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April 27, 2018

FILED ELECTRONICALLY

Independent Electricity System Operator
1600, 120 Adelaide Street West
Toronto, Ontario
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Attention: Stakeholder Engagement

Dear IESO Staff,

Re: Independent Electricity System Operator (“IESO”) – Market Renewal Program (“MRP”) Energy Workstream – Market Power Mitigation Design Considerations (March 27, 2018) Response to the request for feedback

Capital Power Corporation (“Capital Power”) appreciates the opportunity to provide feedback to the IESO on the materials that were presented and discussed at the March 27, 2018 meeting on Market Power Mitigation (“MPM”). The comments herein provide the views of Capital Power based on the preliminary design of the MPM framework. Capital Power looks forward to providing additional feedback as the MRP progresses.

Principles

The MPM framework contemplated by the IESO is an important consideration for the MRP. In establishing an appropriate design, the IESO must consider key principles that underlie a successful MPM framework. Of critical importance is market design that encourages efficient price formation, a level playing field, competitive market outcomes that ensure revenue sufficiency, and regulatory certainty.

Price Formation

There has been a consistent trend in Ontario and other markets across North America where market rules have evolved in a manner that prevents prices from consistently reflecting the cost of delivered energy. While it is appropriate to consider a framework to prevent misuses of market power through the implementation of a mitigation framework, it must also be contingent on reforms to rules that impact price formation.

Capital Power submits that outcomes that are reflective of the underlying fundamentals of competitive markets provide an optimal and efficient distribution of benefits to all market participants. To achieve these outcomes, the penultimate market design should incent competitive behavior among resources in response

to price signals. These price signals should, to the extent possible, reflect the marginal cost of production and the willingness of system demand to continue consuming.

In the absence of a market design that can achieve competitive price formation, the result of which are areas of the market susceptible to the undue exercise of market power, it is appropriate to consider a MPM that prevents abuses in specific circumstances.

Level Playing Field

A well designed MPM framework should support a market design that fosters competition and ensures a level playing field among market participants. This level playing field should ensure equal treatment between new and existing assets, fuel types, companies and locations. In the context of the MPM framework, this ensures market participants can be confident the framework is applied in a manner that is consistent and fair.

Similarly, the MPM framework must ensure a level playing field between resources in the Ontario market and neighboring jurisdictions. This will ensure the province will continue to attract long term investment in generation that is required to maintain local reliability.

Revenue Sufficiency

The experience of generators in markets across North America demonstrates that revenue sufficiency is a recurring concern under most prevailing market designs. A MPM framework should not compound these concerns unnecessarily.

Absent a holistic consideration of MPM frameworks across energy, operating reserves, and capacity markets, the IESO risks causing reliability issues due to revenue sufficiency concerns among merchant generators that will be required to meet long term system needs. The MPM framework implemented by the IESO should prevent misuses of market power, while providing generators a reasonable opportunity to recover their costs and earn a return on capital invested in Ontario.

Regulatory Certainty

With significant changes proposed in the Ontario electricity market, providing certainty in the design and implementation of the MPM is critical for investor confidence. Stakeholder should have clear guidance on timelines for implementation, and conduct that is permissible under the revised framework. Similarly, there should be clear processes and guidance in place that codifies the governance structures that are required for successful implementation of MPM frameworks.

Design Alternatives

The IESO material presented at the March 27th session included preliminary design decisions for the MPM framework that exclusively use Conduct and Impact Tests (“C&IT”). While there is an extensive list of jurisdictions that use similar frameworks, additional analysis should be undertaken to establish C&IT as the most appropriate method for Ontario’s circumstances.

Capital Power submits that additional consideration should be given to complementary structural mitigation that could further tailor the MPM to the Ontario context. Consideration of an additional screen for confirmation of pivotal suppliers should be considered. This should be applied as an initial screen that will conclude whether further evaluation of C&IT is required prior to mitigating offers.

