171 FERC ¶ 61,172
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Neil Chatterjee, Chairman;
Richard Glick, Bernard L. McNamee,
and James P. Danly.

California Independent System Operator Corporation — Docket No. ER20-1075-000

ORDER ACCEPTING TARIFF REVISIONS

(Issued May 29, 2020)

1. On February 25, 2020, the California Independent System Operator Corporation (CAISO) filed, pursuant to section 205 of the Federal Power Act (FPA),[1] tariff revisions to modify certain aspects of its capacity procurement mechanism (CPM). In particular, CAISO submitted alternative tariff sheets reflecting two approaches for determining CPM compensation for resources with cost offers above the soft offer cap – a preferred approach, and an alternate approach for the Commission to consider in the event it finds CAISO's preferred approach is not just and reasonable. In this order, we accept CAISO's preferred approach, effective June 1, 2020, as requested.

## I. Background

2. Since 2006, CAISO and the local regulatory authorities within its balancing authority area, chiefly the California Public Utilities Commission (CPUC), have jointly administered the resource adequacy program. The resource adequacy program requires that load serving entities procure capacity to meet their forecasted peak load plus a reserve margin, as established by their local regulatory authority. The program also requires load serving entities to procure local and flexible capacity, as determined by CAISO and adopted by their local regulatory authorities. To remedy unresolved resource adequacy deficiencies and/or meet specified reliability needs, CAISO relies on backstop capacity procurement authority under the CPM provisions of its tariff.[2]

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[1] 16 U.S.C. § 824d (2018).

[2] CAISO Tariff, § 43A.

3. Under the CPM tariff provisions, resource owners submit bids in a competitive solicitation process, and based on the bids submitted, CAISO offers CPM designations to address one of the circumstances specified in the tariff.[3] The tariff provides two options for the compensation of CPM resources. First, the resource can receive compensation based on its capacity bid price up to the CPM soft offer cap, which is set at $6.31/kw-month.[4] The CPM soft offer cap is based on the going-forward costs (i.e., fixed operations and maintenance costs, ad valorem taxes, and insurance costs) of a reference unit,[5] plus a 20% adder to that total cost.[6] The second option is for the CPM resource to offer capacity into the competitive solicitation process at a cost above the soft offer cap and to cost-justify that offer by making a filing with the Commission based on the formula in schedule F of the *pro forma* Resource Must-Run (RMR) contract. This formula compensates a resource based on its full annual cost of service, including a return on and of capital, for its net plant at the time of the contract.[7] Regardless of which option a resource selects, it retains all revenues it earns in the CAISO markets.[8] A Commission-approved, resource-specific CPM price remains in effect for the remainder of the calendar year in which it was approved, and for the subsequent two calendar years, unless superseded by a subsequent Commission-approved price during that period.[9]

4. The term of a CPM designation can range from a minimum of 30 days up to 12 months (annual CPM designation), depending on the purpose of the designation.[10] CAISO does not require resources to submit bids into the CPM competitive solicitation process. However, if a resource does submit a bid, and CAISO accepts the bid, the resource must accept the designation. If CAISO offers a CPM designation to a resource

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[3] *Id.*, § 43A.2.

[4] *Id.*, § 43A.4.1.1.

[5] The reference unit used to set the soft offer cap is a merchant constructed mid-cost, 550 MW combined cycle unit with duct firing or similar advanced combined cycle resource, based on costs reported in the California Energy Commission Cost of Generation Study and Model. *Id.*, § 43A.4.1.1.2.

[6] *Id.*, § 43A.4.1.1.2.

[7] *Id.*, § 43A.4.1.1.1.

[8] *Id.*, § 43A.7.3.

[9] *Id.*, § 43A.4.1.1.1.

[10] *Id.* § 43A.3.

that has not submitted a bid in the competitive solicitation process, the resource may decline the designation.[11]

5. CAISO's tariff requires it to conduct a stakeholder process at least every four years to evaluate the level of the soft offer cap, but the tariff does not require CAISO to make a change or to justify to the Commission its decision to retain the existing soft offer cap.[12] CAISO notes that, in 2019, it conducted a stakeholder process to determine whether any changes to the soft offer cap were necessary.[13] CAISO states that it ultimately determined that changes to the existing soft offer cap were unwarranted at this time.

