Decision on Commitment Cost Enhancements

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ISO market provides resources with the ability to indicate and recover costs of committing a resource.

- Resources incur costs when starting up and when running the resource at or above its minimum output level
  - If a resource's daily market revenues are insufficient to cover its commitment costs, a "make-whole" payment is provided
- Resources have two options for specifying start-up and minimum load costs
  - Proxy cost option calculated daily by the ISO
  - Registered cost option which is capped at a percentage above the proxy cost value and fixed for 30 days

Registered cost and proxy cost options share all cost items except for gas prices.

Option	Bid cap	Bidding flexibility	Gas price
Proxy cost	100 percent of daily calculated proxy cost	Daily bidding up to cap	Updated daily
Registered cost	150 percent of monthly calculated proxy cost	30-day hold	Fixed price over 30-day hold

Registered cost has higher cap to account for gas price volatility and costs not fully captured in proxy cost calculation

Under the current framework, February 2014 gas price spike event led to inefficient market dispatch.

- The majority of ISO gas-fired resources were on the registered cost option, which does not reflect daily gas prices.

- Proxy costs did not capture gas price increases that occurred after publication of daily gas price index.

- The ISO sought and received a temporary tariff waiver from FERC to address near-term gas price spikes.

- The ISO committed to a more comprehensive but implementable solution by the next winter.

Management proposes three targeted commitment cost enhancements to be implemented by this winter.

1) Increase the proxy bid cap from 100 to 125 percent;

2) Eliminate the registered cost option for most resources; and

3) Rely on a manual process to update day-over-day gas prices when they increase 25 percent or more.

Increase the proxy bid cap from 100 to 125 percent.

- Provides additional bidding flexibility.
- Addresses almost all historical instances of day-over-day and intra-day gas price volatility.
  - There have only been seven instances since April 2009 when the day-over-day gas increase exceeded 25 percent.
- Gas price increases beyond 25 percent are addressed by the proposed manual process.

Eliminate the registered cost option for most resources.

- No longer necessary due to increase in proxy cost cap
- Fixed 30-day cost does not reflect current gas prices
- Temporarily retain this option for “use-limited” resources that have environmental or operational restrictions
  - Use-limited resources may require a higher bid cap to reflect the cost of their limitations known as “opportunity costs.”
  - 30 day period acts as a market power mitigation measure.
  - Once an opportunity cost solution is implemented, use-limited resources will transition to the proxy cost option.

Rely on a manual process to update gas prices for day-over-day increases greater than 25 percent.

- Manually update the day-ahead market with the most recently available gas price index.

- Delay close of the day-ahead market to facilitate gas price update.

- Expected use of the process is limited but effective in ensuring efficient market dispatch.

- If necessary, use-limited resources on the registered cost option will be automatically switched to proxy during gas price spike periods.

Stakeholders largely support the commitment cost enhancements.

- Generally support increase in proxy cap.
- Stakeholders support temporary retention of the registered cost option for use-limited resources.
  - Stakeholders did not support delaying implementation of the remaining commitment cost enhancements until an opportunity cost methodology was developed.
- Overwhelming support for the use of the manual process to update daily gas prices.
- Some remaining concerns that increase in proxy cost bid cap is insufficient--cap should be increased to 150%.

Management recommends the Board approve the proposal.

- There is strong support for the commitment cost enhancements.
- The enhancements will provide significant market efficiency benefits by reflecting natural gas price volatility in the market dispatch.
- The enhancements provide additional bidding flexibility for market participants to manage their resources.
- The enhancements can be implemented by this winter.