Stakeholder Comments Template

Submitted by	Company	Date Submitted
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Please use this template to provide your written comments on the stakeholder initiative "RMR and CPM Enhancements."

Submit comments to initiativecomments@caiso.com

Comments are due October 23, 2018 by 5:00pm

The September 19, 2018 revised straw proposal and the presentation discussed during the September 27, 2018 stakeholder meeting can be found on the following webpage: http://www.caiso.com/informed/Pages/StakeholderProcesses/Review_ReliabilityMust-Run_CapacityProcurementMechanism.aspx.

Please use this template to provide your written comments on the items listed below and any additional comments that you wish to provide.

Energy Division Staff (hereafter, "ED Staff" or "Staff") appreciates several changes the CAISO has included/added to the revised straw proposal, released on September 19, 2018, including the following:

- Clarifying when RMR and CPM will be used,
- Inclusion of flexible attributes on RMR designations, and
- Making RMR resources subject to a MOO
- Making RMR resources subject to RAAIM
- Removal of the expansion of RMR to a three year period.

However, Staff remains concerned with aspects of the proposal that were not modified in the most recent draft. Staff requests that CAISO work with stakeholders to address the following aspects of the proposal, so they are better aligned with the changing bilateral construct:

- RMR and CPM compensation,
- Establishing a timeline for requesting and approving RMR designations,
- CPM cost allocation, and
- Allocation of flexible attributes for CPM designations.

The CPUC is currently considering a multi-year framework for local RA requirements in Track 2 of R.17-09-020. Implementation of this framework is intended to applicable to compliance year 2020.[1] Staff believes that to develop and successfully implement a workable bilateral framework, there must not be incentives that would motivate a generator to seek an RMR or CPM contract over a bilateral one. Staff remains concerned that the current proposal may encourage front running of the bilateral procurement process would occur. These concerns are addressed below.

1. <u>Comments on September 19, 2018 straw proposal.</u>

<u>RMR and CPM</u>

a. Provide notice to stakeholders of resource retirements

Comments:

CPUC Staff thanks the ISO for providing stakeholders with more transparency around resource owners' plans for retirement or mothballing. Staff had requested, in its August 7th comments, that the CAISO alert market participants when it receives additional retirement communications and/or requests. In its 9/19/18 straw proposal, the CAISO attempts to provide a notification mechanism for its current list of retired or mothballed resources. The notification would be triggered for resources 100 MW or larger. Staff appreciates this element of the proposal and supports any additional transparency and communication the CAISO can provide to stakeholders. For example, Staff requests that CAISO change the threshold size to 40 MW, as this would ensure that it would capture the size of many peakers in operation that may seek (or are currently seeking) retirement.

Additionally, it remains unclear how this list of generator communications/retirement requests will be coordinated with the bilateral framework. Resent retirement activity has made it clear, that CAISO needs to incorporate a retirement planning process into its tariff. This is discussed in section 2 below.

b. Use of RMR versus CPM procurement

[1] D.18-06-030 at p. 28

Comments:

In its 9/19/218 straw proposal, the CAISO clearly establishes that RMR will be used for retirement purposes, which changes the original purpose of RMR from a local market power mitigation tool to a retirement tool. Staff appreciates CAISO providing clarity around the use of RMR.

It is also Staff's understanding that CAISO will remove the current RMR authority that allows for an RMR designation at any time if the resource is needed for reliability. This will be replaced by a requirement that the generator needs to file a formal retirement notice with the CAISO (and the CPUC) in order to receive a designation. The current straw proposal states that:

> "If a resource declines a CPM designation, the ISO will offer the next most effective resource a CPM designation. In the event no other resources are available, the ISO will not go directly to offering the resource an RMR designation. The ISO will inform the resource that if the resource wants to be considered for an RMR designation, the resource must submit a formal retirement notice to the ISO. **This notice must include an affidavit by an officer of the company who has the legal authority to bind such entity attesting the resource will not remain in service and that the decision to retire is definite unless some other type of ISO procurement of the resource occurs, the resource is sold to a non-affiliated entity, or the resource enters into an RA contract. In the formal retirement notice to the ISO, the resource must state that it is planning to retire at a certain date, but no earlier than 90 days from the notice of termination of the PGA.** The ISO will expect the resource to also send a notice to the CPUC, if applicable, indicating its intent to retire."[2]