## II. CAISO Proposal

6. CAISO proposes to replace the existing formula for determining compensation above the CPM soft offer cap with a new formula, to be effective June 1, 2020. CAISO's filing includes two mutually exclusive proposals for pricing these CPM offers, and requests that the Commission first consider CAISO's preferred approach. CAISO specifies that the Commission should consider the alternative approach only if the Commission finds that CAISO's preferred approach is not just and reasonable.[14]

7. Under the preferred approach, CAISO proposes a new formula under which a resource may justify its price above the soft offer cap based on the resource's going-forward fixed costs, using the same cost categories and 20% adder used to establish the existing, Commission-approved soft offer cap. Consistent with the cost categories included in the CPM soft offer cap, CAISO defines going-forward fixed costs as: (1) fixed operations and maintenance costs; (2) ad valorem taxes; and (3) insurance costs. Thus, CAISO states that its proposal reflecting going-forward fixed costs is a more limited set of fixed costs than what resources that bid above the soft offer cap are currently permitted to recover, which is full annual cost of service, including a return on (and of) capital, of its net plant at the time of the contract. CAISO argues that this proposed formula (1) aligns with how the existing CPM soft offer cap is derived, (2) is consistent with prior Commission guidance that CPM compensation should allow for some meaningful contribution to fixed cost recovery and provide incentives

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[11] *Id.*, §§ 43A.5.1, 43.A.5.2.

[12] *Id.*, § 43A.4.1.1.2.

[13] CAISO Transmittal at 12

[14] *Id.* at 15. CAISO notes that its Board of Governors directed CAISO to file alternative tariff sheets in this manner. *Id.* at 16.

for resources to undertake necessary upgrades and long-term maintenance, and (3) reflects the voluntary nature of CPM designations.[15]

8. As stated above, only if the Commission rejects CAISO's preferred approach, does CAISO request that the Commission consider its alternative proposal, under which a resource may justify its price above the soft offer cap based on the same going-forward cost formula as the preferred approach, but without the 20% adder. CAISO asserts that this formula without the adder is consistent with Commission statements that recovery of going-forward costs is appropriate for voluntary, as opposed to mandatory, backstop mechanisms.[16]

9. CAISO also proposes two minor clarifying revisions to its CPM tariff provisions to verify that certain requirements imposed by the resource adequacy provisions of its tariff also apply to CPM resources. Specifically, CAISO proposes a clarifying revision to tariff Section 43A.5.4, which states that the Resource Adequacy Availability Incentive Mechanism also applies to CPM resources. Finally, CAISO proposes a revision to tariff Section 43A.6.2 to clarify that CAISO will publish a report on CPM designations by the earlier of 30 days after it selects the resource or the tenth day of the month in which the designation takes effect.[17]

## III. <u>Notice and Responsive Pleadings</u>

10. Notice of CAISO's filing was published in the *Federal Register*, 85 Fed. Reg. 12,780 (2020) with interventions and protests due on or before March 17, 2020. Timely motions to intervene were filed by Public Citizen, Inc.; the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (Six Cities); NRG Power Marketing LLC; Alliance for Retail Energy Marketers; the City of Santa Clara, California; the California Municipal Utilities Association (CMUA); Northern California Power Agency; the California Department of Water Resources, and Modesto Irrigation District. Timely motions to intervene and comments or protests were filed by Southern California Edison Company (SoCal Edison); the CAISO Department of Market Monitoring (DMM); Powerex Corp. (Powerex); Pacific Gas and Electric Company (PG&E); Calpine Corporation (Calpine); and Middle River Power, LLC (Middle River). CPUC filed a notice of intervention and comments. CAISO, Six Cities, CMUA, DMM,

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[15] *Id.* at 16-18 (citing *Cal. Indep. Sys. Operator Corp.*, 134 FERC ¶ 61,211, at PP 57-59 (2011); *Cal. Indep. Sys. Operator Corp.*, 153 FERC ¶ 61,001, at P 29 (2015) (2015 CPM Order)).

[16] *Id.* at 18.

[17] *Id.* at 23-24.

and Powerex filed answers. On April 9, 2020, CAISO filed an answer to the DMM and Powerex's answers.

### A. Comments and Protests

11. Middle River supports CAISO's preferred approach, noting the need for CPM compensation to provide a meaningful contribution towards fixed cost recovery, particularly because most CPM designations have been short-term.[18]

12. CPUC, DMM, and PG&E support CAISO's initiative to change the formula for determining CPM compensation above the soft offer cap, but urge the Commission to accept CAISO's alterative approach that does not include the 20% adder.[19] CPUC asserts that, in the context of a resource-specific, cost-justified rate, the resource owner should know what long-term upgrades, maintenance, and other capital investments should be expected in the coming year. Thus, CPUC contends that the proposed 20% adder should be unnecessary, and it would be unjust and unreasonable to compensate a resource owner for costs they do not incur. CPUC also notes that CAISO's tariff allows resource owners to include a maintenance adder in their energy market bids and permits CPM resources to retain energy market revenues. CPUC claims that CAISO has offered no concrete justification for the 20% adder since no party has provided data in this or previous proceedings regarding the magnitude of the annual costs for necessary upgrades and long-term maintenance and/or how one would define a "meaningful" contribution to fixed cost recovery.[20]

