COMMENTS OF SELECT EIM ENTITIES[1] ON CAISO'S FERC ORDER 831 IMPORT BIDDING AND MARKET PARAMETERS DRAFT FINAL PROPOSAL

May 20, 2020

On November 17, 2016, the Federal Energy Regulatory Commission ("FERC") issued Order No. 831, requiring that each regional transmission organization and independent system operator: (1) cap each resource's incremental energy offer at the higher of $1,000/MWh or that resource's verified cost-based incremental energy offer; and (2) cap verified cost-based incremental energy offers at $2,000/MWh when calculating locational marginal prices ("LMPs").[2] A critical component of Order No. 831 was that, in order to be just and reasonable, energy offers above $1,000/MWh must be cost-verified. Nothing in Order No. 831 stated that the $2,000/MWh level was intended to be utilized as a penalty price or indication of scarcity 8,760 hours per year.[3]

In both stakeholder comments,[4] and a FERC filing,[5] NV Energy, along with PacifiCorp, Idaho Power Company, Portland General Electric, and Arizona Public Service, explained why implementing a $2,000/MWh power balance constraint penalty is unjust and unreasonable, particularly if applied to the utilities and their customers participating in the Western Energy Imbalance Market ("EIM"). Those comments also reminded the CAISO of the long-standing commitment the CAISO had made to them and to FERC to engage in a stakeholder process *to reduce the existing $1,000/MWh power balance constraint penalty* in steps based on the amount of megawatts of infeasibility.[6]

---

[1] These comments are submitted on behalf of the following EIM Entities: Arizona Public Service, Idaho Power Company, Puget Sound Energy ("PSE"), Portland General Electric Company, PacifiCorp, and NV Energy (the "Commenters").

[2] Order 831 at P 1. For an incremental energy offer equal to or above $1,000/MWh and less than or equal to $2,000/MWh, the RTO/ISO or Market Monitoring Unit must verify that the offer is cost-based before the RTO/ISO may use the offer to calculate LMPs. *Id.* P 78.

[3] Order No. 831 arrived at the $2,000/MWh level because it was above the single cost-based incremental offer in PJM of $1,724/MWh during the Polar Vortex in 2014. Order No. 831 at P. 90. Although the actual cost for of that resource may have been less than $1,500/MWh,[3] *See* Order No. 831-A at P. 6. FERC selected $2,000/MWh in recognition that under limited extreme circumstances "resources may experience costs that approach but are unlikely to exceed $2,000/MWh." Order No. 831 at P 90.

[4] *See* Joint Party Comments Commitment Costs and Default Energy Bid Draft Tariff Language dated May 28, 2019 and Comments of the EIM Entities on CAISO's FERC Order 831 Import Bidding and Market Parameters Revised Straw Proposal dated December 19, 2019. *See also* PSE Comments on CAISO's FERC Order 831 Import Bidding and Market Parameters Revised Straw Proposal dated December 19, 2019.

[5] *See* Motion to Intervene and Protest of the EIM Entity Parties filed in FERC Docket No. ER19-2757 on September 26, 2019.

[6] *See Cal. Indep. Sys. Operator Corp*., 153 FERC ¶ 61,305 (2015) at P. 82. and P. 84 ("We find that the level of the penalty price that will apply when an infeasibility occurs is beyond the scope of this proceeding because there is no proposal in front of us to change the existing CAISO tariff provisions regarding the penalty level. However, we note that CAISO has initiated a stakeholder process to investigate CAISO's transmission constraints and we encourage CAISO and its stakeholders to work together to address these concerns.").

The Commenters greatly appreciate the efforts of the CAISO in addressing the concerns raised by EIM Entities in Docket No. ER19-2757 and the December 19, 2019, Revised Straw Proposal. In its April 23, 2020, Draft Final Proposal, the CAISO continues to set the power balance constraint penalty at $1,000/MWh, unless there is a cost-verified cleared bid greater than $1,000/MWh in which case the penalty would be set at the price of the highest cost-verified cleared bid. The CAISO also identifies improvements to the flexible ramping product that will ensure the power balance constraint is not triggered prior to the flexible ramping product constraints being fully relaxed. These significant improvements to the proposal return the power balance parameter to reasonable levels.

