

154 FERC ¶ 61,005
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Norman C. Bay, Chairman;
Cheryl A. LaFleur, Tony Clark,
and Colette D. Honorable.

Exelon Corporation and
Calpine Corporation

Docket No. EL15-23-001

v.

ISO New England Inc.

ORDER DENYING REHEARING

(Issued January 7, 2016)

1. By order issued January 30, 2015,¹ the Commission denied Exelon Corporation and Calpine Corporation's (Complainants) complaint against ISO New England Inc. (ISO-NE), filed pursuant to sections 206 and 306 of the Federal Power Act (FPA),² which alleged that certain provisions of ISO-NE's Transmission, Markets and Services Tariff (Tariff) relevant to the Forward Capacity Market (FCM) were unjust, unreasonable, and unduly discriminatory.³ Specifically, Complainants challenged the Tariff provisions that require new entrants electing to "lock-in" the clearing price from the first Forward Capacity Auction (FCA) in which they clear to submit what are, in effect, zero-price offers into subsequent FCAs during the relevant lock-in period.

¹ *Exelon Corporation and Calpine Corporation v. ISO New England Inc.*, 150 FERC ¶ 61,067 (2015) (January 30, 2015 Order).

² 16 U.S.C. §§ 824(e), 825(e) (2012).

³ The FCM rules are set forth in section 13 of Market Rule 1 of ISO-NE's Tariff. Capitalized terms used but not defined herein are intended to have the meaning given to such terms in the Tariff.

Complainants seek rehearing of the January 30, 2015 Order. As discussed below, we deny rehearing.

I. Background

2. ISO-NE administers the FCM, in which eligible resources compete in annual FCAs, to provide capacity three years in advance of the relevant capacity commitment period. Although the FCA is intended to produce a single Capacity Clearing Price for all cleared resources, under certain conditions the prices paid to cleared resources may be administratively determined by ISO-NE and differ based on whether a resource is new or existing. ISO-NE's new entrant pricing provision (New Entrant Pricing or New Entrant Pricing Rule) allows a new entrant to lock in the first auction clearing price for up to six additional auctions in order to mitigate price risk. If a new resource elects New Entrant Pricing, the resource may not submit any type of de-list or export bid in subsequent FCAs for Capacity Commitment Periods for which the resource owner elected to have the New Entrant Pricing apply. In other words, in order to lock-in the first-year price, the Tariff requires that the capacity be offered as a price-taker (i.e., at a zero-price offer) in all future years for which it receives the first-year capacity price. Thus, FCM revenues for the new entrant are guaranteed during the lock-in period regardless of whether capacity clearing prices in subsequent auctions over that period exceed or fall short of the initial FCM clearing price.

3. In their November 26, 2014 Complaint, Complainants argued that the combination of the price lock-in and the zero-price offer requirement unreasonably and artificially suppresses capacity prices and results in undue discrimination because new entrants are paid higher prices than are paid to other resources for providing the same capacity services. They stated that the price lock-in suppresses the clearing price in the entry (i.e., year one) FCA because new entrants will offer at an artificially low price knowing that they will receive up to six additional installment payments in subsequent FCAs, and that the clearing price will continue to be suppressed in subsequent FCAs due to new entrants' submittal of zero-price offers. Complainants noted that they were not asking the Commission to eliminate the New Entrant Pricing lock-in, or to alter the treatment of new entrants, but rather to remedy the impacts of the resulting price suppression on other suppliers and the market.

4. Complainants further contended that the Commission's acceptance of the Tariff revisions without addressing the price-suppressing effect of the New Entry Pricing provision was inconsistent with the Commission's rejection of zero-price offers in the PJM Interconnection L.L.C. (PJM) market with respect to its New Entry Price Adjustment.⁴ Complainants stated that the differences between the PJM and ISO-NE

⁴ *PJM Interconnection, L.L.C.*, 128 FERC ¶ 61,157, at P 112 (2009) (PJM Order).

