PG&E's Comments re: Cost Allocation Guiding Principles Straw Proposal

Submitted by		Company	Date Submitted
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A. Introduction

Pacific Gas & Electric (PG&E) appreciates the opportunity to participate in the CAISO's stakeholder process to develop cost allocation guiding principles and to submit comments regarding the February 14, 2012 Straw Proposal. PG&E applauds the CAISO's commitment to this important initiative, its sense of urgency to establish the guiding principles, and the application of these principles to the Flexible Ramping Product.

PG&E supports five of the seven proposed guiding principles. PG&E proposes the CAISO eliminate the "Policy Alignment" principle and revise the "Manageable" principle to better reflect the CAISO's intent.

B. Summary of CAISO's Straw Proposal

The CAISO intends, through this stakeholder initiative, to establish a set of cost allocation guiding principles that can be applied throughout the market. The CAISO plans to first apply these guiding principles to the Flexible Ramping Product currently being developed. Later in 2012, the CAISO will commence a subsequent stakeholder initiative to review existing cost allocations that it currently uses in its markets to ensure they are consistent with the cost allocation guiding principles developed through this process.

The seven guiding principles proposed in the Straw Proposal are:

1. **Causation** - Costs will be charged to resources and/or market participants that benefit from and/or drive the costs. It is a fundamental tenant of just and reasonable energy markets that costs are allocated in this manner.

2. **Comparable Treatment** - Similarly situated resources and/or market participants should receive similar allocation of costs. This principle is similar to "Causation" above, but is intended to emphasize non-discrimination as well as avoiding special treatment of different types of technologies and/or market participants.

3. **Policy Alignment** - Supports the economically efficient achievement of state and federal policy goals. Economic efficiency is achieved through the design and allocation of costs in the CAISO market, incorporating costs/benefits in the bilateral capacity market, and providing additional cost transparency in the CAISO market for other policy decisions.

4. **Incentivize Behavior** - Profit maximization by market participants that are allocated the costs should lead to lower costs incurred by the CAISO market over a reasonable timeframe.

5. **Manageable** - Market participants should have the ability to manage exposure to the allocation. The market design should seek to minimize variability and complexity of the allocation and maximize the transparency of cost drivers.

6. **Synchronized** - The cost drivers of the allocation should align as closely as possible to the selected billing determinant.

7. **Rational** - Implementation costs/complexity should not exceed the benefits that are intended to be achieved by allocating costs.

C. PG&E Comments

PG&E supports five of the seven proposed guiding principles. PG&E proposes the CAISO eliminate the "Policy Alignment" principle and revise the "Manageable" principle to better reflect the CAISO's intent.

Policy Alignment Principle

The intent of the "Policy Alignment" principle is not entirely clear from the brief description provided by the CAISO. However, a generalized principle aligning cost allocation rules to support any particular state or federal policy could be used to justify cost allocation subsidies or carve outs for a particular class of resources or market participants. This "Policy Alignment" principle could lead to an "exception to the rule" for several different policies, which would entirely defeat the purpose of establishing cost allocation principles. PG&E does not support this outcome and strongly recommends the CAISO eliminate the principle of "Policy Alignment."

Cost allocation methodologies should reflect a fair and reasonable allocation to all participants and should not create special cases of participants who are free riders. Equal treatment is key to promoting efficient markets through unbiased price signals and just treatment to all CAISO's participants. In fact, unbiased market prices are useful to understand the cost and benefit of policy goals. Clear price signals provide policy makers the necessary feedback to adjust and develop new policy goals.

Moreover, PG&E notes changing ad hoc cost allocation rules that may seem to align with short-term policy initiatives is not easy. A good example of how difficult it is to change an allocation methodology to better reflect cost causation is the Participating Intermittent Resource Program (PIRP). Stakeholders spent most of 2011 attempting to revise the allocation of uninstructed energy cost to intermittent resources, only to see the stakeholder process end inconclusively. The experience with PIRP is instructive. Once an allocation methodology takes root to support a policy end, any attempt to modify that allocation to a more just and reasonable methodology is often difficult.

Manageable Principle

The CAISO provided further clarification during the conference call regarding this principle, and PG&E asks that the CAISO revise this principle to reflect the clarification. According to the CAISO, the intent of this principle is that cost should be predictable based on a participant's behavior. For example, if the cost to procure flexible ramp-up for a day was high, but only one participant deviated modestly, that participant would unexpectedly receive the majority of the cost. This is an example of a participant receiving an unpredictable allocation and can be addressed by capping the allocation amount to any one participant. However, if this situation is a common occurrence, it is indicative of an underlying issue. In this example, the CAISO may have set an excessive flexible ramp-up requirement, resulting in excessive cost to allocate. PG&E supports this principle of predictability and asks the CAISO revise the principle and consider renaming it "Predictability."

Other Guiding Principles

PG&E's largely supports the other five principles.

Causation and **Incentivize Behavior**: These principles are the keys to good cost allocation. As noted by the CAISO these two principles are really the opposite sides of the same coin. PG&E strongly supports these principles.

Rational: Having the benefits outweigh the administrative cost is a common sense principle which PG&E supports.

Comparable Treatment: PG&E supports the notion that cost allocation rules should be technology and participant neutral.

Synchronized: PG&E supports using allocators that are closely aligned with the cost drivers.