UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation	Docket No. ER19-2757-000

MOTION FOR LEAVE TO ANSWER AND ANSWER OF POWEREX CORP.

Pursuant to Rules 212 and 213 of the Federal Energy Regulatory Commission's ("Commission") Rules of Practice and Procedure, 18 C.F.R. §§ 385.212, 213 (2019), Powerex Corp. ("Powerex") moves for leave to answer[1] and submits this answer to the comments and protests submitted in response to the California Independent System Operator Corp.'s ("CAISO") proposed revisions to its tariff to comply with Order No. 831.[2]

I.
ANSWER

A. The Commission Should Reject Requests To Require Verification Of Imports At This Time

In their comments, a handful of California parties argue that the Commission

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[1] Powerex acknowledges that the Commission's rules do not typically allow answers to protests. *See* 18 C.F.R. § 385.213(a)(2). However, the Commission has accepted such answers in the past when they have assisted the Commission in understanding the issues presented, provided additional information for the Commission's decision-making process, and helped ensure a complete and accurate record. *See, e.g.*, *Equitrans, L.P.*, 134 FERC ¶ 61,250 at P 6 (2011); *Cal. Indep. Sys. Operator Corp.*, 132 FERC ¶ 61,023 at P 16 (2010). Powerex requests leave to file this answer because it will meet these criteria.

[2] *Offer Caps in Markets Operated by Regional Transmission Organizations and Independent System Operators*, Order No. 831, FERC Stats. & Regs. ¶ 31,387 (2016), *order on reh'g and clarification,* Order No. 831-A, 161 FERC ¶ 61,156 (2017).

should reject CAISO's compliance filing due to the lack of provisions requiring cost verification of imports.[3] These parties seek to further delay the implementation of the reforms adopted three years ago by the Commission in Order No. 831 unless the CAISO adopts a framework for the verification of import offers—despite the Commission's previous decision in Order No. 831 *not* to require the verification of imports. These commenters argue that raising the offer cap without adopting import verification requirements could subject customers in California to high prices due to tightening supply conditions in the CAISO balancing authority area ("BAA"). These parties further argue that raising the cap applicable to import offers into the CAISO could cause market distortions due to asymmetry between the $2,000/MWh price cap required by Order No. 831 in the CAISO's organized market and the $1,000/MWh soft cap applicable to bilateral transactions in the West.

The Commission should reject these arguments and accept CAISO's proposal. As an initial matter, in Order No. 831, the Commission determined that the application of a $2,000/MWh offer cap to imports into an organized market without a cost verification requirement is consistent with the long-standing approach to the treatment of imports in those markets and avoids the significant difficulties associated with verifying the costs underlying import offers.[4] Consistent with this reasoning, the Commission has approved proposals by every other

[3] *See, e.g., Cal. Indep. Sys. Operator Corp.*, Notice of Intervention and Protest of the Public Utilities Commission of the State of California, Docket No. ER19-2757-000 (filed Sept. 26, 2019); *Cal. Indep. Sys. Operator Corp.,* Motion to Intervene and Comments of the Department of Market Monitoring, Docket No. ER19-2757-000 (filed Sept. 26, 2019) ("DMM Comments").

[4] Order No. 831 at PP 195-196.

organized market to increase the offer cap applicable to imports without subjecting import offers to verification.[5] None of the commenters have provided a basis for reaching a different result in this case.

The Department of Market Monitoring's ("DMM") claim[6] that market distortions would result from adopting a $2,000/MWh hard cap for imports while the Western Electricity Coordinating Council ("WECC") soft offer cap of $1,000/MWh remains in place is simply not valid, as it fails to recognize key differences between the CAISO's organized market and bilateral trading throughout the rest of the WECC. Most critically, the CAISO's organized markets both award schedules and determine prices on an hour-by-hour (or sub-hourly) basis, while energy in the rest of the WECC is sold predominantly on a day-ahead and forward basis in 8-hour and 16-hour blocks, with a single price that applies to each hour of the multi-hour transaction. In other words, an external supplier may only receive an import award from the CAISO for a handful of hours—or even just a single hour—over the course of the day, and with a different price being applied for each hour. This distinction is significant. The result is that an external supplier may be faced with two choices:

1. Sell a uniform quantity of energy across 16 hours at a single price via a bilateral transaction with a purchaser outside of the CAISO grid; or
2. Offer to sell energy during those same 16 hours to the CAISO market, where both the quantity of energy that is sold (if any is sold at all) as well as the price that will be received can vary hour by hour.

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[5] *See, e.g., PJM Interconnection, L.L.C.*, 163 FERC ¶ 61,002 (2018); *New York Indep. Sys. Operator, Inc.,* 161 FERC ¶ 61,151 (2017); *Sw. Power Pool, Inc.,* 161 FERC ¶ 61,154 (2017); *Midcontinent Indep. Sys. Operator, Inc.,* 162 FERC ¶ 61,270 (2018); *ISO New England Inc.*, Docket No. ER17-1565-000 (Nov. 9, 2017) (unpublished letter order).

[6] DMM Comments at 10-11.

This structural difference illustrates how external suppliers may evaluate opportunities to sell bilaterally at a single price relative to hour-by-hour sales into the CAISO markets, where prices in some hours will be below the multi-hour bilateral price but prices in other hours will be above it.

