Calpine comments on the August 11, 2014 Reliability Services Revised Straw Proposal

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Calpine appreciates the opportunity to comment on the revised straw proposal. Calpine's comments focus on the availability incentive mechanism and revised rules for replacement and substitution. Calpine believes that the proposed single availability assessment for both system and flexible capacity is overly complex and lacks a clear analytic justification. Calpine believes that the CAISO should assess and reward the availability of system and flexible RA separately. Calpine strongly supports the significant streamlining of replacement and substitution rules in the proposal.

*Availability Incentive Mechanism*

The CAISO proposal has three main elements: (1) The CAISO will use whether a resource was bid or scheduled to determine availability, rather than whether or not a resource is on a forced outage; (2) The CAISO will assess availability relative to a fixed target rather than a target that is updated to reflect the historic availability of the RA fleet; (3) The CAISO will calculate a single measure of availability for each resource that reflects its compliance with both the generic and/or flexible must offer obligations. Availability will be rewarded based on a single price applied to this single availability metric.

Calpine is not opposed to the first two elements of the proposal, but Calpine does not support the third element, i.e., assessing the availability of both flexible and generic RA using a single combined metric and providing a single availability incentive payment for both generic and flexible capacity. Ideally, penalties should be related to the cost of replacement capacity. If penalties are below the cost of replacement capacity, suppliers may prefer not to replace rather than comply with the relevant must-offer. If penalties are above the price of replacement capacity, then penalties will artificially inflate RA prices to reflect the risk of incurring penalties. By combining the availability assessments of both flexible and generic RA into a single assessment, suppliers do not necessarily face penalties reflecting replacement cost. For example, a supplier's exposure to penalties might be no greater than the single penalty price regardless of whether it has sold flexible RA alone, generic RA alone, or both flexible and generic RA.

Calpine believes that the CAISO should calculate and reward flexibility separately for generic and flexible RA capacity. The CAISO's primary justification for a single availability metric and incentive payment is that separate metrics and incentive payments might lead to "double the availability incentive risk compared to a generic resource" for a flexible resource that is forced out and hence can comply with neither the generic nor the flexible must-offer obligation. Resources only would be subject to "double" the availability incentive risk in specific circumstances, for example, if each hour of availability had the same weight in each separate availability calculation and the prices used to calculate incentive payments also were the same. This would not be case if, for example, the availability for flexible RA were calculated over many more hours and/or incentive payments for flexible RA were calculated using a lower price.

Calpine does not find persuasive the CAISO's arguments in Appendix B of the proposal against separate availability incentives for flexible and system RA. For example, the CAISO argues that using a low price to calculate availability incentive payments for flexible capacity would "undervalue flexible capacity." In fact, the limited information available about flexible capacity suggest that it is not particularly valuable and can be procured and replaced cheaply—although the pricing will be influenced by whatever availability incentive mechanism is adopted, e.g., high potential penalties could lead to higher prices. In addition, the CAISO argues that a low penalty price would provide insufficient incentives to comply with the flexible RA must-offer obligation. In fact, suppliers have additional incentives, beyond any availability incentive payments, to offer economic bids in CAISO markets and hence comply with the flexible RA must-offer obligation including better opportunities to exploit differences between day-ahead and real-time prices and earn bid-cost recovery compensation. In light of these additional incentives, it is unclear that high penalties are necessary to encourage compliance with the flexible RA must-offer obligation.

*Replacement and Substitution*

Calpine strongly supports the CAISO's proposed changes to replacement and substitution rules, which would greatly simplify replacement and substitution by allowing most planned outages to be coordinated between suppliers and the CAISO without involving LSEs.

With respect to the details of the proposal, section 9.2.5 of the proposal specifies, "If the capacity substituted in is at a higher quality that the original capacity on outage, the substitute capacity must still comply with the higher category must-offer requirements." Calpine requests clarification that for substituted capacity, there is no obligation for it to satisfy the must-offer obligation for the highest flexible category for which it is physically eligible, e.g., if a resource that is capable of providing category 1 flexible RA is used to substitute for category 2 flexible RA that the SC for the substituted resources could choose to subject the substitute resource to the less onerous category 2 must-offer obligation.

Calpine particularly supports the changes to local substitution rules proposed in section 10.3.6. Calpine regularly sells capacity from resources in local areas as system RA and has had longstanding concerns about onerous requirements to replace such resources with local resources even when they have been sold as local.