CPM Soft Offer Cap

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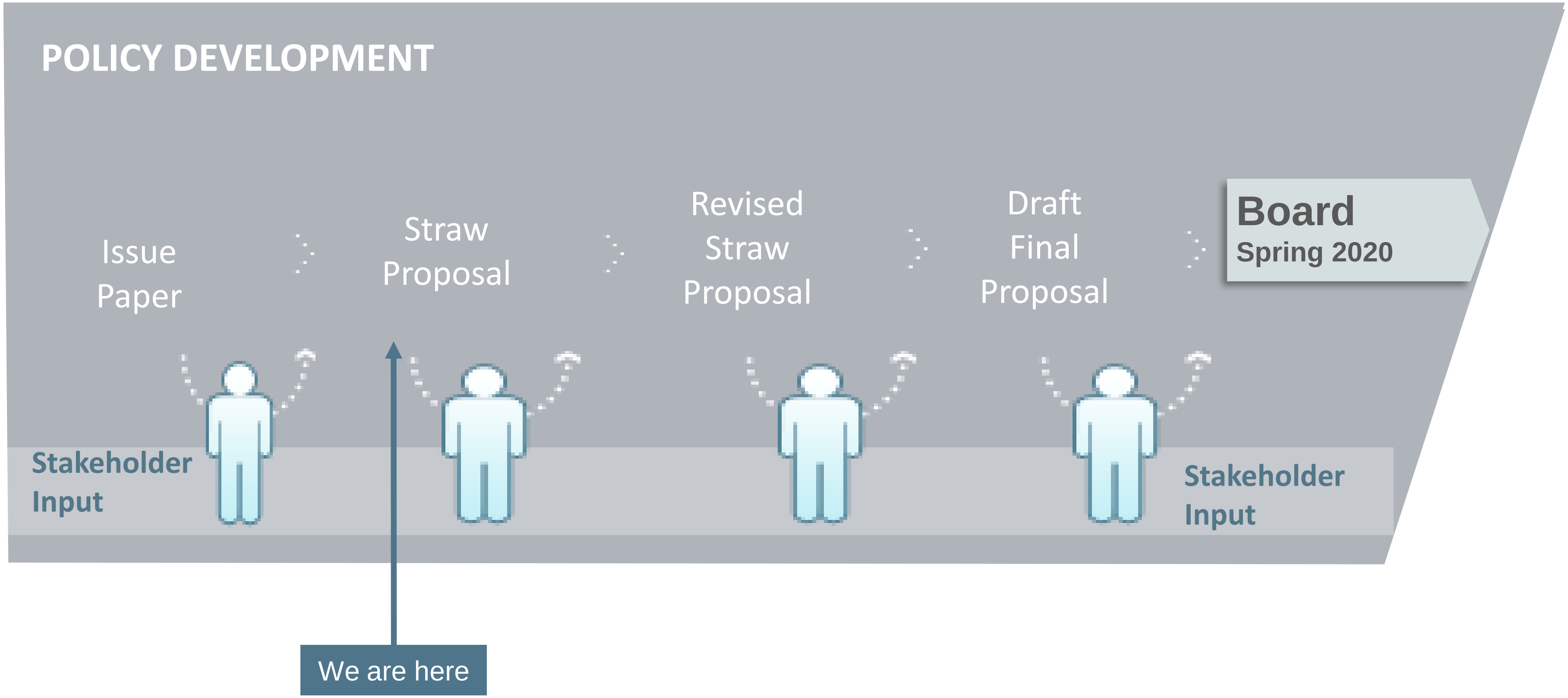
Stakeholder call – Straw Proposal
August 6, 2019

Agenda

Time	Topic	Presenter
9:00 – 9:10	Welcome / policy process	Kristina Osborne
9:10 – 10:30	Review straw proposal • Backstop background • Soft Offer Cap • Compensation for 12-month CPM • Bids above the soft offer cap	Gabe Murtaugh
10:30-10:35	Next steps	Kristina Osborne