An example of the relationship between CAISO hourly prices and the price of multi-hour energy transacted in the bilateral markets is illustrated by comparing prices in the CAISO day-ahead market at COB against bilateral day-ahead prices at Mid-Columbia on February 11, 2019. Bilateral contracts traded on ICE for 16-hour on-peak energy for February 11 had a weighted average price of $218.65/MWh.[7] CAISO day-ahead prices at COB averaged $162.45/MWh during the same 16 on-peak hours. Despite CAISO prices being significantly lower *on average,* the CAISO prices during *three individual hours* significantly exceeded the bilateral price, with the highest single-hour CAISO price reaching $255.34/MWh.

As the data from February 11, 2019 illustrates, hourly prices in the CAISO market must generally exceed the multi-hour bilateral prices during some hours in order for the CAISO markets to be able to compete to acquire external supply. Under most conditions, the current offer cap in the CAISO market does not prevent this from occurring, and the CAISO market prices are able to broadly converge to bilateral transaction prices elsewhere in the west.

On certain days, however—such as when conditions in the western region are tight and/or natural gas prices are elevated across the region—the existing

[7] Source: U.S. Energy Information Administration, *available at:* https://www.eia.gov/electricity/wholesale/.

CAISO offer price cap can be expected to hamstring the ability of the CAISO markets to compete for the limited available external supply. On March 4, 2019, for instance, day-ahead on-peak bilateral prices at Mid-Columbia reached $890/MWh for the 16-hour product. If the CAISO BAA sought to procure external supply under these conditions, CAISO market prices in at least *some* hours would need to be considerably above this level. It is under this type of infrequent but critical condition in which raising the offer price cap to $2,000/MWh, consistent with Order No. 831, will strengthen the ability of the CAISO markets to compete to acquire external supply to meet the reliability needs of the CAISO BAA. Conversely, *failing* to raise the CAISO offer cap on imports is likely to hamper CAISO's ability to compete to attract voluntary external supply during critical days with tight regional market conditions and/or elevated natural gas prices.

Ensuring that the CAISO markets are able to compete to acquire external supply is increasingly necessary to meet the needs of the CAISO BAA. It is widely acknowledged that there is a substantial and growing gap between the quantity of resources committed through California's resource adequacy program and the needs of the CAISO BAA. This resource adequacy shortfall only *increases* the importance of accepting CAISO's proposal. As the Commission has acknowledged, allowing prices to increase during periods of scarcity is necessary to encourage resources to respond when they are most needed.[8] Increasing the

[8] *Settlement Intervals and Shortage Pricing in Markets Operated by Regional Transmission Organizations and Independent System Operators,* Order No. 825, 155 FERC ¶ 61,276 at P 6 (2016) (explaining that implementing shortage pricing during periods where there is a shortage of energy or operating reserves "will provide an incentive for resources to ensure that they are available to respond to higher prices, which should

offer cap applicable to imports will help encourage external resources to voluntarily offer their supply to the CAISO's hourly markets, particularly during periods when conditions are tight throughout the west. Rejecting the proposal, in contrast, will only serve to exacerbate the supply challenges facing the CAISO by preventing the market from sending the price signals necessary to compete for voluntary external supply during critical days with tight regional market conditions and/or elevated gas prices.

B. Further Discussion Of The Penalty Pricing Parameter May Be Warranted

In their protest, the EIM Entities argue that the Commission should reject CAISO's proposal to increase the penalty price that applies when there is a power balance infeasibility from \$1,000/MWh to \$2,000/MWh.[9] These commenters express concern that the application of a \$2,000/MWh pricing parameter has not been supported and may lead to unjust and unreasonable outcomes when applied to the Energy Imbalance Market ("EIM").

Powerex is very sympathetic to the concerns expressed by the EIM Entities. As the EIM Entities acknowledge, certain of the EIM Entities have experienced significant price spikes when the market optimization software encounters "infeasibilities" in matching supply and demand. It is Powerex's understanding that these infeasibilities are usually quite small and may be due to modeling limitations or other technical market issues, rather than indicating any genuine scarcity of

help alleviate shortages and avoid shortage pricing during subsequent dispatch intervals").

[9] *Cal. Indep. Sys. Operator Corp.,* Motion to Intervene and Protest of the EIM Entity Parties, Docket No. ER19-2757-000 (filed Sept. 26, 2019).

supply. Nevertheless, the “all or nothing” approach to shortage pricing in CAISO results in the application of a single penalty price in such situations, which must be equal to or greater than the bid cap. This approach to shortage pricing stands in contrast to the shortage pricing frameworks employed by other organized markets, which are designed to allow prices to gradually increase as supply conditions tighten. Typically, this is accomplished by applying a relatively modest penalty price to small shortages, with the penalty price increasing as larger supply shortfalls—which are more likely to reflect material scarcity rather than technical issues—arise.

Powerex therefore encourages CAISO to work with EIM Entities and other stakeholders to explore solutions that avoid extreme increases in prices for small infeasibilities while ensuring that significant penalty prices are applied when there is material supply scarcity and/or shortages. One potential approach to achieving these dual objectives could be to adopt graduated penalty pricing. For these reasons, Powerex believes the challenges that EIM Entities are experiencing related to CAISO’s implementation of penalty pricing require attention in a CAISO stakeholder process.

II.
CONCLUSION

Wherefore, for the foregoing reasons, Powerex requests that the Commission issue an order consistent with this answer.

Respectfully submitted,

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For Powerex Corp.

October 11, 2019

CERTIFICATE OF SERVICE

Pursuant to Rule 2010 of the Commission's Rules of Practice and Procedure, I hereby certify that I have this day served a copy of the foregoing on all persons designated on the official service list compiled by the Secretary in this proceeding.

Dated at Washington, D.C. this 11th day of October, 2019.

/s/ Stephen J. Hug
Stephen J. Hug

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