

**Comments of Powerex Corp. on
System-Level Market Power Mitigation
Initiative Scoping Document**

| Submitted by | Company | Date Submitted |
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Powerex appreciates the opportunity to provide these comments on the CAISO’s October 28, 2019 *System-Level Market Power Mitigation Initiative Scoping Document* (“Scoping Document”).

The Scoping Document sets forth carefully-considered principles and a “Phase 1” approach developed by CAISO staff to mitigating system-level market power in the CAISO balancing authority area (“BAA”) in the real-time market. **If** the CAISO were to move forward with the near-term implementation of BAA-level market power mitigation in the CAISO BAA in the real-time market, Powerex believes the CAISO’s proposal provides an appropriate conceptual starting point for further stakeholder discussions.

However, Powerex does not support moving forward with the Phase 1 proposal at this time, for several key reasons:

1. **None of the evidence provided by CAISO and DMM to date indicates that there is system-level (i.e., CAISO BAA-level) market power being exercised today (or in recent years).** To the contrary, the evidence shows that CAISO markets are workably competitive, including on days with elevated day-ahead market prices. CAISO day-ahead prices are generally converging, *on average*, to prevailing market prices in other western regions, when appropriately examined on a 16-hour block basis. On some critical days, CAISO 16-hour average market prices may be modestly above 16-hour prices in external regions, while on other critical days CAISO 16-hour average market prices are modestly lower. This broad convergence is consistent with normal, expected, day-to-day price differences, largely resulting from the sequential nature of regional trading timelines.
2. A closer examination of the evidence shows that **the potential for the exercise of system-level (i.e., CAISO BAA-level) market power rarely, if ever, exists today.** During the very limited number of hours and days that CAISO and DMM have identified as having low RSI values, there was additional transmission capacity available to access additional external supply, but this additional potential supply was not included in either CAISO’s or DMM’s RSI calculations. Powerex believes a closer examination of these hours and days would show that this additional potential external supply would likely be sufficient to eliminate any potential for system-level market power (importantly, such potential supply is best understood as *responsive to expected*

CAISO prices, and thus exceeds the quantity of explicit supply offers submitted at CAISO's interties).

3. **There will always be inherent inaccuracies in determining the potential for, and the actual exercise of, market power, as well as in the application of market power mitigation measures.** It is widely recognized that Default Energy Bids in organized markets are unable to accurately reflect the actual opportunity costs of each resource as it changes day to day and hour to hour. This means that any mitigation measures must be used with caution; they should not be applied to circumstances that rarely arise and/or where strong evidence is lacking on the potential for, or exercise of, market power.

While the evidence presented to date does not support a finding of actual or potential exercise of system-level market power, the increasing frequency of price spikes and greater price volatility indicate different challenges that do require immediate attention. In Powerex's view, the main reason for more frequent elevated prices across the CAISO BAA is the numerous gaps in the California Resource Adequacy ("RA") framework, including the participation of paper capacity at the interties, the participation of certain internal resources that frequently fail to perform in critical hours, and the failure to consider expected forced outage rates in RA resource qualifications. Addressing these serious RA issues—which is needed to ensure reliability and to promote efficient market outcomes in the years ahead—should also significantly reduce the potential for the exercise of system-level market power in the CAISO BAA, at least for the next few years.

The CAISO is about to embark on several key market design initiatives, particularly the DAM Enhancements ("DAME") and Extended DAM ("EDAM") initiatives. These initiatives will consume extensive CAISO and stakeholder resources, and each is expected to materially alter the core design of the CAISO's markets. It is far more efficient to examine the need for, and design of, system-level market power mitigation in the context of the market design that will exist in the years ahead, rather than the one that exists today.

Although Powerex opposes moving forward with the development of piecemeal "Phase 1" market power mitigation measures at this time, ***Powerex is supportive of incorporating this issue into the scope of the DAME and EDAM stakeholder processes.***

Powerex recognizes that there is an increasing risk that market conditions in the CAISO BAA could, in the future, enable one or more internal suppliers to exercise market power at the system level, when the CAISO BAA is import-constrained. The exercise of market power—whether by sellers or by purchasers—has the potential to distort market-clearing prices and the efficient behavior that those prices are intended to promote. Moreover, price distortions can rapidly lead to a shift of hundreds of millions of dollars of economic value. If prices were to be unduly elevated through the exercise of system-level market power, California consumers could endure significant financial harm, which is not only inequitable but also undermines confidence in the CAISO markets. Powerex believes additional steps may need to be taken in the years ahead to ensure such outcomes do not occur.

