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Generators Urge FERC to Adopt Centralized Capacity Market in California

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While FERC may be unlikely to mandate a centralized capacity market in CAISO, the complaint proceeding is nevertheless significant since FERC will need to address long-standing, yet increasing, concerns among generators that California's capacity procurement process is flawed.

California's Resource Adequacy Regime

Unlike the three Eastern organized electricity markets,[1] CAISO does not use a centralized resource adequacy procurement process (e.g., a capacity auction) to ensure adequate system capacity and reliability. The reasons for this—and the complex nature of resource planning and capacity procurement in California—are rooted in California's history and its status as a single-state wholesale market subject to both federal oversight by FERC (through CAISO) and state energy policies and initiatives.

CAISO and the California Public Utilities Commission (CPUC) address resource adequacy principally through bilateral, near-term contracting between LSEs and generators of a "Resource Adequacy" (RA) capacity product. For various reasons, including a lack of alignment between resources that LSEs can use to meet RA requirements and those that CAISO actually needs to run its system, the RA market has been viewed by many as flawed. The RA market has increasingly resulted in LSEs not securing capacity commitments from specific generators needed by CAISO—including capacity from flexible natural gas-fired generators that are needed to balance out the system due to increased generation from intermittent resources. This has primarily affected existing natural gas-fired generators, which, unlike new generators, are not eligible under state policy to be included in Investor-Owned Utilities' Long-Term Procurement Plans, since their capacity is already presumed to be available when assessing additional resource needs. As a result, CAISO has had to rely on "last-resort" out-of-market mechanisms to secure capacity from generators that could not sell RA capacity at sufficient prices to sustain operations, even though they are needed by CAISO to operate the system.

The Complaint Proceeding

On June 20, 2018, La Paloma, which owns a 1,124 MW generating facility in McKittrick, California, filed a complaint against CAISO alleging that CAISO's tariff is unjust, unreasonable and unduly discriminatory as it relates to resource adequacy. Premised on the failure of the RA market to send accurate price signals that can attract and retain resources needed for reliability, La Paloma urges FERC, as a remedy, to implement a centralized resource adequacy procurement process like those used in the Eastern markets (i.e., a capacity market with centralized, uniform locational pricing and other key features).

While the complaint was filed by a single generator, it has garnered broad support from other generators and proponents of competitive markets. On August 24, 2018, the Electric Power Supply Association, a trade association representing independent power producers, filed comments supporting the complaint and the implementation of a centralized capacity market. The Western Power Trading Forum also filed comments supporting the complaint. Calpine, a major independent power producer, filed comments supporting La Paloma's claim that the CAISO tariff is unjust and unreasonable as it relates to resource adequacy, but proposed, as a remedy, comprehensive reform of CAISO's backstop capacity procurement mechanisms, which it views as more realistic than a centralized capacity market given the nature of the California market. CAISO, along with various LSEs and public interest groups, has opposed the complaint.

Significance and Next Steps

Complaints about California's wholesale electricity market and capacity procurement process are nothing new. To date, FERC has been reluctant to take action that could be viewed as interfering with the state's energy policy objectives and resource planning process, instead relying on market changes to be considered through CAISO stakeholder processes and CPUC proceedings. La Paloma's complaint reflects an attempt to place the alleged flaws in California's capacity procurement process squarely before FERC to resolve.

In order to direct any reforms, FERC would first need to find the current CAISO market rules unjust and unreasonable. While it is unknown whether FERC will find that La Paloma has met this burden, the complaint comes at a time when the Commission has shown an interest in considering significant reforms to capacity procurement processes in other markets where state policies have allegedly contributed to unjust and unreasonable wholesale market outcomes. Most recently, FERC initiated a proceeding in PJM to consider reforms to address the impact of state energy policies on the wholesale market.[2]

The next step is for FERC to issue an order on the complaint. If FERC were to find the CAISO tariff unjust and unreasonable, FERC could direct reforms to the CAISO tariff or initiate further proceedings to consider such reforms. There is no deadline for FERC to act on the complaint.

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[1] PJM Interconnection, L.L.C.; ISO New England Inc.; and the New York Independent System Operator.

[2] *Calpine Corp. v. PJM Interconnection, L.L.C.*, 163 FERC ¶ 61,236 (2018).

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