

Shell Energy North America (US), L.P.

Comments to CAISO Commitment Cost Enhancements Phase 2 Straw Proposal, October 29, 2014

Mike Evans, Shell Energy, michael.evans@shell.com, 858-526-2103

November 19, 2014

Shell Energy appreciates the opportunity to provide comments to the October 29, 2014 CAISO proposal: Commitment Cost Enhancements Phase 2 Straw Proposal. Our comments focus on the fundamental nature of the market and the appropriate accommodations for the calculation of opportunity costs.

Operation of a market – As a point worth remembering, the original intent of the “market” was to allow suppliers to offer energy at a bid price, the ISO would then select bids in merit order and choose a set of energy bids that met economic and reliability needs. Over the past 16 years, the idea of submitting bids has gradually been replaced by default bids, dispatch at minimum loads and other mechanisms which have not accurately reflected a market. It would be helpful to keep in mind as these types of proposals are devised, markets do provide a more efficient outcome than “command and control.”

Calculation of Opportunity Costs – The ISO may have underestimated the complexity of calculating opportunity costs. However, the proposal does allow for a negotiated value which will likely be the predominate choice of market participants. The time horizon for calculating opportunity costs changes as a function of a unit’s limitations. Often the most stringent limitation is the air permit, which may have annual limits or rolling 12-month average emissions limits, and which cover multiple emission constituents. SCs with peaker use limited resources spend considerable time and effort managing the dispatch of those peaking units within environmental limits, which include both daily and annual or 12-month rolling average. The ISO will have significant work either calculating this data or trying to determine an automatic optimization algorithm.

It is appropriate for the MSC to indicate that it is appropriate and “more efficient to allow high start-up and minimum load bids that reflect opportunity costs of operation...” This does not necessarily mean that the ISO has to calculate those costs, or potentially the ISO could set caps, under which the SC could provide bids, assuming that the caps were sufficiently high that the SC could manage the annual dispatch of the unit under those caps. While it would appear that the ISO is in fact establishing a cap that includes an opportunity cost, the data feeding the calculation and the short term nature of the use of the cap appear so limiting that it will not actually allow the SC to manage the annual/rolling 12-month generation average of the units which it manages. A cap must be sufficiently high that it reflects the dispatch period for the limitation. It is also important to note that the goal of the SC is to obtain winning bids, or to ensure that the unit is dispatched. Thus, there is a balance in which the ISO should have a level of confidence that bidders do want their units to be operated, and that they will thus continue to provide bids in anticipation of operating within their use limitations.

In Section 6.2.1, the ISO seeks input on use of a historical gas price for calculating energy costs. Historical prices have no relationship to future prices. Again, an SC managing its portfolio can procure forward gas or obtain forward gas prices and optimize its bids to manage the hours of operation of the peaker. It is unclear how the ISO would have access to this data, but the ISO would need to utilize forward gas prices. They could subscribe to price forecasting services, for example. In fact, the ISO may consider that allowing an SC to operate under some type of bid cap, which is sufficiently high enough, would be a more optimal solution.

In Section 6.2.4.2, the ISO provides an example where only two of the five peakers modeled had positive opportunity costs. Again, the concern would be that the ISO is not accurately calculating the opportunity cost. The ISO may want to consider that their modeling is simply not accurate enough to reflect the volatility of the market.

In conclusion, it may be appropriate to establish a cap, high enough to allow bidding opportunity costs such that the ULR is able to optimize operation over the rolling or annual 12-month period, within the unit's constraints. SC's currently spend considerable time optimizing dispatch and ensuring that a unit is operated within those limits. A back cast may also be appropriate to evaluate whether the unit was effectively utilized, at which later time, the CAISO could again review its procedures. It would be unfortunate for the ISO to set limits that would artificially constrain or limit bids such that the unit was operated too often, and used up its allowable hours of operation prematurely. This would also have significant impacts on its RA obligations, or the ISO's liability for mis-operation of the unit. The ISO design should offer enough flexibility to the SC to allow the SC to manage the dispatch of the unit through the bidding process to ensure that the unit is available throughout the year and throughout the RA obligation period.