

The Work Group’s efforts are intended to assist RTO West in setting sound credit policy at the outset.

B. Overview and Discussion.

From a financial standpoint, providing transmission services in an open marketplace through an independent, nonprofit organization presents issues that previous transmission service models did not contemplate. The model for FERC’s pro forma Open Access Transmission Tariff (the “OATT”) was a single, vertically integrated utility with an obligation to wheel power across its system for third parties—to the extent there was available capacity—using its own generation resources to provide ancillary services. In contrast, RTO West will wheel power across facilities owned by multiple parties. For purposes of this paper, the RTO West filing utilities have assumed that RTO West will not be an integrated utility and therefore will have to provide ancillary services (particularly imbalance energy) through a market system of third-party bids. Like the transmission providers for which the OATT was designed, RTO West will be obligated to serve as transmission customers’ provider of last resort for ancillary services. Unlike those transmission providers, however, RTO West will have no resources of its own with which to fulfill this obligation.

When it comes to imbalance energy (supplying energy to meet deviations between scheduled deliveries and actual energy consumption), RTO West will depend on third parties to supply system needs and will also depend on third parties to pay for the supplies they require. As events in California have shown, an RTO or other transmission operator can, under adverse market conditions, rapidly find itself deeply in debt to energy suppliers, with few options to respond.

As the example calculations accompanying this overview illustrate,³ if even a small portion of the load using RTO West Transmission Facilities must be served through imbalance energy within a given time period, costs to purchasers can multiply with astounding speed. This is especially pronounced when high energy prices are combined with significant underscheduling of energy needed to serve loads. If the loads for which insufficient energy has been scheduled stay connected to the system, RTO West must cover the shortfall through imbalance-energy purchases. RTO West, as a nonprofit, involuntary “middle person” purchasing imbalance energy from suppliers, could quickly face insolvency if the parties to whom it supplies imbalance energy (likely to be the scheduling coordinator in most cases) cannot or do not settle their financial obligations quickly. High market prices for energy compound the problem severalfold.

Because of its status as provider of last resort, in cases of underscheduling RTO West could find itself with what amounts to a load service obligation without adequate tools to manage that obligation. RTO West will be at the mercy of a market it does not control and dependent on the load-serving scheduling coordinator to cover its imbalance-energy purchases. Meanwhile,

³ “Illustrative Examples of Price Exposure for Imbalance Energy—Various Load, Price, and Duration Assumptions,” attached as Attachment J-4.

assumption of responsibility for an RTO's insolvency (or imposition of unrecovered costs). For one thing, generators and transmission owners would not normally expect to be exposed to the consequences of defaults by parties with whom they do not do business. If the RTO becomes a mechanism for spreading costs of scheduling coordinator defaults to generators, transmission owners, and other scheduling coordinators (as has been the case in California, for instance), then the magnitude and unpredictability of the financial risks associated with market participation can increase exponentially.

There are three factors that cause an RTO's risks associated with imbalance energy to be of such great concern: (1) imbalance energy is used to make up the shortfall between the amount of energy that a scheduling coordinator or load-serving entity schedules and delivers to its customers and the amount of energy those customers actually consume, (2) an RTO may encounter significant impediments to terminating service to a defaulting scheduling coordinator, and (3) the price of energy used to provide imbalance energy is unpredictably volatile and subject to extreme and sustained price spikes. The third factor could cause even the most creditworthy counterparty to become uncreditworthy virtually overnight.

To deal with financial exposure from a defaulting scheduling coordinator, RTO West will need, at a minimum, the ability to disqualify the defaulting scheduling coordinator from further participation in the RTO West system. Even this remedy, however, will require a contingency plan to supply and schedule power to the customers of the disqualified scheduling coordinator. This means that someone must take on the financial and technical responsibility previously borne by the disqualified scheduling coordinator. There are essentially two options: (1) someone must guarantee the financial and scheduling obligations of the scheduling coordinator or (2) everyone using the RTO West system must share in the financial and scheduling burden created by the defaulting scheduling coordinator. The first option would require RTO West to identify, in advance, an entity that is willing to step in as the "backup" scheduling coordinator for customers whose scheduling coordinator has been disqualified. The second option, however, poses serious risks both to RTO West's solvency and to system stability. If no one is ready and willing to serve as backup scheduling coordinator for customers of disqualified scheduling coordinators, the only other recourse available is service termination.

For numerous regulatory, operational, and other reasons, RTO West may not be able to terminate service to a defaulting scheduling coordinator. From an operational standpoint, it may be impossible to isolate from the RTO West Transmission System the loads being served by a defaulting scheduling coordinator. Customer-specific transmission connections are likely to be the exception rather than the rule.

Even in those cases in which it might be technically feasible to terminate transmission deliveries, it may be inequitable. For example, it may be that the customers have paid their scheduling coordinator, but the scheduling coordinator has not paid RTO West. Interrupting power to end-use customers in those cases might be perceived as unfairly penalizing innocent parties.

Leaving aside fairness issues, disrupting power deliveries at the transmission-system level (as opposed to meter-by-meter at the distribution level) could have intolerable consequences with respect to health and safety risks and economic disruption. For example, a customer of a defaulting scheduling coordinator could be a municipal power system with thousands of residential, commercial, and industrial customers.

The infeasibility of service termination for nonpayment creates the problem of a quasi-load-service-obligation for RTO West. At the same time, it could expose RTO West, generators, and transmission owners to significant financial liability and increased rates for transmission services. In severe circumstances it could threaten RTO West's financial viability. For all these reasons, RTO West should take every step to discourage reliance on imbalance energy as a means to serve load. Such steps are critical to ensuring that RTO West markets will be robust enough to remain healthy even under stressful conditions.