



TO: YAKOUT MANSOUR, CAISO GOVERNING BOARD MEMBERS
FROM: GARY ACKERMAN AND ELLEN WOLFE, WESTERN POWER TRADING FORUM
SUBJECT: ICPM STAKEHOLDER PROCESS
DATE: SEPTEMBER 8, 2010

The CAISO Staff is currently developing a replacement for the Interim Capacity Procurement Mechanism (ICPM), as directed by FERC. Staff's proposal is scheduled to come before you for a vote in November. Staff's proposal has two concepts that are essentially non-starters for the independent generation community and to which WPTF objects: (a) it will not provide adequate compensation for resources needed for reliability; and (b) it will neither encourage nor support competitive capacity procurement in the state's Resource Adequacy (RA) program.

There is an immediate need for the CAISO Board to ensure that generators needed for reliability are receiving adequate compensation. The 2009 Department of Market Monitoring report identified a significant gap in the combined revenues that generators are receiving from the CAISO energy and ancillary services and CPUC RA programs and the revenues that generators need to remain viable. The CAISO's recently released 20% renewable report suggests that the problem is likely to worsen as renewable penetration increases. Further, the CPUC recently decided to hold its existing RA program as is, and, therefore, changes in generator compensation can only come from the CAISO modifying its existing rules. How can the CAISO expect the State of California to enjoy the benefits of a modern electric grid when merchant plants are being economically choked into obsolescence?

The Draft Final Staff proposal argues that the CAISO backstop procurement should not impact the State-jurisdictional forward bilateral RA markets. We fundamentally disagree. The mere fact that the CAISO needs to procure through ICPM warrants a signal such that the RA program can adjust to fill that need in the future. The CAISO recognized this interplay during the CPUC rulemaking on long term resource adequacy, where the CAISO argued that in the absence of a centralized capacity market, it is likely that the backstop procurement mechanism would need to fill the role of providing benchmark prices based on the cost of new entry for negotiating forward bilateral resource adequacy contracts. It is therefore

imperative that the CAISO and market participants craft a CAISO capacity procurement mechanism that is comprehensive and that complements the broader RA structure by encouraging efficient price signals and better resource procurement.

In light of these important considerations, we request that you direct CAISO Staff to: (a) revise its proposal so that its backstop procurement mechanism supports the formation of market price signals in the RA market, and (b) engage the CAISO Market Surveillance Committee (MSC) in order to further assist with a fuller evaluation of the issues associated with overall compensation and price mitigation, and to seek an opinion from the MSC on the technical merits of the market design alternatives at issue in this effort, including how they align with the comprehensive resource adequacy frameworks employed by other ISO/RTOs and with the objectives of both the CAISO markets and the broader RA program.¹

Thank you for your consideration.

¹ The MSC was asked to provide an opinion for the initial ICPM proposal two years ago but has not been asked to do so for the Replacement ICPM issue despite the criticality of the issue given the CPUC's failure to approve a centralized capacity mechanism, added CAISO needs, and the downward pressure on prices renewables are causing.