

ISOs/RTOs, the CAISO does not currently have a process to verify supplier costs prior to market clearing.⁴ However, the CAISO is currently undertaking a stakeholder process aimed in part at potentially modifying the CAISO's framework for determining bid cost reference levels including examining potential methodologies for market participants to submit cost-based bids or for the CAISO to verify costs based on market participant provided information.

Designing and implementing verification procedures as required by Order No. 831 will require careful consideration of the complexities of verifying cost-based bids, as well as ensuring consistency with the CAISO's larger market design efforts. Therefore, the CAISO needs to undertake the robust stakeholder process that is already in progress to examine the framework for determining bid cost reference levels. The CAISO anticipates holding additional working group meetings, issuing a final proposal, and bringing the proposal before the Board of Governors by the end of Fall 2017. The CAISO respectfully requests that the Commission grant it an extension until no later than May 1, 2018 to submit its compliance filing as required by Order No. 831.

I. Background

A. Order No. 831

On November 17, 2016, the Commission issued Order No. 831. Order No. 831 requires RTOs and ISOs to cap each resource's incremental energy offer at the higher of \$1,000/MWh or that resource's verified cost-based

⁴ As explained below, other ISOs/RTOs either have market power mitigation procedures that include provisions for determining cost-based reference levels based on cost-based bids submitted by market participants (e.g., PJM) or include provisions for adjusting ISO determined reference levels on a resource specific day-by-day basis using information provided by the market participant (e.g., NYISO, ISO-NE, MISO).

incremental energy offer.⁵ Each RTO and ISO must also cap verified cost-based incremental energy offers at \$2,000/MWh when calculating LMP.⁶ With respect to the verification requirement, the Commission determined that RTOs/ISOs must verify those costs before the offer can inform locational marginal prices.⁷

The Commission directed RTOs/ISOs to explain in their compliance filings what factors the RTO/ISO or its market monitor will consider in the verification process for cost-based incremental energy offers above \$1,000/MWh and whether the RTO/ISO considers such factors in existing market power mitigation provisions or whether new practices or tariff provisions are necessary given the final rule's verification requirement.⁸ The Commission also stated that in creating such a verification process, "we expect that the RTO/ISO would build on its existing mitigation processes for calculating or updating cost-based incremental energy offers."⁹

⁵ Order No. 831 at P 42.

⁶ *Id.*

⁷ The Commission stated that: "The costs underlying a resource's cost-based incremental energy offer above \$1,000/MWh must be verified before that offer can be used for purposes of calculating Locational Marginal Prices. If a resource submits an incremental energy offer above \$1,000/MWh and the costs underlying that offer cannot be verified before the market clearing process begins, that offer may not be used to calculate Locational Marginal Prices and the resource would be eligible for a make-whole payment if that resource is dispatched and the resource's costs are verified after-the-fact. A resource would also be eligible for a make-whole payment if it is dispatched and its verified cost-based incremental energy offer exceeds \$2,000/MWh." *Id.*

⁸ *Id.* at P 141.

⁹ *Id.*

To comply with the directives in Order No. 831, the Commission stated that each RTO and ISO is required to make a compliance filing amending its tariff to implement the final rule, due 75 days after the order's effective date (*i.e.*, May 8, 2017).¹⁰

B. The CAISO's Commitment Costs and Default Energy Bid Enhancements Stakeholder Process

A number of CAISO stakeholders have raised concerns that the CAISO's current market design introduces risks that their units could be inaccurately valued in the market processes, reducing the efficiency of market solutions and potentially compromising cost recovery.¹¹ In response to these concerns, the CAISO initiated the Commitment Costs and Default Energy Bid Enhancements stakeholder process. As part of this process, the CAISO released an Issue Paper on November 18, 2016. Therein, the CAISO explained that this stakeholder process would focus on: (1) evaluating its bidding flexibility design, and (2) determining whether to pursue design modifications.¹²

To address stakeholder concerns, the CAISO is reviewing both commitment costs and default energy bids through this process. In particular, the CAISO is considering options focusing on making bids and mitigation more reflective of suppliers' actual cost expectations, including potentially moving from mitigated price reference levels based solely on published natural gas prices indices to reference levels based

¹⁰ *Id.* at P 220. Order No. 831 was published in the Federal Register on December 5, 2016, and became effective February 21, 2017. Therefore, RTO and ISO tariff compliance filings are due by May 8, 2017.

