

FCA 16 - 18

Dynamic Delist Bid Threshold

Changes

NEPOOL Markets Committee
September 8-10, 2020

Principal Concern

The IMM is proposing that the DDBT be set at exactly its expectation of the next auction clearing price. All delist requests above this level must become statics.

- **Preparing, submitting and locking in prices for statics is much more expensive and risky than dynamics.**
- **This “stickiness” for statics is a disincentive to offer at prices marginally above the DDBT. Failing to recognize this will bias offers and may lead to clearing prices below competitive levels.**
- ***Solution: Set the DDBT at a reasonable margin above the expected clearing price.***

Costs Associated with Statics

The static delist process includes many costs and risks not faced by dynamics, including:

1. Initial decision to to submit static

- Includes time and cost to educate management and staff on process, cost and risk (start ~ 10 mos before FCA)

2. Develop initial estimate of desired delist price

- Based on owner's market assessments, philosophy, risk perspectives, hedging, internal processes, etc. Resource owners do NOT typically fill out a workbook to find out the price at which they want to exit the market.
 - If they are lucky, then the owner's initial price will be similar to the ultimate workbook price; if not: much more work ahead.

Costs Associated with Statics (2)

3. Develop workbook

- **Trainings, and then completing, checking workbook entries**
- **Convert internal philosophy and pricing into something that fits in the workbook paradigm**
- **Consult with the IMM**

4. Finalize and submit workbook

- **Develop backup for estimates in workbook – proformas, contracts, etc.**
- **Get corporate officer to review and certify pricing and workbook entries**
- **After submission, answer IMM questions, provide additional backup as requested**

5. QDN response

- **Review IMM results**
- **Decision-making process**
 - **Review latest market fundamentals, forecasts, regulatory issues and risk of early price lock**
- **Determine and lock in price ~ October 9**

Lock-in Risk

The October lock-in carries significant risks

- **Inability to account for market and regulatory information that may come between October and February:**
 - **Key FCM data, including ICR/LSR values, ISO Qualification filings, Waiver Requests, FERC action on pending FCM questions, ISO proposals for other markets, state & federal regulatory actions.**
 - **Political changes – elections and possible market impacts**
 - **Market changes – forwards, interest rates, public announcements, financial changes to owner**
 - **Physical changes to units or portfolio**
- **Inability to react dynamically in the FCA (remember, the whole point of the Descending Clock was to allow the resources to react in real-time)**

Dynamics vs. Statics

The static delist must bear all the costs, effort and risks discussed on the past several slides. Dynamics do not.

RESULT 1: STATIC DELISTS WILL RATIONALLY IMPUTE THESE COSTS AND RISKS INTO BIDS.

- The sum of these risks and costs is \$xx/kW-mo in the offer price
- If the resource's true, desired (and competitive) price is $>$ DDBT but less than $(\text{DDBT} + \text{"x"})$, the rational action is to not bid the competitive price, and instead bid the $(\text{DDBT} - 1\text{¢})$
 - Resource owner has to hope that his offer to exit at $\text{DDBT} - 1\text{¢}$ clears. *If it doesn't, the resource is stuck with a CSO at a price it didn't want.*

RESULT 2: THE IMM AND THE MARKET NEVER SEE THE TRUE COMPETITIVE OFFER, THE RESOURCE MAY TAKE ON A CSO IT DOESN'T WANT, AND THE FCM MAY CLEAR AT AN UNCOMPETITIVE LEVEL.

Solution

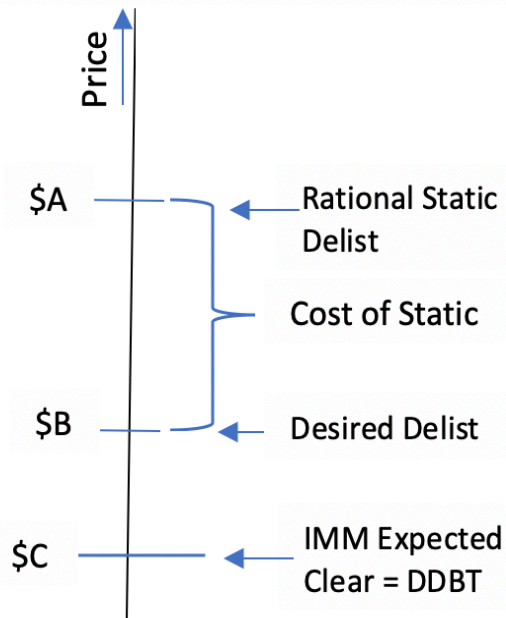
Set the DDBT at IMM estimate of Clearing Price + “x”

What is the right value of “x?”

