

**Comments of The Utility Reform Network  
on the California Independent System Operator’s Reliability Services Initiative  
Submitted April 9, 2014**

The Utility Reform Network (TURN) offers the following comments on the California Independent System Operator’s (CAISO’s) Reliability Services Initiative (RSI), as requested on page 70 of the CAISO presentation titled *Reliability Services, Market Mechanism Working Group* that was discussed at the working group meeting of March 27, 2014 (March 27 Presentation).<sup>1</sup>

In summary, TURN recommends that, in scoping how to develop a “market-based mechanism” to replace the Capacity Procurement Mechanism (CPM), the CAISO consider options other than a stripped-down or “Lite” version of a Centralized Capacity Market (CCM). TURN believes such alternative approaches could (a) maintain the state’s current, successful “market-based” method for ensuring reliability, (b) satisfy the guidance the FERC has provided on replacing the CPM, (c) avoid investing considerable effort in a process that may not yield a workable solution, and (d) minimize the chance of potentially costly federal pre-emption of California’s procurement policies.

California Is Meeting, and Will Continue to, Meet Its Reliability Needs Using “Market-Based Mechanisms”

In considering the CAISO’s anticipated “CCM Lite” proposal, it is important to first consider how reliability procurement is currently conducted within the CAISO footprint. The main buyers, California’s Investor-Owned Utilities (IOUs), obtain much long-term Resource Adequacy (RA) capacity pursuant to technology-specific programs directed by state legislation using Requests for Offers (RFOs) and similar competitive processes. The IOUs procure their remaining RA needs in bilateral markets. Other Load-Serving Entities (LSEs) also purchase RA capacity in bilateral markets. These policies have resulted in significant amounts of forward RA procurement over the last several years and should continue to do so in coming years.<sup>2</sup> The state

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<sup>1</sup> This presentation is available at [http://www.aiso.com/Documents/Presentation-ReliabilityServicesWorkingGroupMar27\\_2014.pdf](http://www.aiso.com/Documents/Presentation-ReliabilityServicesWorkingGroupMar27_2014.pdf). References herein to this March 27 Presentation will cite page numbers of the version that was available as of April 8, 2014 (posted March 27 at 14:22), which included three additional slides from the version reviewed at the workshop.

<sup>2</sup> See Figures 4 and 5 of the Planned Remarks on behalf of The Utility Reform Network by Kevin Woodruff, Principal, Woodruff Expert Services, prepared for the Federal Energy Regulatory Commission Technical

thus already meets the FERC’s guidance that California should “develop...a durable, market-based mechanism that provides incentives to ensure that resources with the adequacy and operational needs CAISO requires are available to meet system needs”.<sup>3</sup>

The only aspect of current procurement that arguably does not occur in markets or similar mechanisms is the CAISO’s little-used Capacity Procurement Mechanism (CPM), the current price of which was set administratively.<sup>4</sup> The FERC has seemingly encouraged the CAISO to file a CPM pricing mechanism that is “market-based.”<sup>5</sup> However, “market-based” is a broad term that encompasses a wide range of possibilities. In response to this guidance, the CAISO seems intent on developing a Lite version of a CCM that meets, or at least approaches, the limited market structures the CAISO and CPUC agreed to implement in the Joint Reliability Plan (JRP). However, alternatives exist that would likely be less burdensome and risky to implement that would produce a price that would be as likely to be as “market-based” as anything that would emerge from the type of auction the CAISO is considering. TURN provides two examples of such alternatives in the next section.

#### Other Non-Centralized “Market-Based Mechanisms” Should be Considered

TURN offers two different approaches to developing a market price for CPM procurement that are worth CAISO consideration. First, CPM prices could be developed from the pricing data the CPUC collects for RA purchases. Reference to such prices would allow CPM prices to “fluctuate over time based on changes in system conditions and the amount of capacity available to meet reliability needs”.<sup>6</sup> The effort to develop and implement such a mechanism, though non-trivial, would likely be much less than the effort the CAISO’s anticipated approach would require.

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Conference on Flexible and Local Resources Needed for Reliability in the California Wholesale Electric Market, Docket No. AD13-5-000, July 31, 2013, available at <http://elibrary.ferc.gov/idmws/search/results.asp>.

<sup>3</sup> March 27 Presentation, page 74, quoting FERC’s “FLRR Order”.

<sup>4</sup> Although CPM prices were negotiated against a backdrop of market prices.