Stakeholder Process



Process Timeline

Milestone	Date
Post Issue Paper	5/30/2019
Stakeholder Call	6/17/2019
Stakeholder Written Comments Due	7/1/2019
Post Straw Proposal	7/24/2019
Stakeholder Call	8/6/2019
Stakeholder Written Comments Due	8/20/2019
Revised Straw Proposal Posted	Sept 2019
Stakeholder Meeting	Sept 2019
Stakeholder Written Comments Due	Oct 2019
Draft Final Proposal Posted	Dec 2019
Board of Governors Meeting	Spring 2020

The ISO has mechanisms for backstop procurement, including the reliability must-run (RMR) mechanism

- ISO filed that the RMR mechanism is used to backstop for the retirement of an essential resource for reliability
  - Resources must submit a notice to retire or mothball from the ISO system
- Full cost of service compensation
  - Will serve to mitigate market power
  - Resources are required to bid 24x7 at marginal cost
  - Resources will not recover market revenues
- Designations are mandatory

The ISO also has the capacity procurement mechanism (CPM) backstop tool

- CPM is used to backstop the RA program
  - ISO only procures after a “cure” period
- Competitive cost compensation with market revenues
  - Bids for CPM are received through the competitive solicitation process (CSP)
  - In theory competitive bids are based on going forward fixed costs (GFFC), market risk, potential capital additions, acceptable return, and expected market rents
  - CPM resources recover market revenues
- Resources are procured for specific (local/system/flex) needs and have bidding requirements accordingly
- If the resource bids into the CSP designations are mandatory
- CPM designations are not administratively burdensome

CPM designations have a 'soft offer cap' to mitigate the exercise of market power

- Any resource bidding into the CSP may bid up to the soft offer cap, and bids will not be reviewed by the ISO
- Eligible capacity that does not bid into the CSP will automatically have bids inserted at just above the soft offer cap
- Resources may submit CSP bids above the soft offer cap, but bids must be cost justified – at FERC - based on cost of service
- The soft offer cap was set using going forward fixed costs for a new large gas fired combined cycle resource
  - GFFC includes insurance, ad valorem, and fixed O&M costs
  - These costs do not include capital and financing costs or taxes

The soft offer cap was initially set in a stakeholder initiative about 4 years ago and triggered this initiative

- Values from the 2014 Cost of New Generation report from the CEC were used to formulate the soft offer cap
- When the policy was implemented it included an obligation to review the soft offer cap every 4 years
  - New CEC study was filed in May
- To avoid piecemeal FERC filings, this initiative also considers:
  - Compensation and competitiveness for 12-month designations
  - Bids above the soft offer cap (RMR-CPM issue)
  - Potential other CPM related items

The ISO makes three major capacity procurement mechanism policy recommendations

1. Retain the existing soft offer cap of $75.67/kW-year ($6.31/kW-month)
2. Implement a 3-pivotal supplier test for annual designations and use cost of service compensation for designations made to resources that fail the test
3. Implement changes proposed in the RMR-CPM Enhancements initiative for bids above the soft offer cap

In comments several stakeholders suggested potential changes to the soft offer cap calculation

- The soft offer cap assumes that going forward fixed costs for a relatively new mid-cost combined cycle gas resource would likely be the price necessary to retain a resource procured through a CPM backstop by the ISO
- A combined cycle resource will likely not be the marginal resource in the future
  - May consider the cost of new storage resources or other technology types
  - Currently few of these resources on the system
  - Costs for these resources were not included in the 2018 CEC study
- Several comments asked for consideration of cost of new entry (CONE) to determine the soft offer cap
  - ISO does not feel this is appropriate given CPM is for adequately compensating <u>existing</u> resources necessary for the ISO to maintain reliable grid operations

Propose retaining the current $6.31/kW-month soft offer cap given CEC report does not justify change