It is unclear to Staff how the CAISO will treat retirement communications that do not include an affidavit. Will the CAISO assess the resource and notify the owner if the resource is needed, or will CAISO wait until the CPM process runs its course? Clarifying this part of the proposal is critical to understanding how generators will interact with the RMR and CPM processes. For example, if a resource notifies the CAISO of its plans to retire without sending in a formal affidavit, and the CAISO notifies the owner that the resource is needed, the resource could then be withheld from the bilateral process so that it could be awarded a CPM designation, above the soft offer cap at its cost-of-service, for the year and get around the requirement that it needs to submit a formal retirement notice.

c. Explore whether Risk of Retirement CPM and RMR procurement can be merged into one procurement mechanism

   Comments: No comment at this time.

[2] Straw Proposal page 14

RMR

d. Develop interim pro forma RMR agreement

Comments: No comment at this time.

e. Update certain provisions of pro forma RMR agreement

   i. Remove AS bid insufficiency test and revise dispatch provisions to align with current market design

   Comments: No comment at this time.

   ii. Update Schedule M and Schedule C to include GHG compliance cost calculation, DAM and RTM gas price index, and updated SC charge calculation

   Comments: No comment at this time.

   iii. Update Schedule M to be consistent with bidding rules in ISO tariff and BPM

   Comments: No comment at this time.

   iv. Seek input on defining a heat rate curve formula in Schedule C for multi-stage generator resources

   Comments: No comment at this time.

f. Make RMR resources subject to a must offer obligation

Comments: CPUC staff supports this provision.

g. Make RMR resources subject to the Resource Adequacy Availability Incentive Mechanism

Comments: CPUC Staff supports this provision.

h. Consider whether RMR Condition 1 and 2 options are needed

Comments:

CPUC Staff does not support keeping a Condition 1 option. RMR resources are that are retiring are claiming they are not economical and therefore it makes no logical sense to then allow for the option to earn rents in the energy markets.

i. Update rate of return for RMR compensation

Comments:

Staff still is not supportive of full cost of service (AFRR) compensation given the ability to toggle between market compensation and cost-of-service compensation. Additionally, Staff does not believe the CAISO has addressed the issues raised by Staff in earlier comments regarding establishing parameters around what costs can be included in cost-of-service compensation (such as asset life limits).[3] Without addressing the compensation issue, resource may continue to opt for this mechanism over the bilateral process. Setting the right cost compensation is critical to addressing and resolving the issues that gave rise to the RMR designations that occurred last year.

Staff continues to believe that compensation should be based on going forward fixed cost (GFFC), plus provisions for any need capital additions, to the extent not already included n GFFC. GFFC should be the default compensation for RMR. Staff believes this change would discourage generators from using the RMR mechanism to get higher compensation than they could through the bilateral procurement process.

CAISO points to the New England ISO Mystic FERC Order as evidence that FERC has approved cost-of-service compensation as just and reasonable.[4] However, without considering the full order and the other details of what full-cost of service should include, it is not accurate to look at cost-of-service compensation in isolation. For example, that same order required Mystic to base its cost of service compensation off of an actual capital structure. Mystic had proposed to use a hypothetical 50/50 debt to equity capital structure when their actual equity was argued to be much lower than 50 percent[5]. The FERC order specifically states:

> While we have found that a 10.88 percent ROE is a conservative proxy for merchant generating facilities, we have also stated that we would prefer to use an actual debt/equity ratio rather than a hypothetical one. We will, therefore, as we have in the past, include in the hearing and settlement judge instructions that Mystic's actual debt/equity ratio be determined. The Commission further sets for the hearing and settlement judge a determination of Mystic's 2004 financial information necessary for a proper cost-of-service analysis[6].

In its recent proposal CAISO states that "[t]he current rate of return, as a component of the cost based rate of return, is specified as 12.25% in the RMR pro forma agreement. This value is

[3] August 7th, 2018 CPUC Staff Comments

[4] New England ISO Mystic FERC Order- 114 FERC ¶ 61,200 P. 49

[5] New England ISO Mystic FERC Order- 114 FERC ¶ 61,200 P. 38 "Mass AG also maintains that Mystic should use its actual capital structure (which, as of October 31, 2005, was approximately 76 percent long-term debt and 24 percent equity), not a hypothetical 50/50 capital structure. It claims that, based on Mystic's actual capital structure, Mystic's pre-tax cost-of-capital should be 11.47 percent, rather than the 12.57 percent that Mystic is proposing to use, based on a capital structure that it does not possess."

