

Memorandum

To: ISO Board of Governors

From: Eric Hildebrandt, Executive Director, Market Monitoring

Date: October 19, 2022

Re: Department of Market Monitoring report

This memorandum does not require ISO Board of Governors action.

EXECUTIVE SUMMARY

This memo provides comments by the Department of Market Monitoring (DMM) on two sets of rule changes being proposed by Management.

- **Washington WEIM greenhouse gas enhancements.** With Washington state's cap-and-invest program starting on January 1, 2023, the ISO must establish a method for calculating the WEIM imports for entities located in Washington. DMM does not oppose the ISO's proposal but recommends the ISO continue working with stakeholders to develop a more efficient approach – such as that implemented for California -- which allows the WEIM optimization to consider the emissions costs of resources outside of Washington that may be dispatched to serve load within the state.
- **Interconnection process enhancements.** The ISO is proposing to make some eligibility requirements for the interconnection process more stringent. The changes should improve the process by making some less viable projects ineligible for transmission allocation, thereby reducing the interconnection queue. An auction mechanism might price and allocate spots in the interconnection queue more efficiently, but an auction could be difficult and time consuming to develop.

This memo provides a more detailed discussion of both these proposals.

WASHINGTON WEIM GREENHOUSE GAS ENHANCEMENTS

Beginning January 1, 2023, the Washington state cap-and-invest program will require emitters to obtain allowances equal to their covered greenhouse gas (GHG) emissions. This will impact the costs faced by entities participating in the WEIM who may have obligations to obtain allowances based on their WEIM transactions. Washington's program will also impact the bids submitted into the WEIM market by suppliers potentially facing allowance obligations. Management proposes two minor enhancements to the WEIM in response to the launch of Washington's program.

The first change is to update the greenhouse gas reference levels used in limiting commitment costs and mitigating energy bids for resources within Washington. The reference levels will use a GHG allowance price that is specific to resources located the state. Before the first allowance auction establishes a market price, the reference levels will use an estimate of the price developed by a consulting firm for Washington's Department of Ecology. These enhancements should help keep the reference levels for resources within Washington participating in the WEIM close to the costs these resources can expect to incur after the start of the cap-and-invest program. DMM supports this aspect of the proposal.

Second, Management proposes a method for calculating the WEIM transactions that will be considered imports into the state for each WEIM balancing area located partly or wholly within Washington. The method that the ISO uses to determine what constitutes a WEIM import can impact greenhouse gas allowance obligations for load serving entities or supply resources participating in the WEIM. For a WEIM entity in Washington, the ISO proposes to report the entity's real-time load in excess of its base schedules as the "imports" that may be subject to a Washington state greenhouse gas allowance obligation. An entity with some load in the state and other load outside the state can determine its portion of load in Washington and calculate a pro-rata portion of these "imports" serving Washington.

With the cap-and-invest program starting on January 1, 2023, it is critical that the ISO establish a clear policy for calculating the WEIM imports for entities located in Washington. Not having a policy could create a larger risk of inefficient behavior or decreased participation in the WEIM than having a suboptimal policy. Therefore, DMM does not oppose the ISO's proposal for determining WEIM transactions counting as imports to Washington.

However, the ISO's proposal for addressing the GHG allowance obligations that can start accruing to load serving entities in Washington due to WEIM transactions may result in significant inefficiencies in the overall WEIM dispatch relative to an approach that allows the WEIM optimization to consider emission costs from WEIM energy imported into Washington. In particular, as the ISO has pointed out, resources in Washington including the cost of allowances in their energy bids may be displaced by similar or even higher emitting out-of-state resources whose emissions costs will not be reflected in the market optimization.

Shortly after the ISO published its draft final proposal, the Department of Ecology issued a rulemaking that resolved the critical ambiguities in their program's rules that had seemed to justify the ISO's simplified approach to calculating WEIM imports to Washington.¹ As a result, DMM recommends the ISO continue working with stakeholders to develop a Washington WEIM greenhouse gas attribution approach that allows the optimization to consider the emissions costs of resources outside Washington.

¹ Washington State Department of Ecology, *Concise Explanatory Statement Chapter 173-446 WAC Climate Commitment Act Program*, 173-446-040(3)(e)(iv), September 2022, p. 8: <https://apps.ecology.wa.gov/publications/documents/2202046.pdf>

DMM recommends the ISO consider developing a version of the “LADWP approach” to GHG accounting proposed in the EDAM revised straw proposal.² The LADWP approach is a relatively straightforward adaptation of the existing California WEIM greenhouse gas design, adjusted for a situation like for Washington, where the WEIM load serving entity, rather than the importing resource, has the obligation to procure the greenhouse gas allowances.

INTERCONNECTION PROCESS ENHANCEMENTS

Management proposes to make some eligibility requirements for the allocation of transmission plan deliverability more stringent. Specifically, the ISO proposes that power purchase agreements (PPAs) have a minimum of 5 years for a project to be eligible for a transmission allocation. If the interconnection customer’s power purchase agreement is not with a load serving entity, two conditions must be met for the project to be considered eligible for transmission allocation. First, the power purchase agreement with the non-load serving entity must meet the 5-year requirement. Second, the non-load serving entity must either demonstrate a contract selling resource adequacy capacity to a load serving entity for a minimum of 1 year, or submit a deposit equal to the higher of \$500,000 or \$10,000 per MW of allocated transmission deliverability.

The current size of the interconnection queue suggests that the cost for an entity to become eligible for transmission allocation is too low. With the price of transmission allocation eligibility too low, the ISO cannot assign priority to the highest value projects. The low price also creates inefficient and inequitable rent seeking opportunities. An interconnection customer could enter the queue without the intention of developing real assets. The intention could instead be to later sell its place in the queue to someone who is developing real assets. Such rent-seeking behavior can increase interconnection process wait times and costs for actual developers of real assets.

An auction mechanism to efficiently price and allocate spots in the interconnection queue might solve this issue. However, such an auction could be difficult and time consuming to develop. The ISO has instead proposed making some eligibility requirements more stringent or costly. The proposed enhancements should be implementable on a much shorter timeframe than a potential auction could.

These proposed changes should improve the interconnection process. Projects that meet the new requirements are more likely to be viable and provide value to the grid. The changes may also deter interconnection requests of more speculative nature, such as those intended to simply extract profits from the interconnection queue rather than to support development of economically viable projects.

² California ISO, *Extended Day-Ahead Market Revised Straw Proposal*, August 16, 2022, pp. 86-88: <http://www.caiso.com/InitiativeDocuments/RevisedStrawProposal-ExtendedDay-AheadMarket.pdf>