

Memorandum

To: ISO Board of Governors
From: Anna McKenna, Vice President of Market Policy and Performance
Date: March 9, 2022
Re: **Decision on central procurement entity implementation and RAIM settlement modification**

This memorandum requires ISO Board of Governors action.

EXECUTIVE SUMMARY

Management proposes tariff changes to accommodate a new central procurement entity (CPE) market participant structure. The California Public Utilities Commission (CPUC) recently issued an order to designate a CPE to procure local resource adequacy resources on behalf of load serving entities under its jurisdiction. A local regulatory authority, like the CPUC, can designate a CPE to procure capacity, and for the CPE to demonstrate to the ISO local resource adequacy resources on behalf of its jurisdictional load-serving entities.

Management proposes the following changes to implement the CPE are as follow:

- New tariff language to recognize a CPE that will be represented by a scheduling coordinator; and
- Clarification of how the CPE would be treated under existing capacity procurement mechanism processes and associated cost allocation.

While the CPUC has designated CPEs for use by its jurisdictional load serving entities, Management is proposing a generic CPE framework in the tariff so that any local regulatory authority can leverage a CPE to procure local resource adequacy resources on behalf of its load serving entities.

Unrelated to the CPE implementation, Management also proposes to modify its resource adequacy availability incentive mechanism (RAAIM) settlement to eliminate the monthly roll-over and annual true-up of unallocated RAIM funds. Instead, the ISO will allocate all excess RAIM funds to metered demand on a monthly basis.

Management's proposal will resolve the potential for funding shortfalls and the resulting need to file waiver requests with FERC related to this issue.

Moved, that the ISO Board of Governors approve the central procurement entity implementation and the resource adequacy availability incentive mechanism settlement modification, as described in the memorandum dated March 8, 2022; and

Moved, that the ISO Board of Governors authorize Management to make all necessary and appropriate filings with the Federal Energy Regulatory Commission to implement the proposal described in the memorandum, including any filings that implement the overarching initiative policy but contain discrete revisions to incorporate Commission guidance in any initial ruling on the proposed tariff amendment.

DISCUSSION AND ANALYSIS

CPE Implementation

In June 2020, the CPUC completed a two year stakeholder process to develop a central buyer system for local resource adequacy capacity. The goal of the central buyer is to provide "cost efficiency, market certainty, reliability, administrative efficiency, and customer protection." Due to scarcity of local resources and the proliferation of load serving entities, a central buyer system was adopted in the hopes of reducing market power and lowering costs of local resources in the bi-lateral resource adequacy market. To maintain retail choice, system and flexible resource adequacy procurement will remain with load serving entities.

Starting in resource adequacy year 2023, the CPUC will no longer assign a local resource adequacy obligation to individual load serving entities under their jurisdiction. Instead, the CPUC will assign each CPE their respective local resource adequacy capacity obligation. The CPE will in turn be responsible for procuring local resources on behalf of its load serving entities and make showings at the ISO to fulfill those obligations. If the ISO needs to procure backstop capacity under the capacity procurement mechanism because a CPE failed to meet its assigned local resource adequacy capacity obligation, then Management proposes to allocate the costs of that procurement to the deficient CPE.

The CPUC ordered PG&E and SCE to each form a CPE to procure local resource adequacy capacity within their respective transmission access charge areas. San Diego Gas & Electric was not ordered to form a central procurement entity.

RAAIM Settlement Modification

The RAIM assesses non-availability charges and makes availability incentive payments to scheduling coordinators based on the availability of their resource adequacy resources. The ISO determines the charges and payments based on how

often during the calendar month a resource's resource adequacy capacity was bid into the ISO's market. This bidding history is then translated into a monthly availability percentage. Based on that percentage, a resource adequacy resource may be eligible for an availability incentive payment, or subject to a non-availability charge. There is a limit placed on the amount of availability incentive payments that are allocated in any month to avoid windfall payments to any particular market participant. However, there is not a limit on the amount of non-availability charges that are collected. Any excess non-availability charges above this limit are carried over and used in future months. At the end of the year, any excess funds are distributed to load serving entities.

The current monthly roll-over and annual true-up can create a financial burden and tariff compliance issues for the ISO when a settlement recalculation identifies that a resource adequacy resource is due a refund or reduction in RAIM charges without sufficient RAIM roll-over funds to cover the refund amount. In fact, this occurred in April 2020, requiring the ISO to seek a FERC waiver to pay the refund from the ISO's reserve account. In this waiver request, the ISO committed to seeking a long-term solution to prevent this funding shortage from happening again, leading to this proposed tariff modification.

PROPOSAL

Proposed Changes to Accommodate a CPE into the Resource Adequacy Showings Process:

When assigned a local obligation by a local regulatory authority, the CPE will be responsible for submitting annual and monthly resource adequacy plans to the ISO following existing resource adequacy plan submission timelines. The CPE will be subject to penalties for late or missing submissions.

Management proposes to revise the tariff to specify that the CPE is responsible for aggregate procurement of local capacity area resources. This change reflects that, under the establishment of the new CPE role, this function will no longer be performed by the scheduling coordinator for load serving entities.

