ISO New England's Performance Incentives Proposal

New England States Committee on Electricity

NECA Power Markets Conference

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Any views expressed should not be construed as representing those of NESCOE, or any NESCOE Manager.

At this time, the States do not have a collective view on ISO-NE's Performance Incentive proposal, amendments, or other alternative design proposals.

ISO New England's New Performance Incentives: Right Solution for the Desired Outcomes?

Some Considerations:

- What drivers lead to the need for reform?
  - Has the region fully vetted the *source* of performance problems?
  - Has ISO-NE defined the *precise problem* to be solved?
  - Did ISO-NE use the most appropriate *performance metrics*?
  - To what extent would completed or in-process *market rule changes* affect the need for design change?
  - To what extent does FERC's ruling in the *NEPGA complaint* affect the need for design change?
- Would other more targeted designs provide the same desired outcomes, particularly in light of other market changes that are moving ahead?

What the “Right Solution” Is Turns on Objectives

- **What are the specific objectives?**
  - Achieving better overall system operational performance?
  - Encouraging some resources to invest in gas pipeline or dual fuel capability?
  - Increasing payments for those resources that “perform”?
  - General need to increase capacity payments?
  - Creating mechanism to select better performers?
  - Finding the least cost way to achieve appropriate level of reliability?
  - Accessing faster ramp times?
- **Desired outcomes depend on one’s priorities**

Uncertainty

- **PI is a novel approach intended to drive multiple outcomes**
  - Reasonable people can debate whether a ***novel approach*** is positive or negative
  - Reasonable people can debate the ***economic theory*** on which it is based
    - Consider Round I of the 2013/2014 Winter Program: from time to time, reasonable economic theory runs head on into business decisions

- **Market changes implemented and on horizon**
  - Reasonable people can debate extent to which changes will address performance challenges

- **There has been substantial debate on what outcomes PI would achieve and at what cost to consumers**
  - High probability that debate will extend beyond FERC filing

In the end, consumers are

Mitigating consumer costs is essential.

So where are the States?

At this time, the States do not have a collective view on the ISO-NE Performance Incentive proposal, amendments, or other alternative design proposals.

One Could Argue On One Hand…

- The "need" for PI - function and frequency of the precise problem - is not sufficiently defined, analyzed
- PI is overly broad and blunt
  - Large penalty applies to all suppliers in all circumstances
  - At the end of the day, increases in the cost of doing business find their way to consumers
- PI design is an experiment. Based on an economic theory.
  - Projected results are based on assumptions, which may not reflect real life business risks, decisions
  - Coming at a time when FERC may be looking for greater consistency
- Forecasting supplier performance risk is very subjective
  - Unknown financial risk may increase consumer cost unnecessarily
  - Puts the Internal Market Monitor in the impossible position of justifying risk, raising market power concerns
- Adding risk may push out otherwise economically beneficial resources
- Other more proven designs could get to desired outcomes directly
  - Price signals best placed in the energy and reserve markets

One Could Argue On The Other Hand…

- Shifts from consumers paying resources for simple availability to paying them for a "slice of system responsibility"
- Creates a mechanism to pay "performers" more, "non-performers" less
- Seeks to address reliability issues related to performance now
- Reduces price volatility compared to other designs
- Focuses on performance to help prevent high price events
- Phased-in approach provides short-term incentive to reach better operational performance (building over time to achieve other benefits)
  - Reduces short-term consumer costs, ensuring consumers do not pay more than needed for desired outcomes

Refinements Under Consideration

- Exemption from penalties for events out of capacity supplier's control
  - Transmission outages that affect supplier performance
  - ISO performance reductions due to system reliability needs
- Stop-loss mechanisms

Considerations in Assessing Refinements

Overly burdensome risks on capacity suppliers translate into unnecessary costs to consumers.

Capacity suppliers in best position to control most risks, so most efficient for them to bear risks.

Thank You and Look Forward to the Panel Discussion

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