



# IESO Response to Issues Identified from Stakeholder Feedback

Day Ahead Commitment Process SE-7

Public

## **Stakeholder Issues/Concerns**

- 1. Offering Reliability Guarantees Every Day**
- 2. Change to Market Design or Philosophy**
- 3. Exports Not Included in Day Ahead Commitment Process (DACP)**
- 4. Inequities in Treatment Between Imports and Domestic Generation**
- 5. Price and Uplift Impacts**
- 6. Preferential Treatment of Energy Limited Resources**
- 7. DACP Timeline**
- 8. Potential for Gaming**

# 1. Offering Reliability Guarantees Everyday

IESO proposes that DACP reliability guarantees would be offered every day; from when DACP is implemented until it is proposed to expire (June 1 to November 30, 2006 or earlier).

## STATEMENTS OF STAKEHOLDER CONCERNS

- a) Offering day-ahead reliability guarantees everyday to imports will drive down real-time market prices, reduce domestic generation market share and result in reduced revenues for domestic generation.
- b) Day-ahead reliability guarantees are only needed on days when reliability is an issue. Reliability is not an issue every day so day-ahead reliability guarantees do not need to be offered every day. Day-ahead reliability guarantees should only be offered for days when reliability is an issue e.g. hot weather, high demand.
- c) History, even the summer of 2005, has shown that the market can usually address real-time reliability issues, even on days that are forecast day-ahead to have reliability problems.

## IESO RESPONSE

- i) DACP is designed to encourage imports to Ontario to be more secure in the source market, by encouraging importers to participate in other markets' day-ahead processes. In New York's case, bids in that market close at 5 a.m. the day ahead. For Traders to know whether to participate in that market, they must know if the DACP is "on", at least two days in advance. This presents too lengthy a window for reliability problems to surface.
- ii) Reliability issues in real-time are often not foreseeable days ahead. There is always a greater risk that import transactions scheduled in real-time will fail or be curtailed in real-time relative to transactions committed and scheduled day-ahead. Such occurrences will place Ontario in the situation it experienced far too often in the summer of 2005: the sudden loss of a large amount of expected supply. To mitigate that risk, day-ahead commitments and reliability guarantees should be offered every day. Providing reliability guarantees to imports every day reduces the risk and exposure to such reliability issues.
- iii) Offering day-ahead commitments and reliability guarantees every day will avoid the possibility of "on again/off again fatigue" on prospective importers.
- iv) Market price reductions would only occur if the DACP results in more imports to Ontario than would occur under the current market mechanisms. This could occur for two reasons. The first is that the DACP attracts more economic import transactions relative to existing market mechanisms and such a result would be an improvement in market efficiency. The second reason is poor day-ahead forecasting of real-time conditions by the IESO (e.g. load forecast inaccuracy), or others (e.g. self-scheduling or intermittent generators forecasts of their outputs).
- v) Impacts on market prices and domestic generation would be part of the review of the DACP in the fall of 2006.

## **HOW THE IESO PROPOSAL ADDRESSES THIS CONCERN**

- 1) IESO will implement performance measures to report on the accuracy of day-ahead load forecasts used in the DACP, to drive as accurate forecasting as possible, and thereby minimize occurrences of over commitment to imports.
- 2) IESO will track other inputs to DACP (e.g. forecasts of self-scheduling, intermittent or TSG generation) to drive as accurate inputs as possible, and will consider adjusting inputs for any regular and consistent biases.
- 3) IESO recommends a sunset for the DACP, at which time IESO Board will reconsider the need for DACP.

## **2. Change to Market Design and Philosophy**

### **STATEMENTS OF STAKEHOLDER CONCERNS**

- a) DACP represents a fundamental shift from the original market design philosophy of relying on market drivers to address reliability.
- b) DACP is another “command and control” measure by the IESO that undermines the IAM.
- c) IESO interventions in DACP will be meddling in the market and result in distorting market outcomes and prices.
- d) IESO interventions in the DACP must be limited and defined.