C&IT Design Considerations

Within a C&IT framework, Capital Power submits the following comments for consideration.

Constrained Zone Designations

Constrained zone designations are a critical input to the MPM framework and serve as the key determinant of the C&IT thresholds that are permitted within the zone. Capital Power supports the broad framework which applies a gradual level of mitigation to a zone depending on the degree to which competition is restricted.

Consistent with the principles above, it is necessary that constrained zone definitions are sufficiently adaptable to changing market conditions. As constraints vary, it is necessary to have a framework with adaptive criteria to allow relatively more permissive C&IT thresholds as the frequency of constraints subsides. This will assist in maintaining the proper price signal – one that is reflective of market fundamentals within the respective zone – promoting competitive forces to respond and efficient consumption by load.

Thresholds

In determining thresholds, the IESO must consider the range of possible outcomes that could occur under a competitive market. The threshold should reflect this range, and should be set at a level to allow for prices to reflect underlying fundamentals. Allowing for prices to approach these thresholds in times of tight supply or unexpected events will ensure the market is attracting and incenting new investment in the technologies that are best able to capture this opportunity and serve the reliability of the system. The room that is afforded to market participants under the threshold allows for proper price formation and is a fundamental aspect a well-designed MPM framework.

Reference Levels

Provided that the proper governance framework is in place, Capital Power supports a process to establish reference levels that are reflective of competitive outcomes. Within the materials presented, a method that resembles the approach used in PJM or SPP (Approach 2) would be preferable. Establishing reference levels through the development of a market manual that prescribes appropriate quantification of costs will improve regulatory certainty. Stakeholder should be engaged in the development of the manual, and the process should consider the level of granularity that is necessary to reflect costs across a range of units without undue administrative burden.

In circumstances where mitigation is applied, the MPM framework should allow for stakeholders to contest reference levels if they are not reflective of their true costs. Due to the approximate nature of administratively-determined reference levels, market participants require a process by which they can justify their costs. This process should allow market participants to submit confidential information to substantiate their requests for an alternative reference level.

Governance

As with the other major market reforms being considered through the MRP, Capital Power submits the MPM discussion should include consideration of governance reforms. The governance framework for the MPM framework should be codified to clearly articulate roles, responsibilities, and expectations of regulators and market participants. Included in the governance framework should be mechanisms for stakeholders to engage with regulators to ensure they are treated fairly. The MPM should be subject to regular review to ensure it continues to meet the desired objectives.

Investigation and enforcement action taken by a market monitor will require proper governance. Clear accountability and processes are required for investigation, enforcement, and adjudication of actions taken against market participants. A public information document outlining the investigation procedures should be developed to clearly articulate these aspects of the MPM framework.

Subsidized Resources

Consistent with many jurisdictions across North America, consideration should be given to how to manage the impact that out-of-market payments have on competitive market outcomes. Mechanisms are required to ensure that subsidized resources are not unfairly impacting the ability of other resources to earn sufficient revenues to continue operating in the market. Absent these measures, subsidized resources risk causing premature retirements of resources that would otherwise be economic. Capital Power recommends that the market impact of subsidized resources be considered and addressed as part of the MRP to ensure undistorted price formation and revenue sufficiency.

Capacity Mitigation

As presented, the IESO has explicitly separated the discussion of mitigation in the energy and capacity markets. Capital Power submits that to ensure the principles of price formation, level playing field, revenue sufficiency, and regulatory certainty are upheld, a holistic discussion of mitigation is necessary. As the price in capacity markets will reflect the net cost of new entry ("net-CONE") - a direct reflection of the revenues a reference technology can be expected to earn in energy and ancillary service markets - there must be clear coordination between mitigation frameworks.

Capital Power appreciates the opportunity to provide feedback on the market power mitigation materials presented by the IESO. Should you have any questions on the contents of this submission, please feel free to contact me at (780) 392-5169 or cmrobb@capitalpower.com.

Sincerely yours,



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