CASPR Proposal: New England States' Initial Thoughts

New England States Committee on Electricity

NEPOOL Markets Committee

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Disclaimer – It's early in the process

- Today's presentation includes some initial thoughts on the CASPR proposal.
- States' thinking will continue to evolve as the proposal moves forward in the NEPOOL process.
- The concepts laid out today are related to high-level, material concerns we see currently with the proposal.
- Other concerns and positions will emerge with continued dialogue and understanding.
- Today, we welcome feedback on our initial thoughts.

Three Primary Concerns, so far…

- Removal of the Renewable Technology Resource ("RTR") exemption
  - Procurements now underway in which states and market participants have counted on it being in place
- Lack of certainty offered by CASPR alone
- Increased consumer cost risk

Additional concerns/preferences will likely emerge as the proposal moves forward.

Concern One - Renewable Exemption

A quick look back, for perspective -

- ISO-NE, NEPOOL and six states supported the RTR exemption.
- FERC has now issued ***four*** orders in which it concluded that the RTR exemption is just and reasonable.

Working Together – We Need Balance

- **2012:** In proceeding addressing multiple FCM design changes, FERC clarified that ***"[p]arties are free to introduce and develop categorical exemptions*** or other measures in the stakeholder process." *ISO New England Inc.*, 138 FERC ¶ 61,027 at P 91 (2012).
- **2013:** FERC encouraged stakeholder process to develop exemption.
  - ". . . given the large number of stakeholders that supported some form of renewable resource exemption, ***we encourage ISO-NE to undertake the development of a stakeholder process for such an exemption***, which could include the development of a demand curve." *ISO New England Inc.*, 142 FERC ¶ 61,107 at P 97 (2013).
- **2013:** FERC acknowledgement that it must balance state policies in market design.
  - ". . . the Commission must balance two considerations. The first is its ***responsibility to promote economically efficient markets and efficient prices***, and the second is ***its interest in accommodating the ability of states to pursue other legitimate state policy objectives."*** *NESCOE v. ISO New England Inc.*, 142 FERC ¶ 61,108 at P 35 (2013).

Competitive Capacity Pricing

- **RTR exemption has been found to be Just and Reasonable**
  - 2014 Demand Curve Order
  - 2015 Rehearing Order: Upheld RTR exemption as Just and Reasonable
  - 2016 Remand Order: Reaffirming RTR Exemption as Just and Reasonable
  - 2017 Rehearing Order: Reaffirming for a third time that the RtR exemption is Just and Reasonable

- **Any assertion that the RTR exemption does not preserve competitive pricing is incorrect.**
  - *Consistent with the four FERC orders, the RTR exemption is J&R and the "FCM with the exemption is the appropriate price."*

- **Three auctions (FCAs 9-11) have been completed with over 2,700mws of new entry since the implementation of the RTR exemption, the market continued to reflect robust interest in the FCM irrespective of RTR exemption state procurement activity was widely known and publicized**

Competitive Capacity Pricing

- "One purpose of capacity markets is to send ***appropriate price signals regarding where and when new resources are needed****.* If renewable resources are being built, but are not reflected in the FCM, then the FCM may send an incorrect signal to construct new capacity that is not needed. ***Not only would the capacity market send an incorrect signal, but customers would have to pay for capacity twice*** – first, for renewable resources via out-of-market mechanisms and second, for additional capacity that is procured because the capacity market has sent the incorrect signal that additional capacity is needed." *ISO New England Inc.*, 158 FERC ¶ 61,138 at P 9 (2017)

- "[T]he price that generators receive in the FCM with the exemption ***is the appropriate price*** because it elicits sufficient entry into the FCM to maintain reliability at least cost, as well as providing a balance between supplier and customer interests." P 46

Accommodate Entry Objective

- "The renewables exemption **fulfills the Commission's statutory mandate by protecting consumers from paying for redundant capacity.** As discussed in ISO-NE's filing, the redundant capacity results from consumers paying for capacity that cleared through the FCA and separately paying for renewable resources built by state entities to meet state policy objectives." *ISO New England Inc.*, 155 FERC ¶ 61,023 at P 33 (2016).

- Maintaining the renewable exemption **balances the responsibility** to promote economically efficient markets and efficient prices, and accommodating the ability of states to pursue other legitimate state policy objectives as noted in NESCOE v. ISO New England Inc., 142 FERC ¶ 61,108 at P 35 (2013).