### **IESO RESPONSE**

- i) DACP uses existing market mechanisms and drivers (pre-dispatch economic evaluation of MP submitted offers and bids) to the extent possible to determine which resources get scheduled, and hence receive commitments and guarantees.
- ii) IESO interventions in the DACP are only taken if reliability would be otherwise at risk and are only necessary because the existing pre-dispatch mechanism cannot optimise resources over a 24-hour period and cannot reflect the operational capabilities of some resources.
- iii) IESO intervention in DACP will be transparent as (i) intervention will be limited to situations where reliability would otherwise be at risk, and, (ii) the IESO would be obligated to report to the market on when and to what extent it has intervened.
- iv) IESO believes a day-ahead market with 24-hour optimization is a better means of scheduling & committing resources day-ahead. It would eliminate the need for the IESO interventions necessary under the DACP. However, a day-ahead market cannot be developed and implemented by the summer of 2006.
- v) IESO sees DACP as a temporary measure and is proposing a sunset time for the DACP. The IESO also will be initiating stakeholder discussions of a day-ahead market in early 2006.

## **HOW THE IESO PROPOSAL ADDRESSES THIS CONCERN**

- 1) IESO will only intervene in commitment decisions if reliability is otherwise at risk.
- 2) IESO decisions must be agreed to by the specifically-affected market participants.
- 3) IESO will report all commitment decisions sought by IESO to maintain reliability.
- 4) IESO will re-initiate stakeholder discussion about a Day-Ahead Market design as soon as possible.
- 5) IESO will pursue resolution to key market pricing issues that currently inhibit responsiveness of flexible resources to market signals.
- 6) IESO recommends a sunset for the DACP, at which time IESO Board will reconsider the need for DACP.

## **3. Exports not Included in DACP**

The DACP does not permit or consider any export transactions. The DACP does not provide any commitments or guarantees to export transactions, or even take likely export volumes into account when committing supply.

### **STATEMENTS OF STAKEHOLDER CONCERNS**

- a) During the summer of 2005, the IESO presumably had to repeatedly rely upon resources committed by its neighbours to keep the lights on in Ontario. Now, Ontario is proposing not to return the favour. The IESO is strongly urged to consider exports bids in the day ahead commitment process.
- b) The proposed real-time penalties/charges for intertie transaction failures will reduce incentives for import and export trade for Ontario. The DACP, with its Import Offer Guarantees, provides an incentive for import transactions, but offers nothing for export transactions. The net result would be less export transactions and fewer customers for domestic generation.
- c) The DACP should at least include export volumes as this would result in more complete commitment of supply resources.
- d) Scheduling and committing exports in DACP will improve regional reliability.

### **IESO RESPONSE**

- i) The IESO and the working group were unable to identify a means of including exports, either as forecasted bulk volumes or individual transactions, that did not either:
  - Require significant administrative measures to ensure exports included and/or committed day-ahead did not result in over-committing supply with the cost of the corresponding reliability guarantees borne by Ontario customers; or
  - Require a complex market mechanism to allow committed exports to buy-out of their day-ahead position when real-time conditions warranted. Such a market mechanism is a typical feature of a day-ahead.

- ii) IESO agrees that including exports (either as forecasted bulk volumes or individual transaction commitments) would result in better day-ahead supply commitments. This issue is still being discussed with stakeholders to try and arrive at an acceptable process.
- iii) If a viable solution as to how to incorporate exports into the DACP by next summer is not available, the process will continue as currently designed. While the Program will not permit resource commitment for exports directly, the increased reliability of imports to Ontario should have an ancillary benefit of providing more stable exports as well.
- iv) A stakeholder engagement process is starting, to align penalties and charges applied to transaction failures in both the real-time environment and the DACP. This process will, among other things, address imbalances between import and export treatments.

#### **HOW THE IESO PROPOSAL ADDRESSES THIS CONCERN**

- 1) IESO continues to discuss possibility of incorporating exports into the DACP, but this cannot hold up the effort necessary to get the balance of the DACP in place by summer, 2006.
- 2) IESO will re-initiate stakeholder discussion about a Day-Ahead Market design as soon as possible.
- 3) IESO recommends a sunset for the DACP, at which time IESO Board will reconsider the need for DACP.

## **4. Inequities in Treatment Between Imports and Domestic Generation**

The DACP provides financial guarantees to imports for the full volume successfully scheduled in the process with the nature of the guarantee being that the import will earn at least its offer price. In contrast, Ontario generators receive guarantees from the DACP that guarantee recovery of incremental costs associated with minimum output over minimum run time.