[6] New England ISO Mystic FERC Order- 114 FERC ¶ 61,200 P. 49

applicable on a pre-tax basis and is applied to the 'net investment' value (undepreciated assets) for resources eligible for RMR."[7] CAISO proposes to change this 12.25% rate to be based on a blend of the most recently approved pre-tax ROE rates for the three large investor owned utilities in California (PG&, SCE, & SDG&E).[8]

The proposed changes to CAISO pro forma agreement to do not differentiate between debt and equity and therefore assumes that the entire submitted cost of service is being financed with equity. If the CAISO continues to pursue cost of service for RMR designations Staff requests that these critical details be looked at, in order to prevent creating financial incentives for generators to use the backstop process rather than the bilateral market.

In addition to capital structure the current proposal fails to identify the "toggling" issue identified in the NYISO FERC order. Toggling is a term that defines the behavior of a generator to move back and forth between market-based compensation to cost-of-service based compensation. FERC summarized this toggling as following:

> The first type arises when a generator is needed for reliability and has an incentive to seek to deactivate prematurely. As one example, the generator may be operating profitably in the market with its existing facilities. Because the generator is profitably operating in the market, its market revenues equal or exceed its going-forward costs. The generator might have an incentive to seek to deactivate prematurely if the generator knows it is needed for reliability (and thus, has market power) and the non-market compensation that it would receive under an RMR agreement would exceed its current market-based compensation.
>
> The second type arises when a generator that is operating under an approved RMR agreement must make capital expenditures to continue to meet the reliability need during the term of the RMR agreement. The toggling concern presents itself when the upgrade would be profitable based solely on market revenues (i.e., without any out-of-market revenues), but the generator seeks to recover the upgrade costs through an RMR agreement and then, after the termination of the RMR agreement, returns to market-based revenues that exceed going-forward costs.[9]

FERC order the NYISO to address the toggling behavior in its RMR proposal, stating that the proposal should include:

> rules to eliminate, or at least minimize, incentives for a generator needed for reliability to toggle between receiving RMR compensation and market-based compensation for the same units. The Commission appreciates that uneconomic units could become economic for a number of reasons, including changing market conditions and the need for and timing of capital investments. However, the Commission is concerned that any

[7] September 19, 2018 Straw proposal at p. 25
[8] September 19, straw proposal at 27
[9] At 23 and 24

> proposed provisions not provide an incentive for a generation resource to propose to deactivate earlier than it otherwise would have in expectation of being needed for reliability and, therefore, be able to receive more revenues under an RMR service agreement than by remaining in the market. As noted above, the tariff provisions should not provide an incentive for a generation resource to re-enter the market after having received accelerated recovery of the cost of additional investments made under its RMR agreement. Accordingly, to address the Commission's concerns related to toggling, NYISO should craft tariff provisions that provide clear guidance to generators regarding the implications of a deactivation notice.[10]

To comply with this order, the NYISO proposed to require reimbursement of capacity expenditure cost as a condition for operating after the termination of an RMR agreement. In response to this proposal FERC found that "NYISO's proposal does not adequately address the first type of toggling because it does not deter toggling by generators that do not require capital expenditures during the term of an RMR agreement."[11] FERC directed NYISO to include a compliance filing with tariff revisions that would discourage type one toggling.[12]

Staff request that the next iteration of this straw proposal include a proposal to address both the types of toggling identified above.

a. Align pro forma RMR agreement with existing RMR tariff authority that currently provides ability to designate for system and flexible needs

   Comments: No comment at this time.

b. Allocate flexible Resource Adequacy credits from RMR designations

Comments:

Staff continues to support the allocation of flexible capacity benefits for RMR designations. As noted above, Staff only supports the use of Condition 2 RMR designations for resources that are retiring and are needed to maintain reliability. In its revised straw proposal CAISO proposes that to qualify for flexible RA credit "the resource owner must agree in the RMR agreement to fulfill RA flexible capacity requirement such as offering economic bids."[13]

Staff does not support this additional requirement. If ratepayers are paying the full cost-of-service of the resource, then they should be awarded all the reliability benefits of the resource. This should not be up to the discretion of the owner.