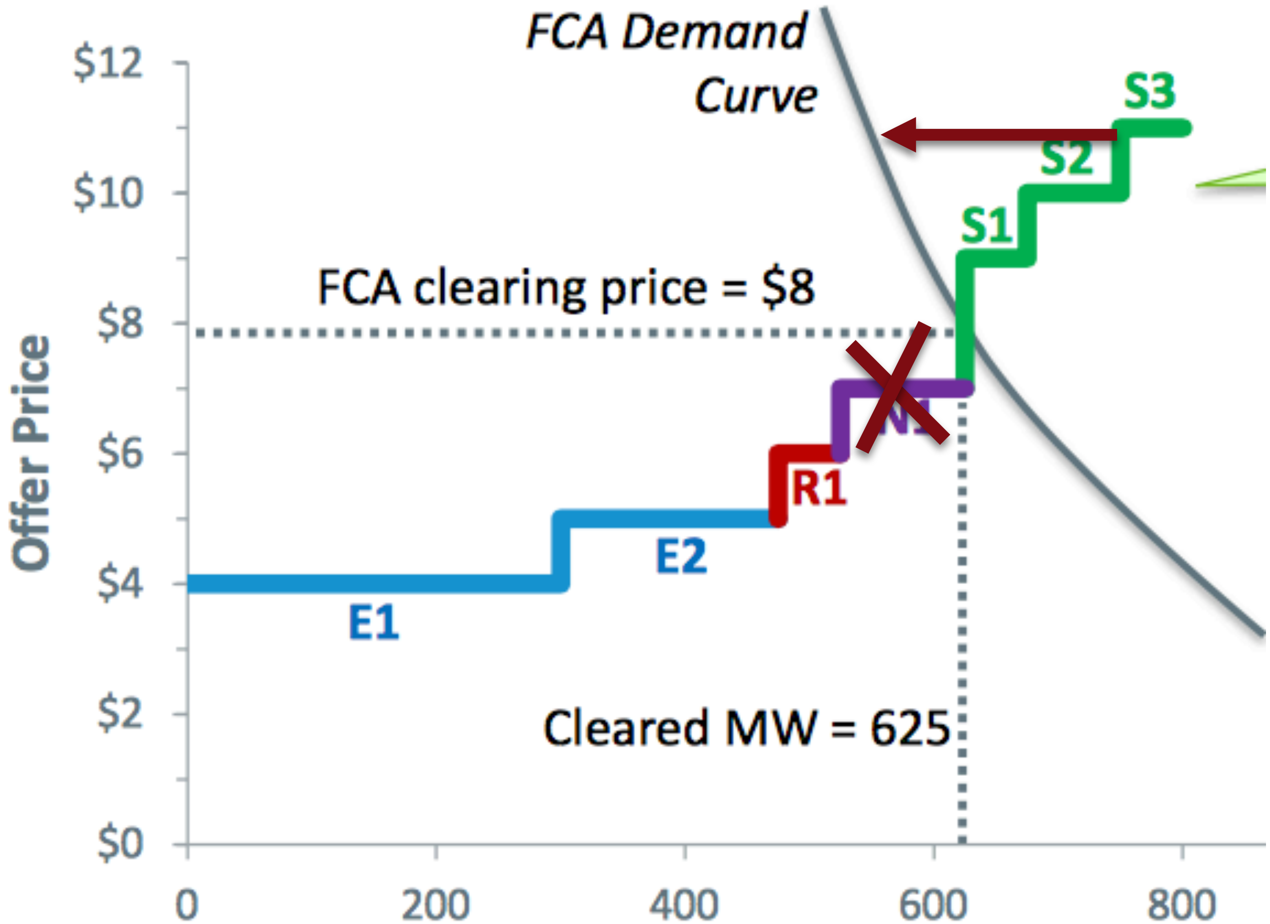
Concern Two - Certainty

- The ability to swap CSOs is dependent on sufficient demand in the substitution auction (“SA”). **CASPR will not Accommodate state needs -**
  - If no Retirement or Permanent De-list bids receive a CSO, then there is no demand in the SA, or
  - If the timing or size do not match up
- **States have issued several RFPs that are now in process in which states and market participants expected to be able to use the RTR exemption in FCA13**
  - The Three State and CT procurements are mostly resources that would qualify under the RTR exemption (RPS-eligible)
  - At least in theory, participants took the RTR into account when preparing bids. States assumed the RTR would be there, too.
  - Under CASPR as proposed, FCA13 auction would start out with a surplus of supply for the SA – “starting out in a hole”.