#### **STATEMENTS OF STAKEHOLDER CONCERNS**

- a) Generators are disadvantaged: Imports appear to have a better reliability guarantee than do Ontario generators. Guarantees offered to imports are based on a return of at least offer prices over the full quantity scheduled in the DACP, which implies a fixed cost and/or profit component with no risk of the volume being subject to dispatch. Guarantees offered to domestic generation are based on submitted incremental fuel and OM&A costs for their minimum operation, in other words, costs only, with no similar ability to lock in profit. Further, domestic generators are still exposed to the decisions of the dispatch algorithm in real time and end up having very little assurances from the DACP. Domestic generators should be offered reliability guarantees on the basis of their day-ahead price or offer price and the volume scheduled in the DACP.
- b) Importers are disadvantaged: The DACP proposes a charge on day-ahead committed imports for failure to flow in real-time. There is no similar penalty for generators failing to meet day-ahead commitment in real-time.

## **IESO RESPONSE**

- i) Imports, whether committed day-ahead or in real-time, face a risk that domestic generators do not. That risk is that, unlike Ontario generators, the imports can only be scheduled for a constant quantity over any hour, and cannot be dispatched up or down in real-time even if the price falls below their offer price. This lack of flexibility in dispatch is the justification for the import offer guarantee both in real-time and day-ahead. Since Ontario generators' dispatch signals will lower output if and when their bid prices are not economic, there is no need to have loads pay Ontario generators a similar guarantee.
- ii) The IESO-administered market is built upon the premise that Ontario generation can be dispatched on a 5-minute basis, and is the fundamental tool in balancing real-time supply and demand. Hence, as the market is currently designed, Ontario dispatchable generators cannot be provided the same volumetric certainty over an hour as is an import.
- iii) Without an Ontario "competitive buy side" in day-ahead timeframe, there is no commercial counter-party willing to take a position that would permit generators to be held whole to a day-ahead price. The only current alternative would be that Ontario non-dispatchable load (load that is not able to make day-ahead decisions) would be counter-party to the risk between day-ahead price and real-time price for all domestic generation. Bearing such a risk is not appropriate as the vast majority of Ontario load cannot manage that risk. Bearing this risk for imports is judged both necessary and acceptable; necessary to attract imports to Ontario, and acceptable because of the volume of imports is limited by the physical size of the connections between Ontario and neighbouring markets; with a similar risk already being borne by Ontario load through the current real-time IOG.
- iv) The difference in penalties for not meeting day-ahead commitments in real-time is recognition of the difference in guarantees. In other words: imports get a greater guarantee with a charge for non-performance while a domestic generator gets a lesser guarantee with no such charge.

## **HOW THE IESO PROPOSAL ADDRESSES THIS CONCERN**

- 1) IESO will re-initiate stakeholder discussion about a Day-Ahead Market design as soon as possible.

# **5. Price and Uplift Impacts**

## **STATEMENT OF STAKEHOLDER CONCERNS**

- a) DACP will exert downward pressure on prices and upward pressure on uplifts. These impacts must be quantified and understood before DACP proceeds.

## **IESO RESPONSE**

- i) While simulation of price impacts of moving to the DACP is not possible, the IESO believes that, directionally, there will be downward pressure on market prices and upward pressure on uplifts. The IESO has prepared a preliminary assessment of price and uplift impacts and that is under a separate tab in this material.

## HOW THE IESO PROPOSAL ADDRESSES THIS CONCERN

- 1) The IESO commits to a review of actual price and uplift impacts as part of the review of DACP in the fall of 2006.
- 2) IESO recommends a sunset for the DACP, at which time IESO Board will reconsider the need for DACP.
- 3) IESO will re-initiate stakeholder discussion about a Day-Ahead Market design as soon as possible.

## 6. Preferential Treatment of Energy Limited Resources

Energy limited resources (ELR) are generation resources that have a limit as to how much energy they can produce over the dispatch day. This limit may be the result of fuel restrictions (e.g. water available in a reservoir of a hydroelectric facility) or environmental restrictions that limit the amount of energy that can be produced. A non-ELR is only limited by the capacity of the facility and could theoretically produce energy at full capacity for 24 hours.

