole governing principle of market design and, alternatively, when a more nuanced and balanced approach is applied. These factors include the following:

- a) The CAISO's primary goal is to maintain overall grid reliability. In this role, the CAISO acts on behalf of load. A number of tools exist to accomplish this outcome, and it's incumbent on the CAISO to achieve this goal in an efficient, cost-effective manner; yet, at the same time, it's important that the CAISO not become a barrier to achieving various public policy objectives related to resource procurement nor undermine the viability of otherwise viable projects.
  
- b) LSE procurement practices determine the what, when, and where of generation development in California (renewable and non-renewable). In this role, the LSEs act on behalf of load. This is true historically; and, it is perhaps the primary reason California has installed over 16,000 MWs of new generation capacity over the past decade. This will be true for the foreseeable future as California strives to replace 15,000 MWs (+) of aging generation and/or coal contracts over the next decade to meet the RPS and other policy objectives. As a result, the CAISO's focus on cost causation and market signals only works if the load receives those signals.

- c) The CAISO's attempt to shift the cost allocation/cost responsibility for its "backstop" procurement and integration activities represents a reversal in approach. Since the CAISO's inception, load has borne this cost responsibility, and the CAISO has managed the electric grid successfully and reliably to the benefit of load. Imposing these backstop and integration costs on electric generators, given the historical success of the current approach, risks weakening the level of electric grid reliability attained historically (rather than improving on it).
- d) Generators operating under existing contracts with an LSE are unlikely to have mechanisms to recover the costs associated with CAISO procurement to maintain grid reliability and integrate renewables. California has over 600 generation contracts. Typically, contracts for renewables, including intermittents, tend to be fixed price over the life of the contract (typically 15-25 years for new resources). The CAISO proposal fundamentally shifts CAISO related costs from one party of the bilateral transaction (i.e. load) to its counter-party (i.e. generation). It is naïve to assume that contract renegotiation en mass provides a meaningful, reasonable path forward.
- e) The CAISO's cost to maintain overall grid reliability on behalf of load, and to integrate renewables in recognition of LSE procurement is inherently unknown and unknowable over the life of a contract. Imposing open-ended responsibility for unknown and unknowable costs on electric generators undermines the integrity of existing contracts. Imposing responsibility for unknown and unknowable costs on developers of future contracts will create a barrier to development by undermining the financing of the project.

### **3) Design - Flexible Ramping Products**

The Stakeholder Meeting revealed an information gap regarding the Flexible Ramping Product design. During the course of discussion, the CAISO appeared to recognize that a number of fundamental design features were not well described to market participants; or, alternatively, the CAISO indicated upon comment that its initial design warranted changes.

Irrespective of the issues associated with cost allocation outlined above, IEP suggests another iteration of stakeholder meetings in order to clarify exactly the technical aspects of the Flexible Ramping Product proposal prior to seeking Board approval.

We appreciate your consideration of these matters.

Respectfully submitted,



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