13. DMM argues that CAISO offers no explanation of how or why a 20% adder is appropriate. DMM posits that a 20% adder may in some instances be too low for some resources, while in other instances may provide additional revenue for resources that do not face additional costs. DMM states that it does not oppose a reasonable adder but recommends that the Commission's assessment take into account that CPM units also retain net energy market revenues. DMM suggests that CAISO consider an option that would allow resources with annual CPM designations to file for resource-specific recovery of potential long-term maintenance and upgrade costs.[21]

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[18] Middle River Comments at 3.

[19] CPUC Comments at 4-9; DMM Comments at 2-7; PG&E Comments at 13-17.

[20] CPUC Comments at 7-9.

[21] DMM Comments at 6-7.

14. Similar to DMM, PG&E argues that the Commission should account for resource-specific market revenues when determining resource-specific CPM compensation above the soft offer cap. Short of that, PG&E asserts that the alternative proposal without the adder is more likely to result in compensation that falls within the Commission's accepted range for reliability services while giving the resource a reasonable opportunity to recover fixed costs.[22]

15. Unlike the parties that object to the 20% adder but support CAISO's alternative approach, Calpine argues that neither of the options proposed by CAISO are just and reasonable because both effectively set a hard cap on a resource's CPM compensation that is below the resource's full fixed costs. Calpine contends that CAISO presents no evidence that its proposal would result in a meaningful contribution to fixed cost recovery because, by definition, a resource's going-forward costs do not cover any return of, and on, existing capital investment, let alone the capital costs of new incremental investment and long-term maintenance. Further, Calpine asserts that shrinking energy margins in the CAISO energy markets cannot be relied upon to provide meaningful recovery of a resource's full fixed costs.[23] Calpine notes that CAISO's proposal is rooted in Commission precedent that requires full cost of service recovery when a backstop procurement mechanism is mandatory, but permits lesser compensation when the mechanism is voluntary.[24] Calpine contends that, because CAISO's tariff conjoins CPM with exceptional dispatch, CPM is not truly voluntary.[25] Calpine explains that, although a resource may decline a CPM designation, an uncommitted resource remains subject to mandatory operation under CAISO's exceptional dispatch tariff provisions.[26]

16. Calpine also disputes CAISO's position that the current formula for CPM compensation above the soft offer cap results in double recovery of a resource's costs because it provides for full fixed cost recovery and the retention of market revenues. Calpine disagrees that the CAISO tariff permits full fixed cost recovery plus retention of market revenues. Calpine claims that a better way to address any potential double recovery of costs would be for CAISO to retain the current resource-specific full fixed

[22] PG&E Comments at 13-17.

[23] Calpine Protest at 11-12.

[24] *Id.* at 4 (citing CAISO Transmittal at 14).

[25] Exceptional dispatch is a manual dispatch instruction issued for purposes of CAISO maintaining system reliability, addressing transmission modeling limitations, or for certain testing-related purposes specified in Section 34.11 of the CAISO tariff.

[26] Calpine Protest at 4-8.

cost recovery option, but to require an *ex ante* or *ex post* crediting of expected or actual net market revenues.[27]

17. Further, Calpine asserts that CAISO offers no support that its proposed 20% adder, when applied to varying levels of resource-specific going-forward costs, will provide all resources with a meaningful contribution to recovery of their fixed capital costs. To the contrary, Calpine argues that capping the adder at 20% will result in widely disparate contributions to resources' full fixed cost recovery.[28]

18. Finally, Calpine argues that CAISO's proposal will suppress CPM prices, at the same time that resource adequacy prices are likely to rise due to a tightening market for local resource adequacy capacity, and therefore is likely to create adverse incentives for load serving entities to forego bilateral resource adequacy contracts and rely on CPM backstop procurement. Further, Calpine asserts that suppressing CPM prices will negate price signals needed to attract new reliability resources as capacity deficiencies arise in California, especially in local constrained areas.[29]

19. In addition to comments on CAISO's proposal, parties offer comments on a number of other topics. In particular, CPUC, DMM, and SoCal Edison also recommend that the Commission require CAISO to undertake a more thorough review of the level of the CPM soft offer cap.[30] DMM contends that CAISO's soft offer cap appears to include significantly overstated fixed operations and maintenance costs, citing concerns with the data included in the California Energy Commission reports that CAISO uses to evaluate the level of the soft offer cap. Further, DMM argues that the level of the soft offer cap deserves additional scrutiny due to the lack of competitiveness in local capacity areas and, therefore, in the CPM competitive solicitation process. DMM highlights its 2018 analysis of the structural competitiveness for major local capacity areas, which shows that there are one or two pivotal suppliers in each of these local capacity areas. DMM also points to two annual CPM designations made by CAISO in 2017, where there were no other available resources that could meet the identified local reliability needs, in support of its assertion that the CPM procurement process is not competitive. Additionally, DMM points out that in CAISO's 2018 solicitations for system capacity,

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[27] *Id.* at 8-11.

