

In determining the size that triggers generation market power concerns, the SMA establishes a threshold based on whether an applicant is pivotal in the market, *i.e.*, whether at least some of the applicant's capacity must be used to meet the market's peak demand. An applicant will be pivotal if its capacity exceeds the market's surplus of capacity above peak demand—that is, the market's supply margin. Thus, an applicant will fail the SMA screen if the amount of its capacity exceeds the market's supply margin.

In applying the SMA screen, the control area market where the applicant is located is first considered. Next, the markets directly interconnected to the applicant's control area market are considered. An applicant will pass the screen if it or its affiliates own or control an amount of generation located in a control area which is less than the supply margin (generation in excess of load) in the control area. The margin will include the amount of generation that can be imported into the control area limited by the total transfer capability (TTC) of the transmission system (*i.e.*, the lesser of uncommitted generation capacity or TTC).<sup>4</sup> Under the Commission's current policy, market-based rate applicants are allowed to sell at market-based rates into any control area where they pass the screen.

All sales, including bilateral sales, into an ISO or RTO with Commission-approved market monitoring and mitigation (PJM, ISO-NE, NYISO, and CAISO) are currently exempt from the SMA and, instead, are governed by the specific thresholds and mitigation provisions approved for the particular markets. At the technical conference, Staff invites comments on whether this exemption should be continued.

#### *Mitigation for Those Failing the SMA Screen*

In the SMA Order, the Commission stated that the primary tools for exercising generation market power are physical and economic withholding. To prevent physical withholding, the Commission required that an applicant who fails the SMA screen offer uncommitted capacity (*i.e.*, generation in excess of each hourly projected peak load and minimum required operating reserves) for spot market sales in the relevant market. To prevent economic withholding, this uncommitted capacity would be priced using a split-the-savings formula.<sup>5</sup> The Commission required that an applicant implement split-

the-savings pricing for spot market sales and purchases.<sup>6</sup>

The Commission reasoned that applying mitigation to spot market transactions will also result in mitigation of generation market power in longer term (forward) markets by creating a kind of competitive "standard offer" service for customers. If sellers attempt to charge excessive, non-competitive prices in forward markets, customers can avoid them by waiting to purchase in the real-time market. This puts market pressure on sellers to offer competitive prices in the forward markets. And when sellers offer competitive forward prices, many buyers will prefer to purchase in the forward markets in order to gain price certainty. Staff invites comments on the reasonableness of this assumption at the conference.

In the SMA Order, the Commission also imposed additional mitigation on applicants failing the screen. The Commission established mitigation for the size of a pivotal supplier (the Commission required that when a transmission provider performs a study pursuant to a request for interconnection, an unaffiliated entity may request that the output of its proposed project be modeled for study purposes to serve load within the control area in which it is located, without having to formally designate a particular load or without having to be selected as a designated network resource at the time of interconnection). In addition, to address concerns regarding residual transmission market power, the Commission required that the parties to the SMA Order employ an independent third party to operate and administer their OASIS sites. (*See* 97 FERC at 61,973).

#### **II. Possible Revisions to the SMA Screen**

Many commenters were critical of the SMA screen. In particular, some commenters claimed that the SMA screen overstates the amount of an applicant's capacity that is available to the wholesale market by including capacity committed to serve native load and pre-existing contract obligations as well as operating reserves set aside to meet regional reliability requirements. Other commenters raised concerns on the use of TTCs to determine import capability, since they claimed that TTCs may overstate transmission availability, thereby overstating the size of the geographic market to the benefit of market-based rate applicants. Some commenters objected that the SMA passes/fails applicants by using a bright-line standard which is overly narrow because it evaluates one hour's supply and demand, thereby neglecting to recognize non-peak generation market power or the lack thereof.

In response to these comments, Staff has identified for purposes of discussion at the technical conference two general methodologies for assessing generation market power that would constitute modifications to the interim SMA screen as announced in the SMA Order: Pivotal Supplier and Market Share.<sup>7</sup> Among the

improvements Staff recommends are that the interim screen should recognize planned generation outages when calculating capacity under the pivotal supplier and market share models discussed below. In addition, Staff recommends that State and Regional Reliability Council operating requirements for reliability (*i.e.*, operating reserves) should be used when calculating capacity in both the pivotal supply and market share screens discussed below.

Staff continues to propose the use of TTCs in applying the interim SMA screen. However, Staff seeks comment on viable alternatives (*i.e.*, flexibility to consider historical firm transactions, losses, and transmission reserve margins affecting available transfer capability). In particular, Staff seeks comment on how much transmission capacity should be included in the analysis where transmission providers (whose control over transmission has not been transferred to an RTO or ISO) calculate the capacity and also participate in generation markets. There are also transmission and other operating constraints inside the control area being evaluated, such that some generators are not able to run to their maximum rated capacity. What percent of these generators' capacity should be included as participating in the market?

Also, to address the commenters' concerns as to the SMA's over reliance on system peak data, options discussed below propose to measure generation market power on a monthly basis. However, Staff solicits the input of technical conference participants as to how the Commission can obtain the data to make such monthly measurements practicable. Migrating to a monthly measurement using the proposed models will require collecting applicant and relevant control area supply and demand monthly information. Monthly data for the supply and the demand for control areas and applicants cannot presently be gathered from a single source. Although supply data could be obtained from the FERC Form No. 714, private or industry data services, and OASIS information, and demand data obtained from the FERC Form No. 714 and FERC Form No. 1, Staff would appreciate suggestions as to what current reporting requirements exist that include necessary data and what reporting requirements may need to be expanded to collect the data, if a monthly measurement is ultimately adopted.

In addition, some commenters contended that the SMA Order was flawed because it lacked clarity and explanation when defining the data that would be used. In response, Staff has developed definitions for the data used in the interim generation market power screens discussed below. These definitions are set forth in Appendix A and Staff seeks comment on the clarity and accuracy of these definitions.

below), Staff is not focusing on them at this time because of the intensive data requirements associated with these screens that would make them burdensome and costly for many applicants, and would be administratively difficult for Staff to review and perform in the 60-day statutory time period.

<sup>4</sup> As the Commission explained in the SMA Order, the total amount of TTC is used as only a point of reference to establish the maximum amount of uncommitted generation supply, even though this amount of generation could not be simultaneously imported into an applicant's control area. The Commission stated in the SMA Order that intervenors will be allowed to present arguments on a case-by-case basis that another factor limiting import capability is appropriate, if warranted by the facts.

<sup>5</sup> A seller's incremental cost (the out-of-pocket cost of producing an additional MW) is compared with a buyer's decremental cost (the cost of not producing the last MW). The average of the incremental and decremental costs is the split-savings price. The details of how split-the-savings pricing was to be implemented are described in the SMA Order. *See* 97 FERC at 61,971–73.

<sup>6</sup> For purposes of this paper, spot market sales are intended to include only hourly transactions.

<sup>7</sup> Although several alternative screens were proposed by commenters (which are summarized