Concern Three – Cost Risk

- This concern relates to the "Fictitious Entry" rule.
- Other stakeholders have noted the same consumer cost concerns.
- Still other stakeholders have noted different concerns:
  - Cost to qualify for participation in the auction will be lost, leading to limited participation.
  - Naturally clearing resources - which states want for consumers - will be replaced by those that receive contracts.
  - Will change investor actions by making the act of getting a contract from a state the primary way to enter the market ("market focus").

FCA "Blow Out" Concern



If new supply (N1) is deterred from participating in the FCA, the risk exposure is participating resources in the PA are only those with mitigated higher prices (S1,S2,S3) which slide to the left.

Every $1 increase is approx. $400M in consumer costs.

What are Options to the Fictitious Entry Rule?

- Several suggestions have been made to date:
  1. All new entry keeps its CSO
  2. Allow only the likely beneficiaries of the Fictitious Entry rule to keep their CSO, DR/EE.
  3. Pay a minimum payment to new resources if their CSO is swapped out to cover the cost of participation.
- System conditions will change risk perspective
  - For example, in today's over-supply condition with limited load growth and a demand curve moving to the left, the likelihood of new clearing is low.
  - As the system reaches closer to NICR this concern will grow
    - However with DR/EE being replaced a FCA "blowout" could still occur just at much lower level (only move slightly up the demand curve)

Option One to Fictitious Entry Rule

- **Allow all new entry to keep the CSO**
  - This solves the "blow out" risk but fails objective No. 2 - to limit oversupply.
  - The annual cost of oversupply is much lower (e.g. 1,000mw x $11/kw-mth = $132M per year) however -
  - The probability of a FCA blowout is low-medium compared to the probability of oversupply, which is high (e.g., states will meet their state laws)
  - Solves concern of natural clearing resources and "market focus" concerns.

Option Two to Fictitious Entry Rule

- **Allow DR/EE to Keep the CSO**
  - Limits the Fictitious Entry issue to those resources less likely to take advantage of the Fictitious Entry gaming opportunity.
  - Limits but doesn't remove the "blow out" risk.
  - Doesn't solve natural clearing resources or "market focus" concerns.

Option Three to Fictitious Entry Rule

- **Make a minimum payment to new resources whose CSO is swapped out**.
  - Removes blow out risk if payment is high enough to encourage participation in the PA.
  - Will prevent oversupply
  - Doesn't solve natural clearing or market focus concerns.
  - Will add consumer costs

Preliminary Initial Thought Forward

To meet the objectives of competitive pricing, certainty, avoiding shifting risks to consumers, and ensuring robustness, an initial way forward is as follows:

1. **Maintain but modify the RTR exemption**

2. **Allow all new resources that receive a CSO in the primary auction to retain their CSO.**

Change the Fictitious Entry Rule

- Allow all new resources that receive a CSO in the primary auction to retain their CSO
  - Solves many of the concerns stakeholders have noted to date.
  - Ensures that non-procuring states (and procuring states) do not add incremental consumer cost risk to the markets as a result of this change.
- BUT, makes meeting objective No. 2 harder
  - SO how to fix that…..

Modify the RTR Exemption

- Remove the current resource definition (do not restrict to renewable or alternative energy portfolio standards as defined in state laws in effect on January 1, 2014)*

- Transition the annual MW carryforward cap to 500mws in FCA13, 300MWs in FCA14,and then 200mws annually there after (basically eliminate the current just and reasonable rolling carryforward)

*The definition of who/what can enter as supply in the substitution auction is an open and important question.

RTR and CASPR - Hand and Hand

- **Transition is needed to accommodate actions now in process**
  - Similar to need of the transitional demand curve.
  - State and market participants expected the RTR exemption, which FERC has upheld *four* times. to be in place; removing it mid-course is seriously problematic, frustrates expectations, creates real fairness problems.
- **Known future accommodations (through transparent state actions and RTR exemption) will provide price stability and incentive to act under CASPR**
  - Knowing that supply in the substitution auction will dry up over time, resources will act accordingly to take advantage of the CASPR incentive ("severance payment").
- **Result: less use of the RTR exemption**.

CASPR and the RTR exemption *together*
meet all objectives better than either one alone.

Thank You We Look Forward to Your Questions and Feedback

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