I. Improvements in the Draft Final Proposal

In September 2019, the CAISO submitted a filing at FERC that would double the power balance penalty to $2,000/MWh. The proposed doubling of the power balance penalty price was not required by FERC in Order No. 831. The Commission noted, "[a]n RTO/ISO may file, pursuant to section 205 of the Federal Power Act, to propose modifications to shortage prices or other market elements that require revision in light of the offer cap reforms adopted in this Final Rule."[7]

In January 2020, the CAISO notified FERC that it would extend implementation of its compliance with Order No. 831 to fall 2021 to allow more time for policy development and implementation resulting from this policy initiative. In the Draft Final Proposal, the CAISO proposes to set the power balance constraint penalty price used by the market to $2,000/MWh, and scale related price parameters accordingly, only during periods when verified energy costs are greater than $1,000/MWh. In the event the market is using the penalty prices scaled relative to a $2,000/MWh power balance constraint penalty price and the market must relax the power balance constraint, the CAISO proposes that the market set energy prices at the price of the highest-priced cleared economic bid. The CAISO selected this alternative "because it is reasonable to assume that costs will not justify energy bids greater than $1,000/MWh the vast majority of the time," and "it is reasonable that unless there are actually costs greater than $1,000/MWh, the power balance constraint relaxation penalty price will remain at $1,000/MWh."[8]

The revised approach reflected in the Draft Final Proposal is a significant improvement from the proposal pending in Docket No. ER19-2757. While accommodating the potential for cost-justified LMPs between $1,000/MWh and $2,000/MWh as required by Order No. 831, the revised approach essentially returns to the status quo; in the overwhelming majority of intervals where there is no cost-justified bid above $1,000/MWh, the power balance parameter penalty price will remain at $1,000/MWh. The revised proposal should be adopted and quickly reflected in an amended filing in Docket No. ER19-2757.

[7] Order 831 at P. 210 and 213.

[8] Draft Final Proposal at 8.

II. No Additional "Scarcity" Adder Above the Cost-Justified LMP Is Appropriate as a Penalty Price in the EIM

In the event there is a cost-justified bid above $1,000/MWh, the CAISO does not propose to impose a penalty price above the cost-justified bid as applied to either the CAISO Balancing Authority Area ("BAA") or the BAAs of the other EIM Entities. The Commenters support this approach. If in response to the Market Surveillance Committee or other comments; the CAISO determines that an additional penalty above a cost-justified bid above the $1,000/MWh level is needed to encourage imports into the CAISO BAA, that additional adder would not be appropriate as applied to the EIM. FERC has recognized that parameter penalties applicable in the CAISO's BAA may not be just and reasonable applied to the EIM.[9]

As Balancing Authorities, EIM Entities are responsible for maintaining the supply balance within their respective BAAs. Their resource adequacy requirements are determined by their local regulatory authorities through an integrated resource planning process. Limited infeasibilities will not send price signals to modify that process. They will, however, produce unjust and unreasonable prices for that interval if the power balance parameter penalty is set at a price that would not be appropriate, but for a cost-based justification reflective of extreme conditions.[10]

The CAISO recognizes scarcity pricing through shortage of ancillary service reserves. As reflected in Section 27.1.2.3 of the CAISO Tariff, the graduated shortage pricing is as follows:

---

[9] In an Order issued on July 20, 2015, FERC stated, "[w]e note that CAISO states its intention to explore whether the transmission constraint parameter should be calibrated at different levels, as well as the advantages and disadvantage of reducing the $1,000/MWh parameter price." During the April 9, 2015 technical conference at FERC, the CAISO testified, "[t]hose parameters were designed for the California ISO system" and, "[a]t least from the perspective of the EIM application of that parameter, at this point it may not be the right parameter to use . . . ." *Cal. Indep. Sys. Operator Corp.*, Transcript of April 9, 2015 Technical Conference, Docket Nos. ER15-861-000 and EL15-53-000, at 129–38 (Apr. 9, 2015) at 16–17. The CAISO noted that the EIM only optimized energy, and did not co-optimize reserves. Accordingly, the power balance constraint penalty was not applied in the same way in the EIM as compared to the CAISO market. *Id.* at 18.