[28] *Id.* at 11-14.

[29] *Id.* at 15-19.

[30] CPUC Comments at 9-10; DMM Comments at 7-18; SoCal Edison Comments at 8.

CAISO issued CPM designations for most of the eligible bid capacity, indicating that many of the suppliers were individually pivotal.[31]

20. CPUC and SoCal Edison raise another concern regarding the potential stranding of the flexible capacity associated with annual CPM designations. CPUC explains that, under the existing CPM tariff provisions for system and local designations, CAISO allocates resource adequacy credit to the affected load serving entities, which reduces those load serving entities' obligations to procure system and local resource adequacy capacity. CPUC points out that CAISO does not obtain the flexible capacity attributes of a designated resource, nor does it allocate the flexible capacity to load serving entities to reduce their otherwise applicable capacity requirements. CPUC states that, as a result, the more stringent must-offer assessment hours for flexible resources do not apply which could potentially jeopardize reliability in the event that CAISO does not have access to sufficient flexible resources. Further, CPUC contends that it is not just and reasonable for customers to pay for the CPM capacity without receiving all of the benefits (i.e., flexible capacity) that these resources could potentially provide. CPUC highlights that CAISO's RMR tariff provisions allocate the flexible capacity of RMR resources and argues that CPM resources should be treated comparably.[32] SoCal Edison asserts that failure to allocate such attributes for any CPM resource receiving an annual CPM designation could create a substantial risk of creating artificial scarcity in the market for flexible resource adequacy capacity and requests that the Commission direct CAISO to allocate the flexible capacity attributes.[33]

21. SoCal Edison and PG&E claim that the existing CPM designation process is not competitive. SoCal Edison requests that the Commission direct CAISO to implement a three pivotal supplier test to assess market power for the annual CPM competitive solicitation process. SoCal Edison argues that the CPM soft offer cap alone is not sufficient market power mitigation. SoCal Edison asserts that the use of CPM has changed since the current design was implemented in 2015 from a mechanism used for short-term procurement, for which the soft offer cap was just and reasonable, to a tool used for larger and longer-term procurement. SoCal Edison contends that this change in usage warrants scrutiny and redesign of the CPM.[34] PG&E contends that the current soft offer cap is too high to ensure competitive outcomes in the CPM competitive solicitation process, as demonstrated by data on CPM designations since 2012, and requests that the

[31] DMM Comments at 7-18.

[32] CPUC Comments at 10-12.

[33] SoCal Edison Comments at 6-7.

[34] *Id.* at 3-6.

Commission direct CAISO to publish data and metrics disclosing how competitive the processes are.[35]

22. Powerex does not comment directly on CAISO's instant proposal but instead describes perceived deficiencies in the overall California resource adequacy construct and argues that these shortcomings demonstrate the importance of an effective CPM. However, Powerex contends that the current structure of CPM limits CAISO's ability to secure commitments of external physical resources, which may be increasingly needed given generation retirements within the CAISO balancing authority area, and also due to the short duration of a CPM designation, below-market CPM compensation, and short CPM lead time. Powerex encourages CAISO to work with stakeholders to adopt a modified CPM framework that can obtain forward commitments of the internal and external capacity necessary to allow CAISO to safely and reliably operate its system. Specifically, Powerex recommends a minimum six-month seasonal CPM product, CPM compensation up to at least the full annualized cost of new entry, and a shift of both the CPM process and overall resource adequacy program to year-ahead or multi-year procurement.[36]

## B. Answers

23. CAISO reiterates its position that although both proposals are just and reasonable, it prefers the option that includes the adder for the same reasons stated in its filing. CAISO disputes arguments that it must provide additional analysis in support of the proposed 20% adder, arguing that it must only demonstrate that its proposed rate falls into a zone of reasonableness. CAISO avers that it has shown that an adder-based methodology is a reasonable approach to afford resources some meaningful opportunity to recover additional fixed costs and reflects the Commission's approved use of an adder in determining the just and reasonable soft offer cap.[37]

24. CAISO asserts that DMM's suggestion for a resource-specific approach for compensating CPM resources receiving 12-month, whole unit CPM designations that submit offers above the soft offer cap should be rejected because this suggestion constitutes a material modification of CAISO's proposal that is contrary to the limitations

[35] PG&E Comments at 8-13.

