

To: NEPOOL Markets Committee
From: Internal Market Monitor (IMM)
Date: April 24, 2023
Subject: LS Power's Repowering Proposal

In this memo, the IMM offers its initial assessment of LS Power's proposed rules to allow a repowering resource to revert to its original existing resource status. While we understand the time constraints faced by LS Power that have resulted in an expedited stakeholder review process, such a proposed rule change requires a thorough assessment of all the associated issues, which is simply not practical in this timeframe. However, we offer these initial thoughts to assist stakeholders with their review of the proposal and will be available to discuss this memo at the upcoming NEPOOL Markets Committee meeting.

Background

LS Power is proposing changes to Section 13 of Market Rule 1 of the ISO New England Tariff ("Tariff") as a way to remove its obligation to repower the Ocean State Power 2 Resource ("OSP2"), a 270 MW facility that cleared as part of a New Generating Capacity Resource in Forward Capacity Auction 15 ("FCA 15").

In FCA 15, LS Power proposed repowering OSP2 with an additional 64 MW, or more than a 20% incremental output. Under Tariff Section III.13.1.1.1.2(a), the repowering proposal allowed the 270 MW Resource that was previously counted as capacity to participate in FCA 15 as a New Generating Capacity Resource, which cleared a total of 334 MW (270 MW plus 64 MW of repowering) of capacity at the clearing price of \$3.98 kW/mo for the associated Capacity Commitment Period (i.e., June 2024 to May 2025).¹ In turn, under Tariff Section III.13.2.3.2(e), because a portion of the New Generating Capacity Resource (in fact, all 334 MW) cleared in the FCA, the former "associated Existing Generating Capacity Resource" must be "permanently de-listed as of the start of associated Capacity Commitment Period" to avoid double counting of capacity.² In addition, LS Power elected the 7-year rate lock that was available under the Tariff at the time, whereby the New Generating Capacity Resource would receive the fixed

¹Tariff Section III.13.1.1.1.2(a) provides in relevant part: "When investment in the resource will result, by the commencement of the Capacity Commitment Period, in an increase in output by an amount exceeding . . . 20% of the summer Qualified Capacity" ... "the whole resource shall participate in the Forward Capacity Auction as a New Generating Capacity Resource." (emphasis added)

² Tariff Section III.13.2.3.2.(e) provides in relevant part: "If any portion of the New Generating Capacity Resource clears in the Forward Capacity Auction, the associated Existing Generating Capacity Resource shall be permanently de-listed as of the start of the associated Capacity Commitment Period." This provision ensures that the previously counted as capacity that clears as "new" is not double counted.

capacity payment of \$3.98 kW/mo for the next six FCAs (regardless of clearing price) for the associated Capacity Commitment Periods.

LS Power has announced that it would like not to invest in the repowering of the cleared New Generating Capacity Resource and to “revert back” to the original 270 MW Resource. LS Power asserts that the ISO has responded that a repowering project must either be: (a) completed as originally contemplated in its Show of Interest; or (b) terminated in its totality, which would result in the loss of the whole plant’s ability to participate in the Forward Capacity Market (FCM) in perpetuity (forfeit of Capacity Network Resource Capability) and forfeit of Financial Assurance (FA), including that associated with MWs which are currently operational. In response, LS Power has proposed Tariff revisions that would allow them not to go forward with the repowering obligation while retaining FCM-eligibility on the currently operating facility, ranging from revisions to commercialization rules to a partial forfeiture of FA and partial forfeiture of its 7-year rate lock. LS Power has also asked for expedited vote on this issue as it is in the process of determining if they are going to move forward with this project or not.

IMM Assessment of Current Tariff Provisions

The IMM’s view is that once the combined repowered resource (334 MW) cleared FCA 15 as a “New Generating Capacity Resource,” its entire capacity then became subject to the critical path schedule (CPS) monitoring and termination provisions that apply to a new resource. This includes the possibility of the ISO exercising its right to seek termination in the event of LS Power’s non-performance of the repowering obligation, which is ultimately subject to the Commission’s approval and determination.³ The Tariff also provides, “upon Commission ruling, the Project Sponsor shall forfeit any financial assurance provided with respect to that Capacity Supply Obligation.”⁴

IMM Initial Assessment of Design Proposal

The IMM is sympathetic to the situation LS Power is in and to the fact that circumstances can change and impact a Participant’s business decisions. We do think taking a fresh look at the repowering rules in the Tariff is a good idea, but we have a number of concerns with the proposed rule changes and the short evaluation timeframe. In summary, the evaluation will need to assess incentives to limit the exercise of market power and gaming, and provide a clear and commensurate remedy if a participant is unable to perform on its repowering obligation.

³See Tariff Sections III.13.2.3.2(e) and III.13.3.4A. Under Tariff Section III.13.3.4A, if a Project Sponsor fails to comply with CPS monitoring Tariff provisions, then the ISO “shall have the right, through filing with the Commission, to terminate the resource’s [CSO] for any future Capacity Commitment Periods and the resource’s right to any payments associated with that [CSO] in the Capacity Commitment Period, and to adjust the resource’s qualified capacity for participation in the Forward Capacity Market.”

⁴Tariff Section III.13.3.4A. In practice, a range of remedies could be available in the event that LS Power does not perform on its repowering obligation — from being compelled to strictly perform, to paying monetary damages and a penalty, to an outright termination of eligibility to participate in the capacity market — all of which remain subject to the approval and determination of the Commission.

First, this design change is being brought through the stakeholder process in an expedited way, which does not allow for a comprehensive review of the impacts of the change. Design changes need to be vetted to ensure they do not create other issues down the road (unintended consequences). Under the IMM business process, we review rule changes for how they enhance the function of the market as well as ensuring market power concerns are appropriately addressed. This review is an iterative process and not something that can be sufficiently completed in this expedited time frame.

Second, an assessment of market power or gaming issues needs to be completed. A fundamental design intent of the repowering provisions was to provide a means of securing capacity revenue certainty, for the *entire* capacity of the resource for a multi-year period, in order to underpin significant investment to maintain operation or to increase the capability of the resource. Once cleared as a new capacity resource, there is no Tariff means of reverting to the original resource. While this, on the face of it, is very restrictive, it was intended to act as a strong deterrent to potentially setting a higher clearing price and securing a multi-year revenue stream, and subsequently toggling back to the original status.

In the context of this proposal, the elimination of the multi-year price lock helps attenuate market power concerns by limiting the payoff of a successful withholding strategy. There are also market power mitigation protections already in the Tariff that apply to the existing resource, namely the review of a Static De-List Bid. However, while existing resources are reviewed for seller-side market power (inflated bids are subject to downward IMM adjustment), there is no such review of new supply offers, which are subject to buyer-side market power review (upward adjustment) only. This allows the new resource to be offered as high as the auction starting price down to its offer floor price. Therefore, there is still an open question of whether this proposal increases the opportunity for exercising market power or gaming, which tends to be a greater concern when capacity conditions are tighter (for example, than conditions in FCA 15).

Third, the IMM is concerned that the proposed changes create an ability for a participant to “unwind” its repowering obligation (and rate lock election) retroactively, with limited consequences for essentially breaching that obligation. This proposal does not factor in the potential market harm caused by the clearing of the repowering resource in the FCA, and may not adequately incentivize Market Participants to deliver on obligations obtained in the auction.

In short, the capacity market, and all of the rules around CPS monitoring, Financial Assurance and commercialization need careful monitoring to ensure participants that take on obligations in the FCM will face strong incentives to deliver on those obligations.