New England States Committee on Electricity

To: ISO-NE, Power Supply Planning Committee
From: New England States Committee on Electricity
Re: Issues Associated with ISO-NE's Proposed Installed Capacity Requirements for 2010/2011 Third Annual Reconfiguration Auction
Date: October 13, 2009

At the Power Supply Planning Committee Meeting on September 29, 2009, ISO-New England, Inc. (ISO-NE) proposed Installed Capacity Requirement (ICR) values for the third Annual Reconfiguration Auction (ARA3) for the 2010/2011 Commitment Year. This third auction is the last auction to be held prior to the start of the 2010/2011 Commitment Year. Therefore, it is the last organized market opportunity for capacity resources to trade obligations and for ISO-NE to add or reduce capacity obligations to meet the revised ICR. The New England States Committee on Electricity (NESCOE) provides herein its perspective on the issue of assumed tie benefits within ISO-NE's proposed ICR calculation.[1]

Under current market rules, ISO-NE is required to calculate ICR for the last ARA prior to the Commitment Period - the auction at issue - using tie benefits estimated assuming "as is" conditions under which neighboring control areas can provide emergency support consistent with their current level of capacity resources. In contrast, ISO-NE must calculate ICR for the Forward Capacity Auction and ARAs preceding the ARA3 using tie benefits estimated assuming "at criterion" conditions under which neighboring control areas are assumed to have "just enough" internal resource to meet the 1-in-10 Loss of Load Expectation (LOLE) standard. Market Rule 1 provides ISO-NE with limited discretion in the calculation of ICR and its subsequent actions in the last ARA in the event that capacity obligations are greater or less than ICR.[2]

---

[1] Certain issues related to ICR determinations, including tie benefit methodologies, "as is" and "at criteria" assumptions, and associated issues are under discussion concurrently in the regional stakeholder process.

[2] Market Rule 1, Section III.12.9: "The ISO shall calculate tie benefits using "at-criteria" assumptions for purposes of modeling the adjacent Control Areas, except that when calculating the Installed Capacity Requirement, the Local Sourcing Requirements and Maximum Capacity Limits for use in the annual reconfiguration auction closest to the relevant Capacity Commitment Period, the ISO shall calculate tie benefits using "as-is" data for the purposes of modeling the adjacent Control Areas. <u>If, pursuant to this Section III.12.9, tie benefits are determined to be different at the time of a subsequent reconfiguration auction than assumed in the Forward Capacity Auction, the total amount of tie benefits assumed available over the interface may be limited, if and as necessary, to the assumed interface limit minus any Import Capacity Resources obligated for the relevant Capacity Commitment Period in prior auctions</u>." (Emphasis added.) Section III.13.4.3(a): "Where more capacity than needed is obligated, the ISO may in its discretion submit supply offers in subsequent annual reconfiguration auctions to release the excess capacity, but in any case the ISO shall be required to submit supply offers as appropriate in the third annual reconfiguration auction for a Capacity Commitment Period to release the excess capacity." Section III.13.4.3(c) provides rules for ISO-NE's supply bides.

With respect to ARA3, tie benefits assuming "as is" conditions are 3,415 MW. As a point of reference, this number is 1,555 MW above the tie benefits value of 1,860 MW used for the 2010/2011 ARA2, based on "at criterion" conditions. According to ISO-NE, this level of tie benefits would leave the region with a 4.3% / 9.3% reserve margin calculated without and with Hydro-Quebec Interconnection Capability Credits.

Although the tie benefits that result for ARA3, as contemplated by the rule, are 3,415 MW, ISO-NE nonetheless proposes a value of 1,860 MW. This number reflects the tie benefits value used in ARA2.

As a general matter, we must rely to some degree on ISO-NE's judgment in connection with technical determinations that relate directly to the reliable operation of the system. However, this is not a matter where ISO-NE has used its technical expertise in developing a proposal. Here, the circumstances in which ISO-NE should have discretion to depart from rules and how it approaches that discretion warrants the region's serious consideration. This is particularly true when ISO-NE's preferred outcomes come at a cost to consumers in excess of what the rules would impose on them. In this case, it is possible that the cost associated with using ISO-NE's proposed tie benefit value could be nearly $65 million greater than the costs that would flow from the rule.

When ISO-NE proposes to depart from the application of a rule, its proposal should reflect analyses of a range of alternatives and include a detailed explanation of reliability needs, estimated emergency events, and cost implications of the various options, along with a rationale for reaching its preferred decision or proposal given the various tradeoffs between alternatives. ISO should also reflect upon the effect that alteration of established market rules may have upon the markets themselves. Drawing a number from a prior year or some other similarly simple method suggests at least an appearance of an ad hoc approach.

ISO-NE's discomfort with the result of tie benefit values contemplated by the rule and it's informal approach to selecting an alternative suggests it would be appropriate for the region to consider adopting criteria to govern the circumstances in which a departure from the rules may be appropriate, the analysis that should be set forth to inform decisions about alternative approaches, and the criteria by which decisions should be made. Consideration of this issue should follow the region's ongoing discussions about appropriate assumptions. In addition to providing stakeholders with a more complete basis for proposed decisions, such criteria could also help provide greater certainty and send appropriate signals to market participants. The discussion above suggests that ISO-NE's proposal requires further analysis, including a rational for the various alternatives presented and the cost implications of these alternatives.