¹¹ Commitment Costs and Default Energy Bid Enhancements issue paper ("Issue Paper") at 6. A copy of the Issue Paper can be found at: https://www.aiso.com/Documents/IssuePaper_CommitmentCost_DefaultEnergyBidEnhancements.pdf

¹² *Id.* at 4.

either on suppliers' bid-in cost-based offers or alternatively based on *ex ante* adjustments to natural gas price reference levels based on published natural gas prices indices, based on suppliers' expectations of actual fuel costs. The stakeholder initiative is also examining related topics including potential changes to the market power mitigation method for commitment costs and allowing hourly variation in minimum load costs.

As part of this stakeholder process, the CAISO is developing the standards against which it would verify a supplier's submitted cost-based bid. This will include potential changes to the cost components that are acceptable to be included in bids and the basis for determining the costs of these individual components. For example, the CAISO and stakeholders are currently examining the degree of cost risk that can be included in bids and the basis for determining natural gas costs and hydro opportunity costs. In conjunction with this, the CAISO and stakeholders will develop the types of information that a supplier would have to provide to support their claimed costs and the CAISO's procedures for using this information to verify costs. For instance, the CAISO currently has no established standards for verifying natural gas cost information submitted by suppliers. The CAISO establishes reference levels used in its market power mitigation process by using published natural gas price indices. Though the CAISO tariff has provisions for negotiated default energy bids, the cost inputs for these are fixed and do not include provisions for day-by-day adjustments to fuel prices based on cost information submitted by a supplier and upon a supplier's request for an adjustment. The CAISO provisions use fuel costs as published in an index.

Although this initiative was originally focused on the cost basis of reference levels used for market power mitigation, the CAISO would use these same procedures for verifying costs of bids greater than \$1,000/MWh, as required by Order No. 831, both in terms of the *ex ante* and *ex post* verification processes required by the final rule. Because of this overlap, the CAISO determined that the most efficient course was to merge the Order No. 831 compliance requirements into its ongoing stakeholder process. The CAISO is currently conducting a series of working group meetings with stakeholders and plans to issue a final proposal, bringing that proposal to its Board of Governors by the end of Fall 2017. The CAISO also anticipates filing the resulting tariff changes with the Commission in 2018. After that time, the CAISO will be able to make its Order No. 831 compliance filing based on the bid-verification process that results from this stakeholder process.

II. Motion for Extension of Time

The CAISO respectfully requests an extension of time to file updated tariff provisions in compliance with Order No. 831. Specifically, the CAISO requests an extension so that it can develop and implement provisions necessary to verify cost-based energy bids over \$1,000/MWh through the stakeholder process that was already ongoing at the time Order No. 831 was issued, and in which the CAISO and its stakeholders are considering substantially similar issues.

In Order No. 831, the Commission directed each RTO/ISO to explain in its compliance filing the factors that will be considered by the RTO/ISO or its market monitoring unit in the process for verifying incremental energy offers above the

\$1,000/MWh price cap.¹³ The Commission determined that this requirement was not needlessly cumbersome because RTOs/ISOs could “build on existing processes for market power mitigation.”¹⁴

The CAISO plans to fully comply with the Commission’s directives in Order No. 831. However, the CAISO does not have an existing process for market power mitigation that is sufficient to comply with the requirements of Order No. 831. The CAISO’s existing market power mitigation process is based on administratively calculated reference prices (known as “default energy bids”). While these prices represent a reasonable proxy for a resource’s average costs, they would not be sufficient to validate individual cost-based offers prior to market clearing timeframes, as is required under Order No. 831. In this respect, the CAISO is different from other ISOs/RTOs, which either have market power mitigation procedures that include provisions for determining cost-based reference levels based on cost-based bids submitted by market participants (*e.g.*, PJM, SPP), or include provisions for adjusting ISO/RTO-determined reference levels on a case-by-case basis using information provided by the market participant (*e.g.*, NYISO, ISO-NE, MISO). Therefore, substantial refinements are necessary in order for the CAISO’s mitigation methodology to be sufficient for purposes of compliance with the validation requirements of Order No. 831.

The CAISO is already considering such refinements as part of its Commitment Costs and Default Energy Bid Enhancements stakeholder process. Indeed, one of the primary goals of this stakeholder process is to examine potential market enhancements

¹³ Order No. 831 at P 141.