- The ISO used going forward fixed costs (GFFC) for a CC resource plus 20% to initially calculate the soft offer cap
  - These values were obtained from the 2014 CEC cost of new generation report
- The 2018 CEC report indicated a decrease from $75.67/kW-year ($6.31/kW-month) to $70.67/kW-year ($5.89/kW-m)
- ISO discussed changes made between the two studies with the CEC to determine drivers of the change
  - Change from 550 MW CC resource to a 700 MW had largest impact
  - Several changes with smaller impacts

Stakeholders expressed concern around 12-month CPM compensation in comments

- Several stakeholders expressed concern for resources receiving 12-month CPM designations in the comments on the issue paper and in the RMR-CPM initiative
  - Concern that resources needed for reliability could receive $6.31/kW-month CPM payments
  - This may be possible because of infrequent local competition
  - Actual compensation needed for depreciated resources may be significantly less than the soft offer cap
  - Less concern for resources receiving 30 or 60 day designations

The ISO proposes a 3 pivotal supplier test for 12-month CPM designations

- The 3 pivotal supplier test examines ownership of eligible capacity that could meet backstop need
  - Capacity designated for RA, CPM or RMR is not eligible for consideration
  - The three largest suppliers will be removed and the residual available capacity will be compared to the local need
- If the available capacity fails the 3 pivotal supplier test, the CSP and standard compensation will not be used
- If the test does not fail, the CSP and typical CPM construct will be used for designation

Compensation for these CPM designations will be the same as the compensation for RMR

- Schedule F and Schedule L will be used to determine full cost of service for these designations
- Compensation will include:
  - Operations and maintenance expenses
  - Depreciation expenses
  - Return on taxable allowance
  - Variable costs from operation
  - Necessary annualized capital additions costs
- Compensation will not include market rents above what the resource costs to operate in the market

Full cost of service CPM designations

- Designations will only be made to full resources
  - Full cost of service paradigm is incompatible for partial resource designations

Will comply with all aspects of the RMR contract, these may include:

- Similar cost allocation to what exists today
- RA credit for all resource attributes will be allocated to the same entities receiving credit for the resource designation
- Resources receiving designations will be required to bid into the market 24x7 at variable costs
  - Bids will include all major maintenance and opportunity costs
  - All revenue above variable costs and major maintenance will be clawed back to prevent double recovery
  - AS and RUC bids will be at $0, similar to RMR resources
- Resources will be subject to RAAIM
- Extended offers from the ISO may be rejected
- No requirement for the resource to file a notice to retire or mothball with the ISO

Example: Full cost of service CPM designation to a 75 MW resource for a 50 MW deficiency

LSE	Req. (MW)	Shown (MW)	Shortage (MW)
1	100	100	
2	100	80	20
3	100	70	30
TOTAL	300	250	50

Initial Allocation	Residual Allocation
	100/300 * 25 MW
20/50 * 50 MW	100/300 * 25 MW
30/50 * 50 MW	100/300 * 25 MW