Management proposes to modify tariff sections that specify how CPUC-jurisdictional load serving entities are assigned local resource adequacy obligations and give the CPUC the flexibility to assign a local resource adequacy obligation to a CPE or a load-serving entity. Management also proposes to continue to directly assign non-CPUC jurisdictional load serving entities a local obligation using the tariff defined default allocation methodology. Management proposes to create an annual window in which a local regulatory authority may choose to shift all or part of their jurisdictional load serving entities' local resource adequacy obligation to a CPE, and to allow local regulatory authorities to assign their load serving entities local obligations to the same CPE. Management also proposes the flexibility to allow different local regulatory authorities to designate the same CPE if desired.

A CPE serves a procurement function, and not a load-serving function. Because a CPE will not serve load, the ISO's tariff and settlement provisions that are based on load-share ratio will not apply to a CPE. Therefore, Management proposes that CPEs be exempt from tariff provisions that cap a load serving entity's local resource adequacy obligation at their system resource adequacy obligation in the monthly resource adequacy process.

On a separate but related issue, this tariff provision can have unintended consequences for load serving entities like the California Department of Water Resources that serve load in multiple transmission access charge areas. Such entities are allocated a local resource adequacy obligation in each transmission access charge area that is capped at that entity's system resource adequacy obligation amount. This treatment could lead to higher local capacity procurement mechanism cost allocation as compared to an equivalent load serving entity that serves load in only a single transmission access charge area. Management proposes to modify the tariff to allow for load serving entities with load in multiple transmission access charge areas to cap their local obligation at their system obligation in each transmission access charge area. This provision would only apply in the monthly resource adequacy time frame.

Management is not proposing any changes to its backstop capacity procurement mechanism process, other than to incorporate a CPE into the existing relevant tariff language. Management proposes to allow the CPUC to allocate the resource adequacy credits for capacity procurement mechanism procured resources to its jurisdictional CPEs and load-serving entities. Since a CPE does not have a load share, it will not be allocated capacity procurement mechanism costs associated with a collective local deficiency, system deficiency, flexible deficiency, significant events, or exceptional dispatches.

Management also proposes to allow the CPUC to allocate the credits for reliability must-run units to CPEs and load-serving entities, but proposes no changes to the reliability must-run cost allocation methodology.

RAAIM Settlement Modification:

Management proposes to modify the current RAAIM settlement processes to eliminate the rule that unavailability charges assessed in excess of the monthly cap will roll over to fund allocations in future months. Rather than rolling excess funds into the next month, the ISO will allocate any excess RAAIM charges for generic resource adequacy or flexible resource adequacy to metered demand. This change ensures that RAAIM settlements charges and credits are fully netted out and allocated within the month they are incurred. This change also addresses the issue that necessitated the FERC waiver in April 2020.

This change should also increase the effectiveness of RAAIM by ensuring that a resource's performance in a given month is either paid or charged for that month. Additionally, by allocating the excess funds to metered demand, load serving entities

will be compensated for resources that did not perform in accordance to their resource adequacy contract obligations.

POSITIONS OF THE PARTIES

Stakeholders generally support this package of enhancements and believe it will allow the ISO to implement the CPE framework in time for resource adequacy year 2023.

Stakeholders support the tariff revisions to recognize the CPE in its local resource adequacy allocation and showings process. Stakeholders also support the tariff revision to cap a load serving entity's monthly local obligation at its system obligation in each transmission access charge area.

A majority of stakeholders support the ISO's clarification for accommodating the CPE into its capacity procurement mechanism and cost allocation processes. However, one stakeholder advocated that the ISO allocate both individual and collective local deficiencies directly to the CPE. Management believes it is appropriate to maintain the current collective local deficiency cost allocation methodology because this CPM designation is not tied to any specific party's failure to meet their procurement obligation. The benefits of such a designation flow generally to load and not a CPE, so it is appropriate to maintain the current approach of allocating pro rata by load share to load serving entities in the transmission access charge area.

One stakeholder offered an alternative approach to Management's proposal for allocating the costs of CPM designations for individual local deficiencies under the CPUC hybrid procurement framework. A key principle of backstopping the RA program through the CPM authority is that the CAISO, wherever possible, allocates the costs of a CPM in proportion to how a LSE (and now CPE) is deficient in meeting its upfront RA requirements. Management's proposal maintain this principle of allocating the costs based on an entity's deficiency relative to its requirements. The alternative proposal, however, would not meet this principle in all cases.

Stakeholders representing load strongly supported Management's proposal to eliminate the monthly roll-over of excess RAIM funds and to allocate this to metered demand.

One stakeholder representing generators strongly objects to Management's proposal. They argue that rather than eliminating the monthly roll-over to address the settlement issue, the ISO should prioritize RAIM penalty refunds over paying out incentives in the settlement recalculation. Management's proposal does prioritize the refunds in the settlement recalculation. However, the fundamental problem is that the carry-over mechanism exposes the ISO to financial risk when the distribution of adjusted RAIM funds are from subsequent months' RAIM incentive payments. Thus, it would be irresponsible in light of the ISO's past need to obtain a waiver from FERC to resolve the problems caused by the rollover. Their alternate proposal to maintain the rollover does not address the core issue eliminating the monthly roll-over addresses.

CONCLUSION

Management requests the ISO Board of Governors approve Management's proposal for the implementation of the CPE and to modify the RAIM settlement rules. The changes will allow the ISO to effectively implement the new CPE role, as well as improve RAIM incentives and more appropriately allocate RAIM penalty proceeds.