[10] As described previously by CAISO,

> Fundamentally, as designed and approved by the Commission, the Energy Imbalance Market serves as a means by which balancing authority areas other than the CAISO can choose *voluntarily* to serve as much, or as little, of their imbalance needs as they wish, and for resources to compete to serve the balancing authority needs of all balancing authority areas in the EIM area. The Energy Imbalance Market does not co-optimize ancillary services and energy, as the CAISO does in its own balancing authority area…Consistent with this principle of the Energy Imbalance Market, the sufficiency tests do not test for resource adequacy. They are designed to evaluate whether each EIM Entity will meet specific capacity tests and flexibility tests to ensure that it does not "lean" on the capacity of any other EIM Entity. The Commission accepted this design of the Energy Imbalance Market, recognizing that "CAISO and the EIM Entities continue to operate under their separate respective tariffs, amended in part for EIM arrangements only. Hence, when the EIM entity fails these tests, the only consequence is that transfers between the balancing authorities are frozen to the levels prior to failing the test. The consequence of failure is not complete isolation of the entity from the Energy Imbalance Market generally. The CAISO's proposed enhancement does not change these rules at all.

CAISO Reply Comments in Docket No. ER15-861 dated May 21, 2015 at 9-11.

Product	Shortage	Impact
Non-Spinning Reserve	Up to 70 MW	$500
	70 MW-to 210 MW	$600
	Above 210 MW	$700
Spinning Reserve	Any amount	$100
Regulation	Any amount	$200
Maximum upward sum		$1,000

Ancillary services are not part of the EIM. Each EIM Entity is responsible for maintaining, deploying, and replenishing their own reserves. Thus, in the EIM, the CAISO is triggering the power balance constraint penalty only at the maximum level, even when there may be extremely limited quantities of bid insufficiencies and when there is no actual physical shortage of resources in the EIM Entity's BAA.

As noted in the December 19, 2019, joint EIM Entity comments referenced above, it is important to differentiate between transient shortages and scarcity conditions. While there is not a definition in the market today that differentiates between "transient shortage" and "scarcity," the Commenters generally find that a transient shortage is one of short duration (1-4 market intervals) and/or of small magnitude. Transient shortages can be caused by forecast error, load bias, or market lag. To illustrate this point, Portland General Electric reviewed its infeasibilities from January 2018 through February 2019 and confirmed that 73% of RTPD infeasibilities and 30% of RTD infeasibilities during this timeframe lasted two intervals or less. These short, low magnitude infeasibilities are not reflective of actual scarcity.

Under FERC and federal court precedent, any non-cost-based incentive or penalty must be needed and no more than needed for the intended purpose[11] and that there must be "a correlation between the incentive and the result to be induced."[12] Also, FERC has stated that it is "not appropriate for a penalty price to apply when no actual scarcity exists."[13] EIM Entities may have resources, such as use-limited, short-start peaking units, that are not participating due to current market rules.[14]

[11] *City of Detroit v. Fed. Power Comm'n*, 230 F.2d 810, 817 (D.C. Cir. 1955), *cert. denied sub nom., Panhandle E. Pipe Line Co. v. City of Detroit*, 352 U.S. 829 (1956) ("*City of Detroit*"); *see also Farmers Union Cent. Exch. Inc. v FERC*, 734 F.2d 1486, 1503 (D.C. Cir. 1984) ("FERC failed to forecast or otherwise estimate the dimensions of the need for additional capacity, and did not even attempt to calibrate the relationship between increased rates and the attraction of new capital."); *City of Charlottesville v. FERC*, 661 F.2d 945, 950 (D.C. Cir. 1981) (citing *City of Detroit*); *Pub. Serv. Comm'n of N.Y. v. FERC*, 589 F.2d 542, 552–53 (D.C. Cir. 1978). The Commission recognized this requirement in its 1992 Policy Statement on incentive ratemaking which stated, the Commission "is free to set rates [above cost-based rates] to provide incentives so long as there is a correlation between the incentive and the result to be induced." *Incentive Ratemaking for Interstate Natural Gas Pipelines, Oil Pipelines, and Electric Utilities*, 61 FERC ¶ 61,168, at 61,594 (1992) (citation omitted).

[12] I*ncentive Ratemaking for Interstate Natural Gas Pipelines, Oil Pipelines and Electric Utilities,*. 61 FERC ¶ 61,168, 61,594 (1992).

