7 Capacity Market Monitoring and Mitigation

This section addresses the mechanisms that the AESO is proposing to monitor and mitigate the exercise of market power

7.1 Mitigation of supply-side market power

7.1.1 The AESO's supply-side market power mitigation regime will include a must-offer requirement, a market power screen to identify firms that have the potential to profitably withhold capacity, a default offer price cap to restrict economic withholding by firms that fail the market power screen, and asset-specific offer price caps for mitigated qualified capacity assets with demonstrated net avoidable cost above the default offer price cap.

Must-offer requirement

7.1.2 A firm must offer the full UCAP from all qualified capacity assets into a capacity auction, as described in Section 5, *Base Auction* and Section 6, *Rebalancing Auctions*, subject to the delisting process described in Section 2, *Supply Participation*.

Market power screen

7.1.3 Before every base auction the AESO will:

(a) calculate and assign a UCAP for all prequalified capacity assets, as described in Section 3, *Calculation of Unforced Capacity Ratings*;

(b) conduct an *ex ante* market power screen to identify firms that have the potential to profitably exercise market power; and

(c) notify each firm that has failed the market power screen individually, before the commencement of the base auction.

7.1.4 The market power screen will not be applied to rebalancing auctions.

7.1.5 The market power screen will identify firms that have the ability to profitably increase the clearing price of an auction by 10% or more by withholding existing capacity from a base auction. The AESO will apply the market power screen using the following steps:

1. Calculate the average amount of UCAP of existing capacity assets that would need to be withheld from the market so that the auction clearing price would rise by 10% at a segment of the demand curve above the inflection point and at a segment of the demand curve below the inflection point around the inflection point; and

2. Calculate the portfolio size of existing capacity assets, measured in UCAP, that would be profitable from the 10% increase in auction clearing price by withholding the UCAP amount calculated in step 1. A firm that has a capacity offer control over a portfolio of existing capacity assets, measured in UCAP, equal to or greater than the size identified in step 2 above will fail the market power screen and will be subject to market power mitigation.

Default offer price cap

7.1.6 A firm that fails the market power screen will be required to offer all of its UCAP from existing capacity assets in the firm's portfolio at or below the default offer price cap of 80% of net-CONE in the base auction.

In the situation where the price cap is set at a gross-CONE multiple in accordance with subsection 4.4.2(c), the default offer price cap will be 80% of the ratio between the multiple of gross-CONE and the multiple of net-CONE specified in subsection 4.4.2(c), multiplied by gross-CONE.

For clarity, the default offer price cap will apply to the offers of an existing capacity asset located inside Alberta, including demand response assets, as well as the offers from existing external assets under the offer control of firms who fail the market power screen.

Asset-specific offer mitigation

7.1.7 A firm that fails the market power screen may request an asset-specific offer price cap for a qualified capacity asset with net avoidable costs higher than the default offer price cap.

7.1.8 Firms that fail the market power screen and request an asset-specific offer price cap must submit to the AESO, for review and approval, a cost submission justifying the requested asset-specific offer price cap.

7.1.9 A firm that submits a cost submission for an asset-specific offer price cap must indicate if the cost submission is based upon whether the qualified capacity asset would: (i) temporarily delist; or (ii) continue participation in the capacity market or the energy and ancillary service markets.

7.1.10 The cost submission will demonstrate the asset's net avoidable costs, based on the following formula (see subsection 7.1.13 below for an itemized list):

Net avoidable cost = avoidable cost – energy and ancillary services offset

Where "avoidable cost" means those described in subsection 7.1.12.

Where "energy and ancillary services offset" means the expected energy revenues less the variable costs required to be incurred to generate those revenues.

7.1.11 Additional details regarding the appropriate escalation rates that may be applied to calculate the avoidable costs measured in the dollar of the delivery year will be developed by the AESO and subject to further consultation.

7.1.12 The guiding principles that the AESO follows in interpreting "avoidable cost" include:

(a) Avoidable costs must be the costs that would not be incurred if the capacity asset is delisted for a year. Costs that would be deferred but would still occur in a subsequent year are not considered as avoidable.

(b) Avoidable costs must be those that are expected to be incurred only during the obligation period when the capacity asset is delisted.

(c) All avoidable costs must adhere to the principle of cost reduction, not reallocation, transferring or re-monetization of the costs.