Tariffs that the Commission relied upon in an earlier proceeding to explain its approach are no longer valid due to changes to the ISO-NE capacity market, including the introduction of a sloped demand curve.⁵ At the same time, Complainants stated that there are two noteworthy differences between ISO-NE's New Entry Pricing rule and PJM's New Entry Price Adjustment. First, the lock-in period in ISO-NE's program is seven years, versus three years in PJM. Second, ISO-NE's lock-in option is generally available to any new entrant, while PJM's lock-in applies only in narrow circumstances and thus is rarely triggered. These differences, according to Complainants, result in greater price suppression under ISO-NE's New Entry Pricing Rule than under PJM's New Entry Price Adjustment mechanism.

5. Complainants requested that the Commission implement either an approach consistent with that taken in PJM, by requiring new entrants to submit offers higher than zero in subsequent auctions, or an alternative remedy such as offering some type of lock-in option to existing resources.

6. In the January 30, 2015 Order, the Commission denied the Complaint, finding that Complainants did not meet their burden under section 206 of the FPA to show that the challenged rules were unjust, unreasonable, and unduly discriminatory. The Commission reasoned that a resource whose construction has recently been completed and that has accepted a price lock-in typically has very low going-forward costs and would, if behaving competitively, submit an offer reflecting those costs. The Commission explained that by offering at a significantly higher price, a resource would risk not being selected when the market price exceeds the resource's incremental costs and the resource could have received a profit. Moreover, the Commission noted, by requiring locked-in resources to offer near their going-forward costs, the auction can select the set of resources with the lowest costs. Thus, the Commission concluded, it is efficient for such a resource to offer as a price-taker (effectively submitting a \$0 price offer), because it is efficient for such a resource to be selected in the auction over resources with higher going-forward costs.⁶

7. The January 30, 2015 Order noted that much of Complainants' arguments as to why ISO-NE's current Tariff is unjust and unreasonable focuses on the inconsistency between ISO-NE's requirement that a lock-in resource must offer as a price-taker and PJM's Commission-approved offer price requirements for lock-in resources. The Commission acknowledged that, in certain limited circumstances, PJM's New Entry

⁵ See *New England Power Generators Ass'n v. ISO New England Inc.*, 146 FERC ¶ 61,039, at P 58 (2014), *order denying rehearing and clarification*, 150 FERC ¶ 61,064 (2015).

⁶ January 30, 2015 Order, 150 FERC ¶ 61,067 at P 30.

Price Adjustment rules may result in higher prices paid to existing resources than under ISO-NE's zero-price offer requirement, but the Commission was not persuaded that this difference, in itself, rendered ISO-NE's rules unjust and unreasonable. Therefore, the Commission found that Complainants did not show that ISO-NE's zero-price offer requirement was unjust and unreasonable.⁷

II. Request for Rehearing

8. On rehearing, Complainants argue that, in finding that Complainants failed to satisfy their burden under FPA section 206, the Commission did not provide a reasoned basis for finding that there is no artificial price suppression in the post-entry FCAs and also failed to address the Complainants' arguments regarding artificial price suppression in the entry FCA.

9. With respect to the post-entry FCAs, Complainants argue that the Commission misunderstood and mischaracterized the Complaint. Complainants state that the Complaint addressed all capacity that is subject to the price lock-in and that must be offered into subsequent FCAs at a zero-price offer, not just how the portion of the resource's capacity that did not clear initially is treated in future auctions for purposes of determining the clearing price and total quantity of capacity procured, as stated in the January 30, 2015 Order.

10. Complainants also contend that the January 30, 2015 Order ignores the reason for the price-locked resource's low going forward costs, which, they assert, are a direct result of the New Entry Pricing Rule that provides price guarantees over the seven-year lock-in period. Complainants claim that such capacity would not have entered the market absent the New Entry Pricing Rule, noting that the Commission found, in approving the extension of the lock-in from five to seven years under the New Entry Pricing Rule, that the extension was necessary in light of the risk of lack of investment when new capacity is needed.

11. In support of their contention that the Commission failed to respond to their arguments regarding artificial price suppression in the entry FCA, Complainants state that the testimony of their witness, Mr. Schnitzer, explained that under the proposed New Entry Pricing rule, a new entrant will offer at an artificially low level knowing that it will receive up to six additional installment payments in the succeeding FCAs instead of being paid the entire amount in the first year. Complainants state that this view of price suppression in the entry FCA is consistent with the Commission's prior acknowledgement that extending the price lock-in period from five to seven years may result in lower market clearing prices. However, Complainants argue, this creates an

⁷ January 30, 2015 Order, 150 FERC ¶ 61,067 at P 31.

unduly discriminatory pricing scheme, where new entrants benefit from installment payments over the lock-in period while other suppliers do not receive any payment to make up for the lower price in the FCA in which the new entrants first cleared. Complainants' proposed solution is for existing suppliers in the entry FCA to receive an option for a similar installment payment.