- \$0.50 to \$1.00 seems reasonable given past experience.
- ISO analysis of new DDBT method’s accuracy (August MC, Slide 12), indicated that it misses the actual (historic) clearing price by 25%. *With a \$2 clear, that 25% margin is 50 cents; with a \$4 clear, it is \$1.00.* A margin of this size would help address this inaccuracy.
- The last four FCAs, all of which were certified as competitive, had an average clearing price of \$0.98 below the DDBT.
- Alternately the IMM could review all static delists submitted since FCA-1, compare them to the DDBT in place at the time, and pick a reasonable confidence interval – say 90% of all statics were $> \text{“DDBT + x”}$ and solve for “x.”

Graphic Example

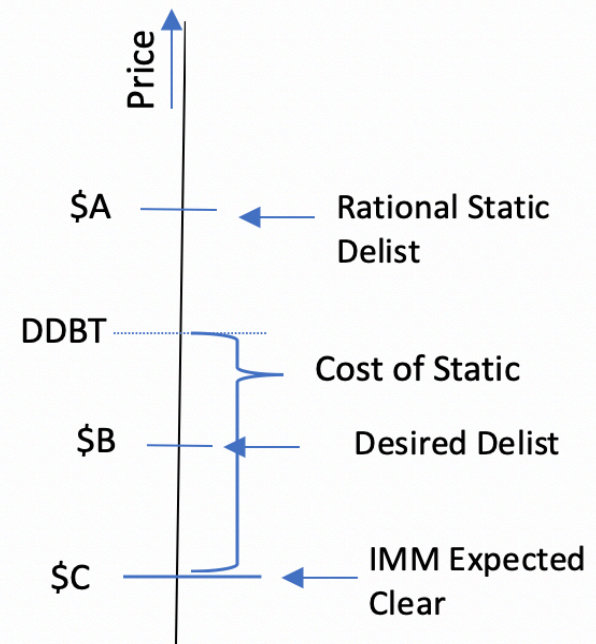
ISO Original Proposal



Result: Resource either

- **Statically delists at \$A or**
- **Dynamically delists at \$C and *hopes* it doesn't get a CSO**

Proposed Modification



Result: Resource delists at its cost (\$B)

Issues Raised at Prior MC

Doesn't a bandwidth just move the problem to a different price?

- **If the IMM expected clear is \$2, and bandwidth is \$0.75, what about the resource that wants to offer \$2.80?**

A: We have the same issue with use of any bandwidth, yet that doesn't mean we don't use them:

- **Mitigation, DDP, NCPC, compliance, etc.**
- ***In this case, it's even less of a concern:***
 - **Point is we want an efficient, competitive price**
 - **Assuming IMM's new model is an accurate predictor of clearing, it is much more likely that a competitive clear is close to this value (say \$2 to \$2.75) than it is further away ($> \$2.75$).**
 - **So while the \$2.75 resource may be annoyed to have to submit a static, the "stickiness" of its static delist bid is less likely to bias overall market outcomes.**

Does a bandwidth offer other advantages?

Yes it does. Consider:

- **Reliability rejections. Any delist rejected for reliability suppresses prices (considered price-taker)**
 - This is, unfortunately, very common – 8 of 14 FCAs
- **BTM solar and other DG resources are reducing NICR, but from outside the market (therefore without the same obligations and penalties for failing to perform as resources inside the market, with a CSO)**

These items are potentially biasing clearing prices below competitive levels. Adding a DDBT bandwidth may help reduce, or at least not exacerbate, these concerns.

Other Solutions

Convert the October “lock-in” from a price-certain to an offer cap.

- **Resource owner could delist, *in the auction*, at any price up to the approved price that comes out of the workbook process.**
- **May have some auction software complications; needs input from ISO.**
- **Only solves part of the problem – the risk of the lock-in timing. Other “stickiness” concerns discussed earlier would remain. But the timing is a big part of the problem, so it would still be very helpful.**