[13] *Cal. Indep. Sys. Operator Corp*., 153 FERC ¶ 61,305 (2015) at P. 83.

[14] For example, in March 2018, the CAISO Board of Governors approved rules to allow suppliers to submit market-based bids for commitment costs that would only be mitigated to a reference level if a test in the market detects the resource has commitment cost local market power. Otherwise, these "market-based" bids will only be limited by a circuit-breaker commitment cost bid cap. In addition, market participants would be accorded a negotiated option for

Moreover, PacifiCorp, NV Energy, Idaho Power Company, Arizona Public Service, and Portland General Electric submitted comments on the Flexible Ramping Product Refinements stakeholder process recommending that the CAISO place greater priority on incorporating forecast levels of load, wind and solar in the determination of the real-time flexible ramping requirement. Ensuring that this requirement is properly calibrated is vital in any resource sufficiency evaluation. Stated simply, the power balance constraint parameter penalty price has a different application and effect on the *voluntary* EIM. While the best approach would be to adopt the Draft Final Proposal without modification and not apply an adder to any cost-justified LMPs in any BAAs, it would certainly be unreasonable to apply an arbitrary adder to the EIM power balance constraint parameter penalty price.

III. Decisional Classification

The December 19, 2019, Comments opposed the determination that this initiative falls entirely within the advisory role of the EIM Governing Body. An initiative proposing to change rules of the real-time market now falls within the primary authority of the EIM Governing Body when either: (1) if the proposed new rule is EIM-specific in the sense that it applies uniquely or differently in the balancing authority areas of EIM Entities, as opposed to a generally applicable rule, or (2) for proposed market rules that are generally applicable, if "an issue that is specific to the EIM balancing authority areas is the primary driver for the proposed change."

The December 19 Comments noted the specific circumstances of EIM Entities as individual BAAs responsible to assure adequacy of supply while participating in a voluntary market warranted a different approach, including the differences identified in the following chart.

CAISO	EIM
Co-optimization of ancillary services	Energy-only
Mandatory participation through must-offer requirement	Voluntary participation to economically trade energy
Resource sufficiency achieved through bids	Resource sufficiency test prevents "leaning;" resource sufficiency is a responsibility of EIM Entity as a Balancing Authority
Problems with incenting day ahead deliveries	Not applicable
Graduated scarcity pricing applied based on amount of ancillary service insufficiency.	Power balance constraint penalty may be triggered even if the Balancing Authority Area has no shortage of resources or insufficient supplies of ancillary services

In response the CAISO stated in the Draft Final Proposal,

> In response to the Revised Straw Proposal, some EIM Entities stated in their comments that they objected to this proposed classification. Their objections were focused exclusively on the first topic – i.e., the price of the penalty prices used by the market and market pricing when the power balance constraint is relaxed. Their

determining commitment cost reference levels. However, the CAISO has delayed implementation of this important improvement until late 2022, at the earliest.

> comments explained that they objected strongly to one of the options offered in the Revised Straw Proposal in which the penalty price would be scaled to $2,000/MWh. Their comments argued that the CAISO should instead develop a different methodology for establishing market prices that gradually increase based on the amount of infeasibility to $1,000/MWh. The CAISO believes that this proposal in conjunction with the *Flexible Ramping Product Refinements* initiative addresses these concerns.

As noted in the introduction to these comments, the Commenters greatly appreciate the responsiveness of the CAISO to the substance of their prior comments. However, whether a commenter agrees or disagrees with a proposal or whether the CAISO agrees with or rejects a comment does not justify the decisional classification. Rather it is the subject of the initiative in question and its effect on the EIM Entities that dictate the role of the EIM Governing Body. As explained above, scarcity pricing and the relationship to the power balance constraint "apply uniquely and differently" to EIM Entities. Accordingly, the just and reasonable level of the power balance constraint penalty in the EIM should be considered separately under the primary authority of the EIM Governing Body.

IV. Conclusion

The Commenters greatly appreciate the CAISO's continuing attention to this important issue. These are challenging times and there are many competing priorities. The Final Draft Proposal should be adopted and reflected in a revision to the tariff proposal pending in FERC Docket No. ER19-2757.