12. In addition, Complainants state that the January 30, 2015 Order "completely ignores" statements in the Complaint asserting that the Capacity Carry Forward Rule will not provide a remedy for price suppression resulting from the zero-price offer requirement contained in the New Entry Pricing Rule because the Capacity Carry Forward Rule will not trigger in FCA 9 and will be eliminated in FCA 10, and thus questions about that rule's efficacy are moot.

13. Finally, Complainants argue that the January 30, 2015 Order is inconsistent with the PJM Order, and that the Commission failed to explain its departure from that precedent. Specifically, Complainants argue that the Commission found that PJM's proposal to allow zero-price offers from price-locked resources was not just and reasonable and was unduly discriminatory, while subsequently allowing the same rules to go into effect in ISO-NE.⁸ Complainants argue that the Commission cannot avoid its own precedent by stating that displacement of existing resources by price-locked resources offering as price-takers is an efficient result. Complainants state that although capacity price suppression lowers capacity procurement costs in the short run, such price suppression will raise prices and harm reliability in the long run, which the Commission has found in other proceedings. Complainants further state that there is no record evidence, analysis, or consideration of the long-term effects of such price suppression to support the Commission's conclusion. Complainants further state that the Commission failed to address their argument that the zero-price offer requirement in the New Entry Pricing Rule results in undue discrimination because it creates a two-tiered compensation system where existing resources receive the FCA clearing price while new entrants that lock-in their price receive guaranteed additional payments. Complainants argue that the Commission previously determined in PJM that a zero-price offer requirement would result in unduly discriminatory pricing because the new entrant would receive its first year price for all the locked-in years, while existing resources would receive a lower price.⁹ Complainants state that the Commission has departed from precedent that found existing and new resources are similarly situated with respect to capacity markets and should receive the same price.¹⁰

⁸ Request for Rehearing at 14-15 (citing PJM Order, 128 FERC ¶ 61,157 at P 112).

⁹ *Id.* at 19 (citing PJM Order, 128 FERC ¶ 61,157 at P 112).

¹⁰ *Id.* at 20 (citing PJM Order, 128 FERC ¶ 61,157 at P 102).

III. Discussion

14. As discussed below, we deny rehearing.

15. We disagree with Complainants' assertion that the Commission failed to provide a reasoned basis for finding that the New Entry Pricing Rule, coupled with the lock-in requirement, is just and reasonable and also failed to address the Complainants' arguments regarding artificial price suppression in the entry FCA. The January 30, 2015 Order found, and we affirm here, that a competitive resource would offer into the capacity market in years two through seven at its going-forward costs, and that a new generator typically would have low going-forward costs, approaching zero. As the Commission explained, the incremental costs for a newly-constructed resource are typically near zero because new resources need relatively little maintenance to satisfy their capacity obligations. By allowing sellers to reflect their going-forward costs in their offers, ISO-NE is able to select the most efficient (lowest cost) set of resources, because the low offer prices reflect low going-forward costs. These considerations support a conclusion that the zero-price offer requirement is just and reasonable.

16. With respect to Complainants' argument that the lock-in option suppresses clearing prices in the entry FCA, we acknowledge that the existence of the lock-in option may result in lower capacity clearing prices than might result absent that option.¹¹ But we disagree that this amounts to unreasonable price suppression or undue discrimination between new and existing resources. Rather, any lowering of the entry-FCA clearing prices is an acceptable byproduct of a just and reasonable market rule—i.e. ISO-NE's New Entrant Pricing Rule—that achieves particular and distinct objectives in the region. As the Commission stated when it accepted ISO-NE's proposal to extend the lock-in option from five years to seven years, the lock-in option strikes a reasonable balance between incenting new entry through greater investor assurance and protecting consumers from very high prices.¹² We therefore affirm our finding that ISO-NE's New Entrant Pricing Rule and associated mechanics remain just and reasonable.