[36] Powerex Comments at 3-13.

[37] CAISO April 1, 2020 Answer at 15-21.

established in *NRG Power Marketing., LLC v. FERC*[38] and because it would blur the distinctions between RMR and CPM compensation.[39]

25. CAISO contends that Calpine's claim that full cost of service compensation is required for CPM is without merit. CAISO states that the Commission has previously rejected RMR-type cost of service pricing for CAISO's voluntary backstop procurement mechanism, finding that because the mechanism is voluntary, "resources are free to decline [the] designation and pursue other avenues of recovering fixed costs."[40] Rather, CAISO asserts that the Commission has held that compensation for resources that elect to accept a CPM designation need only provide for a meaningful contribution toward fixed cost recovery. CAISO argues that the 20% adder provides a meaningful contribution toward a resource's fixed costs, particularly when coupled with existing tariff provisions that allow a CPM resource to retain energy market revenues. Further, CAISO asserts that Calpine's references to the proposed revisions as a "hard cap" are misleading. CAISO states that, under the Commission's well-established nomenclature, a hard-offer cap or price cap identifies a specific number above which a market participant may not be paid, regardless of their costs. CAISO avers that the formula proposed here is a soft offer cap because it permits a market participant to exceed an identified dollar threshold based on a specific showing of its costs. CAISO contends that Calpine's arguments about disparate recovery levels ignore that full fixed cost recovery is not required for a voluntary backstop procurement mechanism.[41]

26. CAISO disputes Calpine's claim that CPM is mandatory. CAISO asserts that this claim constitutes a collateral attack on the Commission's explicit finding that "CPM designations are voluntary,"[42] and on CAISO's Commission-approved exceptional dispatch terms and pricing, rendering the claim beyond the scope of this proceeding. CAISO also notes that the Commission has previously rejected identical arguments by Calpine.[43] CAISO argues that Calpine's protest on this issue is based on a flawed understanding of CAISO's exceptional dispatch process, which suggests that, if a resource declines a CPM designation for a certain month, CAISO will be more likely to

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[38] 862 F.3d 108 (D.C. Cir. 2017).

[39] CAISO April 1, 2020 Answer at 21-26.

[40] *Id.* at 30 (citing *Cal. Indep. Sys. Operator Corp.*, 125 FERC ¶ 61,053, at P 36 (2008)).

[41] *Id.* at 28-35.

[42] *Id.* (citing *Cal. Indep. Sys. Operator Corp.*, 168 FERC ¶ 61,199, at P 32 (2019)).

[43] *Cal. Indep. Sys. Operator Corp.*, 134 FERC ¶ 61,132, at P 38 (2011).

issue exceptional dispatch instructions to that resource during the month for which it declined the CPM designation.[44]

27. In addition, CAISO contends that Calpine is incorrect that the current formula for CPM compensation above the soft offer cap does not permit retention of market revenues. According to CAISO, its tariff clearly contemplates that all CPM resources, including those with above-cap offers, retain market revenues.[45]

28. CAISO asserts that Calpine's claims that either of the proposed compensation methodologies will result in load serving entities relying on CPM instead of entering into bilateral resource adequacy contracts is speculative and unsupported. First, CAISO notes that the Commission previously found that the soft offer cap is set at the higher end of resource adequacy prices and, therefore, should not cause load serving entities to forego bilateral resource adequacy contracts and rely on CPM backstop procurement.[46] Second, CAISO posits that the type of potential distortion discussed by Calpine would require evidence that numerous resources have felt compelled to submit offers above the soft offer cap, but CAISO points out that, in the history of CPM and its predecessors, no resource has ever sought to cost justify a price above the soft offer cap. Thus, CAISO claims that Calpine has offered no evidence to support its concerns on this issue. CAISO argues that none of the other issues raised by Calpine, such as increased use of CPM or potential capacity shortages in the coming years, relate to the narrow issues raised by this proposal.[47]

29. CAISO argues that the other issues raised in the comments—such as requests to lower the soft offer cap, allocate flexible resource adequacy credits, or undertake a major overhaul of the CPM framework—are beyond the scope of this proceeding and, therefore, the Commission should reject them.[48] Six Cities and the California Municipal Utilities Association likewise assert that requests for broad structural changes to CPM and the

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[44] CAISO April 1, 2020 Answer at 37-41.