The DACP requires energy limited resources to identify their daily energy limit so that these resources are not scheduled by the pre-dispatch engine to produce energy above that limit. The pre-dispatch would then schedule these resources in the first available hours of the day that these resources are economic.

The DACP allows only energy limited resources to revise their offers after the first two runs of the pre-dispatch schedule during the DACP in order to try to solve reliability problems identified in those first two pre-dispatch schedule runs. No other resources are allowed to revise their bids or offers during the DACP.

### STATEMENT OF STAKEHOLDER CONCERNS

Why are energy-limited resources given the opportunity to change offers during the DACP? Specifically, why are ELRs allowed to change offer data during the DACP and allowed to solve reliability problems? Couldn't/shouldn't the IESO also allow other resources to change dispatch data to resolve resource shortfalls?

### IESO RESPONSE

- i) Non-ELR resources would be scheduled economically by the pre-dispatch scheduler in any and all hours of the day for which the participant has indicated a desire to operate. The pre-dispatch scheduler, because of its hourly myopic optimization, cannot determine the most economic period to utilize ELR resources across the day. Participants with ELR are allowed to change their offers so that the market, rather than the IESO, can address identified reliability issues. In other words, the pre-dispatch engine will automatically solve reliability problems using non-ELR resources in hours that the participant has indicated a willingness to be available.
- ii) Allowing non-ELR resources to also change their offers would result potentially in a constantly moving reliability issue that the market could never catch. The end result of this could be more IESO intervention to address reliability problems.

## **HOW THE IESO PROPOSAL ADDRESSES THIS CONCERN**

- 1) ELRs are only permitted to change their offers after the first two of the four pre-schedule runs during the DACP.
- 2) After the DACP is completed, all participants can change their offers and bids as they see fit within the existing market rule requirements and in recognition of any applicable day-ahead commitments.

## **7. DACP Timeline**

### **STATEMENTS OF STAKEHOLDER CONCERNS**

- a) Concern that the DACP concludes at 15:00, and that a gas fired generator needs to complete their gas nominations before 12:00. The DACP should conclude earlier, or alternately could the IESO offer reliability guarantees based on earlier pre-dispatch iterations.
- b) Concern that the DACP concludes too early to be able to reflect current day operations in the availability of energy limited resources for the next day.

### **IESO RESPONSE**

- i) The proposed timeline was discussed extensively by the Working Group. For every reason for concluding the DACP earlier there was a reason for concluding it later. The proposed timeline is a compromise between the impact on gas markets, neighbouring electricity markets and existing market system capability.
- ii) The proposed timeline with reliability guarantees provided by 15:00 hours provides greater certainty than today's market, for a gas fired generator to fine tune their supply.
- iii) The DACP will not provide full volumetric commitment that could be available through a full-featured Day-Ahead Market. Rather, it will only give assurances of cost recovery for minimum output operation.
- iv) The proposed timeline permits existing processes and systems to be used for the DACP.

## **HOW THE IESO PROPOSAL ADDRESSES THIS CONCERN**

- 1) The proposal balances diverse scheduling needs and provides more certainty than today's market.
- 2) IESO will re-initiate stakeholder discussion about a Day-Ahead Market design as soon as possible.

## **8. Potential for Gaming**

### **STATEMENT OF STAKEHOLDER CONCERNS**

- a) There is concern that the lack of firm commitments on generators to actually make themselves available and generate in a manner that is consistent with the outcome of the DACP can create opportunities that are clearly advantageous to Ontario generators over day-ahead imports.

## **IESO RESPONSE**

- i) The DACP (and indeed the entire IESO-administered market) is built on the premise of the submission of reasonable data by market participants. The IESO Market Assessment Unit (MAU) will continue monitoring of the market on behalf of the Market Surveillance Panel as it does now; in other words, reviewing market outcomes to identify inappropriate or anomalous conduct, such as abuses of market power or gaming. As long as market participants continue to demonstrate competitive behaviours the MAU does not expect market surveillance will be any more intrusive than it is now. In regards to the DACP, bidding behaviour that is consistent between the DACP and the real-time market, or changes that can reasonably be explained, is the sort of expected behaviour that will be observed by the MAU on a regular basis.