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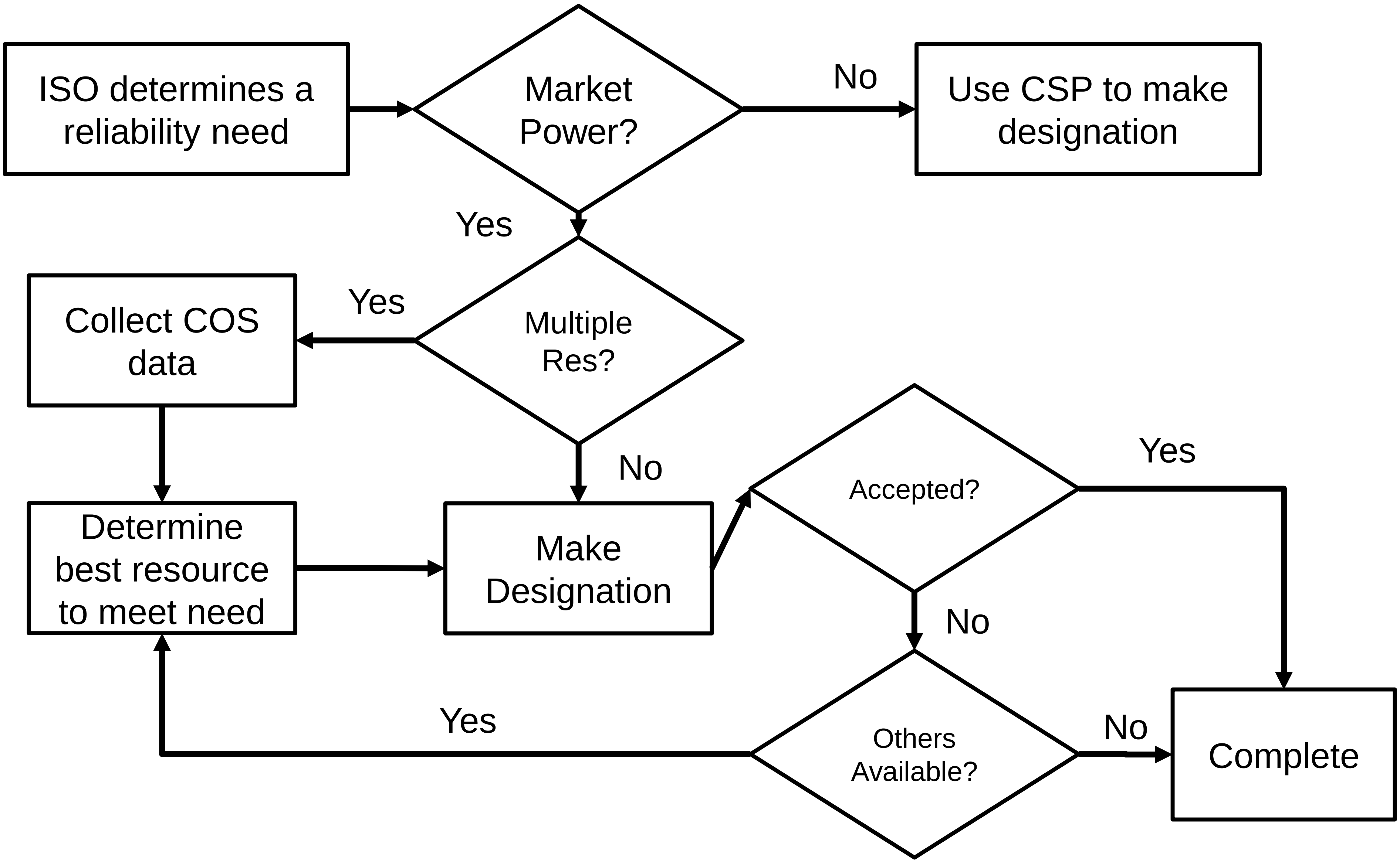
BACKSTOP: 50 MW

Decision tree for awarding 12-month CPM designations



The ISO is not proposing further changes to the enhancements proposed in the RMR-CPM initiative

- In the RMR-CPM initiative the ISO proposed updating bids above the soft offer cap to align with the CPM SOC
  - Current bids can reflect full cost of service, and are eligible to receive market revenues
  - Proposed bids will reflect GFFC+20% plus market revenues, with alternate sheet reflecting only GFFC plus market revenues
- This tariff language has not been filed at FERC yet, but will be included in this filing with CPM SOC
- The changes proposed in this initiative do not cause a need for changes to the proposal from the previous initiative
- The ISO has never made a CPM designation to a resource bidding above the soft offer cap

Next steps

Date	Milestone
August 20, 2019	Comments due
Sept 2019	Revised straw proposal publication
Sept 2019	ISO stakeholder call to discuss the revised straw proposal

Stakeholders are encouraged to submit written comments by August 20 to initiativecomments@caiso.com; use template available at following link: http://www.caiso.com/Documents/CommentsTemplate-CapacityProcurementMechanismSoft-OfferCap-StrawProposal.doc