Additionally, Staff requests that allocation of flexible RA credits also be extended to CPM designations. Not allocating the flexible benefits of CPM designations will strand the flexible capacity of these resources.

[10] RMR Order, 150 FERC ¶ 61,116 at P 21.
[11] 155 FERC ¶ 61,076 at P 125
[12] 155 FERC ¶ 61,076 at 126 and 127
[13] September 19, 2018 Revised Straw Proposal p. 28-29

c. Streamline and automate RMR settlement process

Comments: No comment at this time.

d. Lower banking costs associated with RMR invoicing

Comments: No comment at this time.

CPM

e. Change CPM pricing formula for resources that file at FERC for a CPM price above the soft-offer cap price

Comments:

CAISO proposes to change the cost compensation for CPM bids above the soft offer cap. The current tariff allows generators to file for compensation above the soft offer cap using the current RMR pro forma which allows for total cost recovery (AFRR) and retention of market revenues.[14] In its 9/19/18 straw proposal, CAISO modifies the current compensation to be full cost-of-service minus retention of market revenues. This compensation is essentially the same as the proposed mandatory RMR compensation. The only difference between the two proposals is there is no provision for capital addition cost recovery under the CPM. This means that resources seeking full cost-of-service recovery can use CPM to avoid the RMR requirement to file an affidavit notifying the CAISO of its retirement. Moreover, Staff questions why it is necessary to provide full cost-of-service for a designation that is not "mandatory." While Staff appreciates the claw back of capital additions, this proposal still leaves room for generators to avoid the formal retirement requirement and still be allowed sunk cost recovery. As discussed in prior comments Staff remains concerned that this proposal allows for a generator to avoid the retirement requirements and still receive its full cost-of-service compensation. Staff is also concerned that cost-of-service is not appropriate and would encourage generators to toggle between cost-of-service compensation and market-based compensation.

f. Evaluate year-ahead CPM local collective deficiency procurement cost allocation to address load migration

[14] CAISO Tariff, § 43A.4.1.1.1 "For a resource whose sales are under FERC jurisdiction that is providing CPM Capacity to be compensated at a rate higher than the CPM Soft Offer Cap, the resource owner must make a limited resource-specific filing before FERC to determine the just and reasonable capacity price for the resource as calculated per Schedule F to the pro forma RMR Agreement in Appendix G of the CAISO Tariff."

Comments:

In its current straw proposal CAISO proposes "to keep the current year-ahead CPM local collective deficiency procurement cost allocation methodology, as it believes that the issue of load migration has largely been addressed by the CPUC's June 2018 RA Decision."[15]

Staff does not believe that the CPUC's recent RA decision addresses all of the issues of load migration. For example, load migration can still occur from month to month even after the year ahead forecast is locked down. While the decision attempts to lock down some level of certainty around large amounts of load migration, it does not completely eliminate the possibility of load migration occurring from month to month. Staff recommends that the CAISO use the same cost allocation mechanism used for monthly and intra-monthly CPM designations.

g. Evaluate if load serving entities are using CPM for their primary capacity procurement

Comments: No comment at this time.

2. Other Comments

Please provide any additional comments not associated with the items listed above.

Comments:

Staff continues to believe that a generator retirement process is needed. Such a process would facilitate coordination with bilateral procurement process and the CAISO's Transmission Planning Process. Coordination with these two processes requires a longer retirement notification timeline than the current rules require. Currently resources can seek retirement at any time of the year. For most resources seeking to permanently retire their resource and or repower, there is a 90-day notice requirement to the CAISO. However, the timeline is even shorter for resources seeking to mothball their resource (60-day notice is required). And even shorter for QFs/CHP facilities, which have no retirement notice requirement.