¹¹ We note that while the Commission concedes the possibility that the lock-in option may result in lower capacity clearing prices in the entry FCA, capacity sell offers from new resources remain subject to ISO-NE's Commission-approved minimum offer price rule. Absent exemption or a display of going forward costs below defined Offer Review Trigger Prices (ORTP), new capacity sell offers are limited by the ORTPs, which the Commission has found to be a just and reasonable rate. *ISO New England Inc.*, 142 FERC ¶ 61,107 (2013).

¹² *ISO New England Inc.*, 147 FERC ¶ 61,173, at P 56 (2014).

17. We next turn to Complainants' assertion that the Commission inappropriately, and without explanation, departed from precedent by accepting ISO-NE's requirement that a resource that has elected to lock-in its clearing price for seven years must offer as a price-taker, given the Commission's rejection of a similar proposal in the PJM Order. As noted above, the January 30, 2015 Order recognized that this argument was central to Complainants' case, and acknowledged that, under certain limited circumstances, PJM's New Entry Price Adjustment rules may result in higher prices paid to existing resources than those under ISO-NE's zero-price offer requirement. The January 30 Order stated, however, that due to differing clearing mechanics, neither set of rules results in an inefficient selection of capacity, and therefore both can be just and reasonable.¹³

18. Complainants assert that the Commission's findings in the January 30, 2015 Order reflect a departure from the PJM Order. As the markets have evolved, so too has the Commission's opinion regarding whether zero-price offers from locked-in resources may be just and reasonable. Based on further consideration, the Commission has realized that a zero-price capacity offer from a new merchant resource that has cleared in at least one previous auction and has incurred construction costs can be a competitive offer that reflects the resource's going-forward costs, not an attempt to lower capacity market clearing prices. Once a new resource clears its initial capacity auction (and incurs significant costs to satisfy that capacity obligation), it has an incentive to ensure that it clears in subsequent auctions. A zero-price offer strategy is consistent with that incentive.

¹³ In PJM, a lock-in resource must offer its capacity in two subsequent auctions at the lesser of: (1) its initial sell offer; or (2) 0.9 times Net CONE in the Locational Delivery Area. Although the New Entry Price Adjustment rules guarantee revenues for such a resource for two subsequent years, the offer requirement could result in the resource clearing a smaller quantity than it cleared initially. If so, the New Entry Price Adjustment rules detail how the lock-in resource's capacity will be used to determine the capacity supply curve and market-clearing prices in the two subsequent auctions. Under New Entry Price Adjustment, the initial cleared lock-in quantity needed for reliability will be included in subsequent supply curves as an effective price taker. Additional lock-in capacity may clear under the offer requirement only if it is lower cost than other offered capacity resources. New Entry Price Adjustment rules support economic efficiency by ensuring that previously cleared lock-in capacity clears the auction, thus recognizing that load has already committed to purchase the lock-in capacity for the relevant delivery year, and any portion of the lock-in resource's capacity paid out-of-market is simply a byproduct of the design of PJM's New Entry Price Adjustment rules. *See* PJM OATT at Attachment DD, sections 5.14(c)(4), 5.14(c)(5)(ii) and 5.14(c)(5)(iii).

19. Moreover, we note that Complainants' requested relief—namely that ISO-NE enter lock-in resources into capacity auctions in years two through seven at higher prices and purchase uncleared capacity from those resources out-of-market—could have a significant cost impact on New England customers. The lock-in option is available to every new resource that clears an auction in ISO-NE. In a scenario where one or more new ISO-NE resources lock in their prices in year one, and auction clearing prices in subsequent years drop such that those resources do not clear at the year-one price, New England customers could incur significant costs to pay the lock-in resources out-of-market. For these reasons, we reject Complainants' arguments.

20. With respect to Complainants' argument that the Commission failed to address their argument that the Capacity Carry Forward Rule was an inadequate remedy to price suppression resulting from the zero-price offer requirement because the rule is now moot, we note that, contrary to Complainants' assertion, the Capacity Carry Forward Rule remains a part of the ISO-NE Tariff at this time. More importantly, as discussed above, we are denying the Complaint because our approach regarding zero-price offers has evolved, not because of the existence of this rule.

21. For the foregoing reasons, we will deny Complainants' rehearing request.

The Commission orders:

Complainants' request for rehearing of the January 30, 2015 Order is hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.