¹⁴ *Id.*

that would provide greater flexibility to ensure mitigated prices are reasonable reflections of suppliers' cost expectations.¹⁵ This tracks the Commission's expressed goal in Order No. 831 to "ensure that all suppliers have an opportunity to recover their costs."¹⁶ This issue was driven in large part by stakeholder concerns that their CAISO default energy bids have certain limitations and do not adequately reflect incremental costs, resulting in undervalued default energy bids.¹⁷ In its Issue Paper, the CAISO proposed a number of possible enhancements to address these concerns, including (a) considering moving from a reference level mitigation methodology to one based on daily submitted bid-in cost-based offers; and (b) retaining a reference level mitigation methodology but introducing *ex ante* fuel price adjustments to reduce the risk that suppliers will be faced with mitigated prices that do not reasonably reflect their expected costs.¹⁸

Permitting the CAISO an extension of time in order to develop the Order No. 831 compliance provisions in conjunction with this stakeholder process is appropriate. In Order No. 831, the Commission encouraged RTOs/ISOs to build on existing processes for market power mitigation.¹⁹ The Commission did so in recognition of the fact that there are numerous complexities associated with the verification of incremental energy offers, including the need to ensure appropriate price mitigation.²⁰ These statements support the CAISO continuing to develop its Order No.831-compliant bidding and

¹⁵ Issue Paper at 7.

¹⁶ Order No. 831 at P 4 (footnote omitted).

¹⁷ Issue Paper at 30.

¹⁸ *Id.* at 35.

¹⁹ Order No. 831 at P 141.

²⁰ *Id.*

verification process in conjunction with its existing stakeholder process. As explained above, the CAISO, unlike other ISOs/RTOs, does not have an existing market power mitigation process that it can leverage to verify individual cost-based energy offers. Therefore, even if the CAISO had not already initiated a stakeholder process to address these types of issues, the CAISO would still need to develop the verification procedures required by Order No. 831, and would do so through a new stakeholder process.

However, because the CAISO has already begun considering these issues, it is important that the yet-to-be-determined enhanced mitigation methodology developed to comply with Order No. 831 function in an integrated and holistic fashion with the CAISO's current market design goals, especially with respect to any commitment cost and default energy bid modifications that the CAISO and its stakeholders may wish to implement. Attempting to carry out any or all of the Order No. 831 directives in a manner detached from this process would risk inconsistent design approaches, which would undermine the efficient functioning of the CAISO's markets and likely necessitate further modifications to address those consequences. For instance, the CAISO has stressed that any increased bidding/market power mitigation flexibility would need to be balanced with appropriate mechanisms to protect against market power abuses.

Also, significant time and resources have already been devoted to this initiative. When the Commission issued Order No. 831, the CAISO had had already initiated its stakeholder process. To date, the CAISO has posted an issue paper, solicited written comments on that paper, and held multiple working group meetings.²¹

²¹ Working group meetings have been held March 30, 2017 and April 20, 2017. See https://www.caiso.com/informed/Pages/StakeholderProcesses/CommitmentCosts_DefaultEnergyBidEnhancements.aspx.

For these reasons, it is appropriate for the CAISO to implement the modifications necessary to comply with the Order No. 831 directives in the context of its existing commitment cost and default energy bid stakeholder process. Doing so is most likely to result in a robust bid verification process. The CAISO plans to hold additional working group meetings, issue a final proposal, and bring that proposal to its Board of Governors by the end of Fall 2017. The CAISO also anticipates filing the resulting tariff changes with the Commission early next year. Therefore, the CASO respectfully requests that the Commission grant it an extension until no later than May 1, 2018 to file the compliance filing required by Order No. 831.

III. Conclusion

For the foregoing reasons, the CAISO respectfully requests that the Commission grant an extension of time until no later than May 1, 2018 to file the tariff changes directed in Order No. 831.

Respectfully submitted,

Roger E. Collanton
General Counsel
Anna A. McKenna
Assistant General Counsel
California Independent System
Operator Corporation
250 Outcropping Way
Folsom, CA 95630
Tel: (916) 608-7182
Fax: (916) 608-7222
rcollanton@caiso.com

Michael Kunselman
Alston & Bird, LLP
950 F Street, NW
Washington, D.C. 20004
Tel: (202) 239-3395
Fax: (202) 654-4895
michael.kunselman@alston.com

Counsel for the California Independent System Operator Corporation

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