Comments of Powerex Corp. on Capacity Procurement Mechanism Soft Offer Cap Issue Paper

Submitted by	Company	Date Submitted
Mike Benn 604.891.6074	Powerex Corp.	July 1, 2019

Powerex appreciates the opportunity to submit comments respecting the CAISO's May 30, 2019 Capacity Procurement Mechanism Soft Offer Cap Issue Paper ("Issue Paper") and related working group meeting.

As the entity charged with maintaining reliability in the CAISO balancing authority area ("BAA"), it is critical that CAISO have the tools necessary to meet its reliability obligations. The Capacity Procurement Mechanism ("CPM") enables the CAISO "to procure backstop capacity when … insufficient resource adequacy (RA) capacity was procured to ensure reliability[.]"[1] The CPM is thereby the means through which the CAISO can step in to address shortcomings in California's RA framework that, if unaddressed, may leave CAISO operators with access to insufficient resources to safely and reliably operate the grid.

The CPM has taken on greater importance as gaps in California's RA framework have become more apparent and significant. Moreover, there has been a dramatic change in the availability of surplus capacity in areas of the Western Interconnection outside of the CAISO BAA. The retirement of baseload thermal generation, the growth of renewable resources, and growth in peak demand have all combined to significantly reduce or even eliminate the surplus capacity that historically could be assumed to be available in the *short-term* energy markets.

These shifts paint a stark picture for maintaining reliability in the CAISO BAA: the resources *within* the CAISO BAA are no longer sufficient to ensure resource adequacy, while resources *outside* the CAISO BAA can no longer be counted on to be available to supply the CAISO BAA unless they have explicitly committed to doing so on a forward basis. Simply put, maintaining reliability of the CAISO BAA increasingly depends on the ability of the entities responsible for reliability in the CAISO BAA to effectively compete to secure forward commitments from external suppliers.

Powerex believes that a comprehensive overhaul of California's RA framework is necessary to adequately ensure resource adequacy of the CAISO BAA. Powerex

[1] Issue Paper at 3.

supports CAISO's past and ongoing efforts to advocate for critical changes in the RA framework before the CPUC, and in its own stakeholder processes. Recent CPUC actions indicate a growing recognition of the need for such improvements.[2]

Where deficiencies in California's RA framework leave the CAISO to ensure that sufficient resources are committed on a forward basis through the CPM, it is vital that the CPM be as effective as possible. While Powerex recognizes that any changes to the CPM will be of limited effectiveness until more comprehensive changes to the RA framework are implemented, there are steps CAISO can take to make the CPM more effective in procuring forward RA capacity if and when that mechanism is called upon to address procurement shortfalls. Specifically, Powerex recommends that CAISO undertake CPM procurement activities in a manner that is better aligned with the products and timelines under which capacity is committed on a forward basis (including forward contracts for stand-alone capacity of for firm energy) in the bilateral markets in the west outside of the CAISO BAA. These forward capacity and forward firm energy transactions are increasingly for seasonal and annual products, and there is growing interest in obtaining these commitments on a long-term basis, often with terms of one to five years.

Powerex believes that the following changes would help CAISO's CPM to more effectively compete for forward capacity from external resources:

- **Procure CPM capacity as a six-month product** for summer (May-October) or winter (November-April). California's use of single monthly contracts provides suppliers with limited compensation, making such sales unattractive to external suppliers that have alternative opportunities to commit their surplus capacity on a forward basis under seasonal, yearly, and multi-year contracts. At the same time, use of a six-month product retains the ability for CAISO and California load-serving entities to realize savings associated with seasonal diversity between the CAISO BAA's summer-peaking system and those entities with surplus capacity that either experience a winter peak or make sales of surplus capacity for the winter season.
- **Procure CPM on a year-ahead basis**. Sufficient lead time is critical to allowing a seller to plan its system to take into account its forward capacity commitments. This may be especially important for storage hydro systems in the northwest, which can make firm capacity available through advance planning, but which may not otherwise be available as "residual" capacity without such forward commitments and planning. If contracting is deferred until a month ahead, many operational planning decisions will already be implemented, and forward sales of surplus capacity may already be committed to purchasers in other regions, limiting any CPM procurement to whatever residual capacity may be available. As discussed above, the residual capacity that may have frequently been available in prior years

[2] *Order Instituting Rulemaking to Develop an Electricity Integrated Resource Planning Framework and to Coordinate and Refine Long-Term Procurement Planning Requirements*, Assigned Commissioner and Administrative Law Judge's Ruling Initiating Procurement Track and Seeking Comment on Potential Reliability Issues, Rulemaking 16-02-007 (June 20, 2019).

on a monthly basis and/or in the short-term energy markets has largely disappeared, and reliance on short-term energy markets and monthly capacity procurement may result in an inability to achieve procurement targets.

- **Apply a soft offer cap on an annual basis.** The application of the soft offer cap of $75.67/kW per year as a pro-rated cap on *monthly* CPM contracts is illogical and self-defeating. Powerex does not necessarily object to limiting the annual compensation to sellers of capacity to an estimate of the net cost of new entry ("Net CONE"). However, the current soft offer cap takes an *annualized* value of the net cost that must be recovered *each year for multiple years* to support new investment, and then further divides that annual number by 12. It should be self-evident that no new resources can be built on the basis of a single month of forward capacity sales, even at a price that is several multiples of the current monthly soft offer cap. Powerex believes a workable near-term approach may be to use a soft cap to limit the total annual revenues received by a supplier from forward capacity contracts (RA or CPM). For instance, a resource with no forward capacity sales other than CPM would be subject to a higher soft offer cap than a resource that has already sold RA capacity for 6 months of the year.