[45] *Id.* at 42 (citing CAISO Tariff, § 43A.7.3 ("In addition to the CPM Capacity Payment identified in Section 43A.7, CPM resources, including Flexible Capacity CPM Resources, shall be entitled to retain any market revenues received as a result of their selection in the CAISO markets.")).

[46] 2015 CPM Order, 153 FERC ¶ 63,001 at P 29.

[47] CAISO April 1, 2020 Answer at 44-48.

[48] *Id.* at 49-74.

overall resource adequacy construct should be rejected as beyond the scope of CAISO's proposed tariff revisions.[49]

30. DMM, in response to CAISO's answer, offers additional discussion and analysis to support its contention that the current soft offer cap is too high because it overstates operations and maintenance costs.[50]

31. Powerex filed an answer in which it clarifies that it is not protesting CAISO's proposed tariff revisions in this proceeding, nor is it making a request for specific Commission action in response to CAISO's proposal. Rather, Powerex asserts that its comments demonstrate that, due to changing conditions in California that impact the resource adequacy construct, the current CPM framework is likely to be ineffective going forward as a backstop to meet system-wide needs. Powerex repeats its previous concerns and recommendations regarding potential enhancements to CPM design.[51]

32. CAISO filed an answer to DMM's and Powerex's answers. CAISO argues that DMM provides no new information to support lowering the CPM soft offer cap and reiterates that this issue is beyond the scope of the instant proceeding. CAISO again asserts that the issues raised by Powerex are beyond the scope of this proceeding and are supported by conclusory and speculative claims.[52]

## IV. Discussion

### A. Procedural Matters

33. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2019), the notice of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

34. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2019), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We accept the answers filed by CAISO, Six Cities, CMUA, DMM, and Powerex because they have provided information that assisted us in our decision-making process.

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[49] Six Cities Answer at 2-8; CMUA Answer at 2-5.

[50] DMM Answer at 1-5.

[51] Powerex Answer at 2-15.

[52] CAISO April 9, 2020 Answer at 2-8.

### B. CPM Revisions

35. We find CAISO's preferred proposal to modify its tariff's formula for determining CPM compensation above the soft offer cap to be just and reasonable and not unduly discriminatory or preferential.[53] CAISO's proposal to allow CPM resources a 20% adder on top of their going forward fixed costs will allow those resources the opportunity for sufficient recovery of fixed costs plus a return on capital to facilitate incremental upgrades and improvement by the resources. We also find that CAISO's proposed revisions, which make clear that certain requirements imposed by the tariff's existing resource adequacy provisions also apply to CPM resources, are appropriate clarifications of the existing tariff provisions. Thus, we accept CAISO's proposed preferred tariff revisions, as discussed below, effective June 1, 2020, as requested.

36. We are not persuaded by CPUC's argument that it is inappropriate to include a 20% adder in the context of a resource-specific, cost-justified rate. To the contrary, the inclusion of a 20% adder on top of demonstrated going forward fixed costs is consistent with Commission precedent on CPM compensation. In 2015, the Commission accepted CAISO's currently effective soft offer cap, which is based on the going-forward costs of a reference unit plus a 20% adder, finding that this method for calculating the soft offer cap allowed for sufficient recovery of fixed costs plus a return on capital to facilitate incremental upgrades and improvement by resources.[54] The soft-offer cap does not provide full fixed cost recovery, but instead limits cost recovery to defined categories of going-forward costs of a reference unit, which include (1) fixed operations and maintenance costs, (2) ad valorem taxes, and (3) insurance costs. The soft-offer cap also includes a 20% adder of the aforementioned costs, which is intended to facilitate recovery of additional fixed costs. Thus, the Commission has found that it is just and reasonable in the context of CPM compensation to allow resources the opportunity to recover costs beyond their going-forward costs and that a 20% adder is sufficient for this purpose.

37. The reference unit used to determine the currently effective soft offer cap was a mid-cost, merchant-constructed, 550 MW combined cycle unit. This unit was selected because, among other things, gas-fired resources are typically the marginal resources in CAISO's markets and these resources make up the largest percentage of non-resource adequacy resources that are eligible to receive CPM designations.[55] The option provided in CAISO's tariff for resources to submit cost-based offers above the soft offer cap recognizes that some generation resources have higher costs than the reference unit. We

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[53] Given this finding, we do not reach the merits of CAISO's alternative proposal.

[54] *See* 2015 CPM Order, 153 FERC ¶ 61,001 at P 29.

[55] *Id.* P 13 n.27.

find that it is reasonable to calculate the offer caps for such resources in the same manner as the soft offer cap calculation and accounting for the higher costs of those resources.