These resource notification timelines do not allow for the proper evaluation of alternatives. The NYISO's retirement process requires a 365-day notice which allows for alternatives to be considered.[16] A similar process should be considered in California to bridge the retirement of the gas fleet with the reliability planning processes. Staff continues to propose a retirement notification window that would flow into the annual local capacity requirement studies that inform year ahead and future local multi-year RA requirements.[17]

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[15] September 19, 2018 Straw Proposal at p.4

[16] 161 FERC ¶ 61,189 at P. 28 and 29

[17] CPUC August 7th 2018 Staff Comments p. 6 "Staff understands that generators are requesting information on whether they are needed for the coming year so that they can make retirement decisions. Therefore, Staff

According to CAISO's 9/19/18 straw proposal, both resources seeking retirement and mothball status fall under the RMR proposal.[18] Staff understands this to mean that resources seeking to deactivate and preserve equipment at their plant for future use or sale ("mothball") would fall under the category of an RMR designation. CAISO's current straw proposal states that

> the resource must submit a formal retirement notice to ISO. This notice must include an affidavit by an officer of the company who has the legal authority to bind such entity attesting the resource will not remain in service and that the decision to retire is definite unless some other type of ISO procurement of the resource occurs, the resource is sold to a non-affiliated entity, or the resource enters into an RA contract. In the formal retirement notice to the ISO, the resource must state that it is planning to retire at a certain date, but no earlier than 90 days from the notice of termination of the PGA."[19]

Staff is concerned that this process also includes mothballing a facility, which is the temporary shutdown of a facility not the same as taking a resource out of service indefinitely. Staff does not believe there are clear enough guidelines around mothballing a facility. Two of Calpine's peakers (King City Energy Center and Wolfskil Energy Center) were mothballed at the beginning of 2018 and then came into service for the several summer months in 2018 under RA contracts. On October 23, 2018, CAISO updated their announced retirement and mothball list to include a recent 60-day notice from King City requesting mothball status (once again) beginning on January 1, 2019. CAISO's current requirements around mothball status require the resource to be mothballed for a minimum of 2 months and a maximum of three years before losing its deliverability status.

Another resource Ormond Beach had requested formal retirement status (not mothball status for both Ormond Beach 1 and 2) early last year. Following this request, CAISO announced, through its local capacity technical study, that one unit of Ormond Beach would be need for local reliability in 2019. In response to this need, SCE entered a contract of 2019 with Ormond Beach 1 pursuant to CPUC decision D.18-06-030 (that required SCE to attempt to contract with the facility to avoid out-of-market RA procurement). The second unit did not receive contract with SCE since it was not needed for local reliability, however the second unit was updated on the resource retirement list to change its retirement date back to December 2020, when it had previously sought retirement for January 2019. This means it is now available to the market for 2019.

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proposes that CAISO require generators to submit retirement requests by a certain date each year. These requests would be incorporated into the annual local and flex studies so they could be studied within a stakeholder process. In order for this to work, retirement requests for the coming compliance year would need to be made prior to February 15th (or the latest possible date for the CAISO to incorporate into annual Local and Flexible Capacity Requirement Studies). Providing CAISO and market participants with more time to study planned retirements would in turn provide generators with more certainty regarding retirement decisions. If the retirement notice is not submitted in a timely fashion, then the need for the resource would not be assessed in the planning process."

[18] September 19th, 2018 Straw Proposal Figure 2 (p.14)
[19] September 19th, 2018 Straw Proposal p. 14

Another example can be drawn from the Calpine's Metcalf facility which was awarded an RMR designation for 2018, but given recent transmission upgrades in this local area, its RMR contract was not renewed for 2019. Looking at the CAISO's current announced retirement and mothball list, it appears to have returned to the market for 2019. (its 2018 RMR contract was not renewed for 2019 and it has not filed any retirement notice for 2019.)

It appears that without a formal retirement process, that stricter rules around mothballing and retirement need to be established. Importantly, these rules need to be established prior to implementing a mechanism that awards cost of service compensation in one year and then awards market revenues in the next.

Staff supports the use of a generator deactivation notice timeline (retirement process) similar to NYISO's 365-day timeline approved by FERC. Such a timeline allows for the NYISO to consider RMR alternative solutions.[20] We encourage the CAISO to further explore a generator deactivation timeline that can help facilitate a more coordinated approach in planning for generators to exit the grid.

[20] 161 FERC ¶ 61,189 at P. 28 and 29