7.1.13 The AESO may, in its assessment of the net avoidable costs, consider the following items where applicable.

(a) Avoidable fixed costs:

i. ***Avoidable labour expenses.*** Avoidable labour expenses related directly to operations and maintenance of the capacity asset. The categories of avoidable labour expenses may include:

- on-site based labour engaged in operations and maintenance activities;

- off-site based labour engaged in on-site operations and maintenance activities directly related to the capacity asset; and
- off-site based labour engaged in off-site operations and maintenance activities directly related to the capacity asset site.

ii. ***Avoidable administrative expenses.*** The categories of avoidable administrative expenses may include:

- those incurred for employee expenses, with the exception of employee expenses included in labour expenses related directly to operations and maintenance;
- environmental fees;
- safety and operator training;
- office supplies;
- communications; and
- annual asset testing, inspection and analysis.

iii. ***Avoidable fuel availability expenses.*** Avoidable fuel availability expenses are operating expenses related directly to fuel availability and delivery for the capacity asset that are not normally included for recovery in energy and ancillary services market offers. The categories of avoidable fuel availability expenses may include:

- those incurred for fuel transportation;
- costs of natural gas storage;
- costs of gas balancing agreements;
- costs of gas park and loan services; and
- variable mining costs.

iv. ***Avoidable maintenance expenses.*** Avoidable maintenance expenses are maintenance expenses related directly to the capacity asset, with the exception of those included in labour expenses related directly to operations and maintenance. The categories of avoidable maintenance expenses may include:

- those incurred for chemicals and materials consumed during maintenance of the capacity asset; and
- rented maintenance equipment used to maintain the capacity asset.

v. ***Avoidable fixed operating expenses.*** The categories of avoidable fixed operating expenses may include those incurred for:

- water treatment chemicals and lubricants;
- water, gas and station service;
- water rental;
- coal or gas royalties; and
- waste water treatment.

vi. ***Avoidable taxes, fees and insurance.*** The categories of avoidable taxes, fees and insurance may include those incurred for:

- insurance, permits and licensing fees,
- site security and utilities for maintaining security at the site; and

- property taxes.

vii. ***Avoidable carrying charges.*** Avoidable carrying charges may include short-term carrying charges for maintaining reasonable levels of inventories of fuel and spare parts that result from short-term operational unit decisions as measured by industry best-practice standards.

viii. ***Avoidable asset-specific corporate level expenses.*** Corporate-level expenses are those expenses directly linked to providing tangible services required for the operation or maintenance of the capacity asset to the extent that temporary or permanent delisting of the capacity asset results in a cost reduction rather than a reallocation. The categories of avoidable asset-specific corporate level expenses may include those incurred for:

- legal services; and
- regulatory and environmental compliance.

(b) ***Expected payment adjustment costs.*** Expected payment adjustment costs will be based on quantitative risk assessment practices generally used by the industry to estimate risk.

(c) ***Estimated variable operating costs.*** Estimated variable operating costs include, but are not limited to, heat-rate and variable operating and maintenance expenses for use in the AESO's determination of energy and ancillary service market offset. For assets without an observable market price for fuel, fuel-cost estimates may be required. The AESO will estimate the energy and ancillary services offset using the same methodology that the AESO would use to estimate the energy and ancillary services offset for net-CONE calculation, as described in Section 4, *Calculation of Demand Curve Parameters*.

7.1.14 A firm that submits a cost submission for an asset-specific offer price cap request must ensure that the information provided in the cost submission is the same information it uses to make its internal decisions by its senior management or the board of directors. The firm must have a corporate officer attest to the validity of the documentation used to support the asset-specific offer price cap request and confirm the completeness and accuracy of the cost data.

7.1.15 The AESO will review the cost submission and may seek clarification from the firm that provides the cost submission in the review process. The AESO will exclude cost items if the costs are inappropriately included, or inaccurately calculated or recorded.

7.1.16 The AESO will approve the asset-specific price cap request if the cost items are higher than the default offer price cap and will provide an asset-specific price cap. The AESO will not approve the asset-specific offer price cap request if the cost items are lower than the default offer price cap and the asset will be subject to the default offer price cap.

7.1.17 If the firm disputes the AESO's determination with respect to the asset-specific offer price cap, the dispute may be settled through the dispute resolution process discussed in Section 5, *Base Auction*.

7.2 Mitigation of firms with net-short capacity positions

7.2.1 The minimum offer price for all firms will be a price floor of $0/kW-year. No mechanisms for mitigating net-short (or buyer-side) market power will be implemented at the commencement of the Alberta capacity market. This approach may be reviewed at a future date.

7.3 Reporting of auction statistics and market competitiveness

Statistic report following a capacity auction

7.3.1 As soon as reasonably practicable following a capacity auction (likely within 1 week of the capacity auction), the AESO intends to publish on its website, concurrent with the notification of auction results, auction statistics reports including:

(a) clearing price ($/kW-yr);

(b) total cleared capacity (MW);

(c) cleared capacity differentiating between existing and new assets as well as technology type; and

(d) a list of assets with a capacity market obligation after the second rebalancing auction, including asset name, resource type, new/existing/uprates, and awarded MWs.

Assessment following a capacity auction

7.3.2 Following a capacity auction, the AESO may publish on its website an assessment of the following items:

(a) auction competitiveness;

(b) the consistency of market results with market conditions;

(c) whether to pursue potential changes to the market design for future auctions; and

(d) whether there are aspects of the market design that should be more thoroughly investigated in triennial reviews.

Independent performance reviews

7.3.3 The AESO may periodically commission an independent party to review market performance.