Powerex looks forward to the opportunity to engage in constructive dialogue on this topic, including:

1. An examination of new and/or revised local and BAA-level mitigation measures applicable to physical supply in the CAISO's Day Ahead market under the CAISO's DAME Option 2 design; and
2. Consideration of the potential application of reasonable and workable offer price limits and/or mitigation measures to all RA resources—including import RA resources—as part of comprehensive reforms to the RA program.

Notwithstanding Powerex's position as a net seller of products in CAISO's markets, Powerex supports careful examination of system-level market power concerns and the development of appropriate measures that may be necessary to address those concerns. In Powerex's view, when material market inefficiencies are allowed to persist, including but not limited to those that cause material harm to California load-serving entities, confidence in CAISO markets can suffer. For this reason, Powerex has repeatedly supported efforts that lead to more efficient and equitable market outcomes. For example, Powerex supported CAISO's suspension of intertie virtual bidding in 2011 (an issue that cost California ratepayers \$58.6 million)¹, and, more recently, Powerex provided suggestions and support for carefully crafted measures to address the losses being incurred by California ratepayers associated with the CRR auction process. Powerex similarly looks forward to constructive and collaborative dialogue on new and/or revised market power mitigation measures, in the context of DAME and EDAM, to ensure net wholesale market purchasers in CAISO markets are not unduly harmed in the years ahead as grid conditions continue to tighten.

However, Powerex believes stakeholder initiatives and dialogue on market inefficiencies cannot selectively focus on just those issues that may inefficiently elevate market prices and/or otherwise cause harm to California load-serving entities. There are numerous other market inefficiencies in CAISO markets that are currently causing day-ahead and real-time market prices to be inefficiently suppressed and/or are otherwise causing harm to physical suppliers. In Powerex's view, several of these issues are far more pressing than the concerns raised in this stakeholder process, as there is substantial, ongoing, material harm occurring in several of these areas. Importantly, such inefficiencies not only harm net sellers internal to the CAISO BAA, but also harm ratepayers in other regions who are the ultimate beneficiaries of surplus sales in CAISO markets. Such issues include:

- Extensive and highly distortionary **out-of-market procurement** of supply to meet day-ahead imbalance reserve needs, particularly in evening peak hours;
- Frequent, and highly distortionary **load biasing** in the CAISO BAA to meet day-ahead imbalance reserve needs, particularly in evening peak hours;
- Significant systemic **EIM GHG allocation inaccuracies** that shifts the value of clean attributes to other entities, and inefficiently lowers system-wide market prices;
- **The inclusion of speculative physical supply** in the RA program, and in the CAISO markets more generally, inefficiently displacing real physical supply;

¹ *Cal. Indep. Sys. Operator Corp.*, 143 FERC ¶ 61,087 at P 30 (2013).

- An EIM Resource Sufficiency test that enables **CAISO BAA leaning on other BAAs** for capacity and flexibility, particularly in the evening peak (rather than requiring California load-serving entities to acquire sufficient physical capacity and flexibility on a forward basis through an improved System RA program);
- **The lack of robust, graduated, scarcity pricing** in CAISO markets, as the existing scarcity pricing rules rarely apply, notwithstanding frequent market interventions to address the risk of shortages during tight hours; and
- **Extensive use of side-payments to provide additional compensation to thermal generation**, particularly fast-start resources, when FERC, and the rest of the industry, is clearly moving in the direction of efficiently incorporating start-up and no-load costs into market clearing prices.

Powerex recognizes and appreciates that CAISO is aware of each of these issues and has generally included these topics for discussion in other stakeholder processes. Powerex raises these issues in these stakeholder comments because it is concerned that the central issue here—system-level market power—is not a problem that exists today, yet it is being disproportionately prioritized, consuming accelerated attention and scarce resources, ahead of other critical price formation issues. As CAISO continues to expand the footprint of its markets, Powerex believes it is vital that market inefficiencies affecting California load-serving entities do not continue to be elevated in importance and priority, by either CAISO or DMM, over market inefficiencies that affect other entities and regions.