38. We find DMM's argument that CAISO's approach has not been shown to be reasonable because it does not accurately capture costs beyond going-forward costs to be unpersuasive. In the 2015 CPM Order, the Commission did not determine that it was strictly necessary to include an accurate estimate of these costs for a reference unit in calculating the soft offer cap,[56] and we do not believe it is necessary here.

39. We disagree with Calpine's assertion that because an uncommitted resource remains subject to mandatory operation under exceptional dispatch, CPM is effectively a mandatory backstop procurement mechanism. The Commission has explicitly stated that CPM designations are voluntary.[57] Exceptional dispatch is separate from the CPM regime and the fact that resources may choose their preferred method of exceptional dispatch compensation (i.e., resources can elect to receive CPM designations or to be compensated through market revenues, based on their bid price, with the option of receiving supplemental revenues[58]) does not compel a resource to accept a CPM designation. We therefore disagree with Calpine that this compensation structure renders CPM to be a mandatory procurement mechanism that requires a different compensation approach.

40. Further, we find that Calpine's argument regarding weakened incentives for resource adequacy contracting is speculative and unsupported. In accepting CAISO's soft offer cap, the Commission found that "because the soft offer cap represents the high end of the range of current resource adequacy prices, it should not create incentives for load serving entities to forego bilateral resource adequacy contracts and, instead, rely on CPM backstop procurement."[59] As compensation above the CPM soft offer cap also represents the high end of the range of current resource adequacy prices, CAISO's proposal here should likewise not create incentives for load serving entities to forgo bilateral contracting.

41. We will not address comments regarding the level of the soft offer cap, the allocation of flexible attributes for annual CPM designations, the need for additional CPM market power mitigation measures, or potential deficiencies in the overall California resource adequacy framework or other CPM provisions that do not relate

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[56] *See id.*

[57] *See Cal. Indep. Sys. Operator Corp.*, 168 FERC ¶ 61,199 at PP 32, 38.

[58] CAISO Tariff, § 39.10.

[59] 2015 CPM Order, 153 FERC ¶ 61,001 at P 29.

directly to compensation above the soft offer cap. Comments raising these issues are beyond the scope of this section 205 proceeding, as CAISO is only proposing to modify compensation for resources who bid above the soft offer cap and is not proposing other changes to the CPM. Having found that CAISO's primary proposal is just and reasonable, we likewise will not address the merits of alternative compensation methodologies raised by commenters in this proceeding.[60]

The Commission orders:

CAISO's preferred tariff revisions are hereby accepted, effective June 1, 2020, as discussed in the body of this order.

By the Commission. Commissioner Glick is dissenting with a separate statement attached.

( S E A L )

Nathaniel J. Davis, Sr.,
Deputy Secretary.

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[60] *See, e.g.*, *City of Bethany v. FERC*, 727 F.2d 1131, 1136 (D.C. Cir. 1984) (when determining whether a proposed rate was just and reasonable, the Commission properly did not consider "whether a proposed rate schedule is more or less reasonable than alternative rate designs").

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation Docket No. ER20-1075-000

(Issued May 29, 2020)

GLICK, Commissioner, *dissenting*:

1. The California Independent System Operator (CAISO) has filed two options to reform how it compensates certain resources selected through its capacity procurement mechanism (CPM). Both options address the compensation for resources that seek to bid their capacity above a so-called "soft offer cap." Resources that bid above that soft offer cap must justify their bid based on their costs; resources that bid below the soft offer cap need not.[1] CAISO's first option permits resources to submit a bid above the soft offer cap up to a level that reflects their going-forward fixed costs[2] plus an adder equal to 20 percent of those going-forward costs. The second option permits resources to submit a bid that reflects the same costs, but without the 20 percent adder. Under either option, a resource that is selected through the CPM receives its bid price and also retains the market revenues it earns during the period of its CPM designation.[3]

2. Today's order accepts the first option. I dissent from that determination because CAISO has not shown that it is just and reasonable to allow CPM resources to receive an additional 20 percent adder on top of a resource's full going-forward costs *and* all market revenues. I do, however, believe that CAISO has shown that its second option, without the 20 percent adder, is just and reasonable.

3. As an initial matter, I recognize that either of CAISO's two options is likely an improvement over the *status quo*, which allows a resource to bid above the soft offer cap up to its full annual cost of service, including a return on and of capital, and retain all market revenues.[4] But section 205 of the Federal Power Act[5] requires a public utility to

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[1] *Cal. Indep. Sys. Operator Corp.*, 171 FERC ¶ 61,172, at P 3 (2020) (Order).