<sup>5</sup> March 27 Presentation, pages 72-73, quoting a FERC order regarding the CPM. The quotes on these slides say what is *not* acceptable to the FERC – that is, a “fixed going-forward cost price” or a price based on “CONE” (the Cost of New Entry) – but are less clear on which mechanisms that would allow the price of capacity to “fluctuate over time based on changes in system conditions and the amount of capacity available to meet reliability needs” would be acceptable.

<sup>6</sup> *Id.*

Second, an over-the-counter exchange or electronic bulletin board could be developed to allow parties to trade RA capacity bilaterally in a more convenient and transparent manner.<sup>7</sup> Similar to craigslist, such an exchange or bulletin board would allow buyers and sellers to post offers to buy or sell RA capacity. In order to yield information that would help produce CPM prices, such a “craigslist” approach would likely need to be available for capacity trades for terms beyond those needed for CPM purposes. Again, such an approach would also likely require less effort to develop and implement than the coming CAISO proposal.

#### Development and Success of “CCM Lite” Faces Many Challenges

The development and success of a CAISO-proposed market is far from certain. Workshops to date have highlighted many of the challenges to this design, such as designing a short-term auction that does not interfere with existing, functioning markets and a potential lack of auction liquidity.

#### CAISO Needs to Address Potential Impacts of Federal Pre-emption on State’s Markets:

But TURN’s biggest concern is that the auction the CAISO proposes would increase the likelihood of efforts to invite FERC preemption – fueled by recent troubling FERC and federal court decisions regarding conflicts between state and FERC policies – and that the vision of the JRP, which intrudes relatively little on the state’s existing markets, would be supplanted by federal policies not consistent with California’s particular policies.

TURN appreciates that the CAISO states that it wishes to avoid such outcomes.<sup>8</sup> But to sell a proposal for a FERC-regulated “market mechanism” to California customers and policy-

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<sup>7</sup> See Table 12, 1.a, at page 40 of *Developing a Market Vision for MISO Supporting a Reliable and Efficient Electricity System in the Midcontinent*, Foundational Report, prepared for the MISO by The Brattle Group, January 27, 2014, available at <https://www.misoenergy.org/Library/Repository/Communication%20Material/Key%20Presentations%20and%20Whitepapers/MISO%20Market%20Vision%20Foundational%20Report.pdf>.

<sup>8</sup> For example, the CAISO said in response to ORA’s comments on the CAISO’s response to stakeholder comments on reliability services issues paper:

“...it appears ORA’s concern is that there is the potential for FERC to not accommodate California’s pursuit of policy objectives, such as development of renewable resources, in the mandate to approve just

makers, the CAISO needs to explain not just why its proposal itself does not interfere with California's existing markets, but why the submittal and possible implementation of the proposal will not facilitate – or even invite – the FERC or federal courts to effectively override California's electric resource policies.<sup>9</sup>

Further, the CAISO appears poised to propose what is perhaps the most concerning federal policy – a Minimum Offer Pricing Rule (MOPR).<sup>10</sup> In one sense, implementation of a MOPR could arguably still “accommodate policy objectives” and not prevent Local Regulatory Authorities (LRAs) from pursuing “policy-based procurement”. However, a MOPR could still make pursuing these objectives substantially more expensive. If the CAISO wishes to propose a MOPR, it should explain how its proposed MOPR itself will not significantly increase customer costs. Just as important, the CAISO should also explain why the submittal and implementation of one version of a MOPR will not open the door to FERC or the federal courts imposing a different version of a MOPR that is much less accommodating of California's electric resource policies.<sup>11</sup>

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and reasonable market design. The ISO appreciates this concern and in any market design for a forward residual market-mechanism will not create rules that conflict with the ability of an LRA to pursue policy-based procurement. A voluntary market will fully and completely accommodate policy objectives as no supplier or LSE will be required to participate. All policy objectives can be achieved outside the auction and any remaining need can be achieved within the auction.”

See p. 58 of the response, which is available at <http://www.aiso.com/Documents/StakeholderCommentsMatrix-ReliabilityServices-IssuePaper.pdf>.

<sup>9</sup> TURN appreciates that the CAISO cannot guarantee the outcomes of all future regulatory, legal and political processes. However, the CAISO should begin to develop a stance and legal strategy to minimize opportunities for preemption of California's policies for developing a sustainable and reliable electricity grid.

<sup>10</sup> March 27 Presentation, page 67.

<sup>11</sup> See footnote 9.

TURN appreciates this opportunity to provide these comments.

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