[2] Those costs are a resource's "(1) fixed operations and maintenance costs; (2) ad valorem taxes; and (3) insurance costs." *Id.* P 7.

[3] *Id.* P 12.

[4] *See id.* P 3.

[5] 16 U.S.C. § 824d (2018).

show that a proposed revision is just and reasonable, not just that it is a step in the right direction. Accordingly, the fact that both of CAISO's proposed options are improvements over the existing tariff does not relieve the Commission of its responsibility to determine whether those options are, in themselves, just and reasonable.

4. CAISO has failed to demonstrate that the first option, with the 20 percent adder, is just and reasonable. As CAISO's Department of Market Monitoring (DMM) succinctly put it, the "filing does not include any explanation or analysis of how or why a 20% adder is an appropriate level relative to potential costs of 'long term maintenance' and 'environmental upgrades' that would not be recovered under the rest of the CPM payment for going-forward fixed costs plus the unit's net market revenues."[6] Without such evidence, there is nothing in the record to support the Commission's finding that it is just and reasonable to allow resources that bid above the soft offer cap to recover 120 percent of the short-term fixed costs.[7]

5. The 20 percent adder is particularly troubling because, as noted, CPM resources retain all market revenues earned during the period of their CPM designation. Neither CAISO's filing nor today's order explains why we should presume that those market revenues are insufficient to cover a CPM resource's long-term investments or why an additional 20 percent of going-forward costs is appropriate on top of those revenues. Especially given the evidence of market power in the CPM process,[8] the Commission ought to provide some reason to believe that the 20 percent adder will be anything other than a windfall for high-cost generators before finding it just and reasonable.

6. Instead of pointing to any such evidence, both CAISO and the Commission rely on the Commission's acceptance of a 20 percent adder in establishing the current soft offer cap.[9] But that soft offer cap is based on the going-forward costs of a generic reference resource, not the going-forward costs of any particular resource. It is one thing to apply a percentage adder to the costs of a generic resource to ensure that the resulting offer cap covers comparable resources' going-forward costs. After all, a reference resource is supposed to be a representative estimate and will never perfectly reflect the costs of any

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[6] DMM Comments at 6.

[7] *Emera Maine v. FERC*, 854 F.3d 9, 27-28 (D.C. Cir. 2017) (explaining that the Commission had not met its burden to show that a rate was just and reasonable where it failed to point to any evidence indicating that the particular number set was, in fact, just and reasonable).

[8] *See* DMM Comments at 14-18 (discussing the "numerous indications that the CPM process has not been competitive on either a local or system basis").

[9] Order, 171 FERC ¶ 61,172 at P 36; CAISO Transmittal at 16, 19.

single real-world resource. But, under either of CAISO's two proposed options, a potential CPM resource bidding above the soft offer cap gets to recover its actual going-forward fixed costs,[10] eliminating that concern and ensuring that the resource will be able to use whatever it makes in the market to finance any necessary long-term investments. Accordingly, the fact that the Commission used a 20 percent adder when calculating the soft offer cap does not indicate that it is necessarily just and reasonable to apply the same adder on top of an individual resource's actual going-forward costs when calculating that resource's maximum bid.

7. To be clear, my position is not that any adder or other form of compensation on top of a resource's going-forward fixed costs and market revenues is categorically unjust and unreasonable. As DMM notes, it is conceivable that a resource could require additional revenue to cover its long-term costs and, if so, CAISO may want to consider ways for individual resources to recover those particular costs.[11] But the record before us does not provide any reason to believe that it would be just and unreasonable to provide *every* resource offering above the soft offer cap an additional 20 percent of its going-forward costs.

8. CAISO's second option does not provide a 20 percent adder and, therefore, does not present the concerns discussed above. In essence, that option requires resources to use their market revenues to cover long-term investments. Absent evidence suggesting that such revenue is insufficient to cover a resource's long-term costs—evidence which this record lacks—that approach more appropriately balances customer and generator interests and is, in my view, just and reasonable.

For these reasons, I respectfully dissent.

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Richard Glick
Commissioner

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[10] *See, e.g.*, Pacific Gas & Electric Comments at 16-17 (explaining that CAISO's proposed CPM "compensation formula is unit-specific and therefore would be guaranteed to cover the unit's going-forward fixed costs").

[11] DMM Comments at 3-4 (suggesting that "instead of employing a one size fits all 20% adder[, . . .] CAISO could allow a resource seeking compensation above the CPM soft offer cap to demonstrate any actual going forward costs needed for 'long term maintenance' and 'environmental upgrades' that would not be covered under the categories of going forward fixed costs that are recoverable under current CPM tariff provisions" and receive compensation sufficient to cover those specific upgrades).

Document Content(s)