



March 6, 2015

Honorable Cheryl A. LaFleur, Chairman  
Honorable Philip D. Moeller, Commissioner  
Honorable Tony Clark, Commissioner  
Honorable Norman C. Bay, Commissioner  
Honorable Colette D. Honorable, Commissioner  
Federal Energy Regulatory Commission  
888 First Street, Northeast  
Washington, DC 20426

Dear Chairman and Commissioners:

The undersigned national energy trade associations are pleased to share with you the enclosed jointly developed Principles for Energy Market Price Formation Reforms to assist in your important efforts in this regard. Each of the undersigned associations appreciates the Commission holding workshops last year and looks forward to follow up action by the Commission consistent with the enclosed principles.

Sincerely,

EDISON ELECTRIC INSTITUTE  
ELECTRIC POWER SUPPLY ASSOCIATION  
NATURAL GAS SUPPLY ASSOCIATION  
NUCLEAR ENERGY INSTITUTE  
AMERICA'S NATURAL GAS ALLIANCE

## **Principles for Energy Market Price Formation Reforms<sup>1</sup>**

### **March 2015**

In order to provide the market signals necessary to support the investment and customer response needed to maintain reliability, energy prices, to the extent possible, should reflect the true value and marginal cost of providing power to the grid. To help reach this goal, policies that support the resources and services necessary for a reliable electricity system must be in place. As outlined in the principles below, this includes minimizing the impact of market rules and out of market operator actions that interfere with these price signals. The RTOs and ISOs should work to ensure that their market rules follow the principles below to help ensure that each organized wholesale electricity market has rules and mechanisms in place which establish price signals that support and promote efficient operations, reliability, and resource adequacy.

Recognizing that the existing market rules in each RTO and ISO have been developed to address the issues and concerns in that region and that there may be technical challenges associated with implementing all possible improvements to price formation in the immediate term to ensure that all costs are included in clearing prices, FERC should direct each ISO/RTO to consult with their stakeholders to develop and submit a plan to the Commission by a date certain. The plan should detail how current market rules and practices support the principles; identify concrete steps to change market rules and practices as necessary to support the principles; and, establish a timeframe for implementation. There should be periodic reporting to allow the Commission to monitor timely implementation of the plan put forth by each RTO and ISO.

#### **Principles:**

- (1) **Dispatch-Based Pricing** – Wholesale energy markets should provide accurate Day Ahead and Real Time price signals in order to promote efficient operation and resource adequacy. This includes observing the principles of dispatch-based pricing so that the cleared LMP is as consistent as possible with the marginal cost of operating the system, which includes the following:
  - Reflect in market clearing prices all units that are run, taking account of costs such as start-up or no load costs.
  - Include in operator modeling or algorithms the value of or services from all units in the market clearing price, including block-loaded or ramping units, operating reserves, units providing voltage support or reactive power, or units run in response to reliability events or needs.
  - Reflect all operator actions, including for reliability events, in the Day Ahead or Real Time market clearing price.
  - Reflect shortage or emergency situations in market clearing prices to provide needed investment signals.
  - Recover all reasonable and supportable costs incurred in unexpected circumstances, particularly when such costs are incurred in response to operator directives.

- (2) **Commitment** – Getting the Day Ahead commitment correct, including co-optimizing energy and reserves, creates and supports the right dispatch at the right price in the Real Time market. Co-optimized energy and reserve prices should provide market signals that support proper Day Ahead and Real Time reliability, reserve planning, unit commitment and system dispatch.
- (3) **Transparency** – Out of market actions and payments in the Real Time and Day Ahead markets should be minimized as they mask market action or needs and are not hedgeable by market participants. To the extent possible, there should be transparency as to the reasons for out of market payments so that stakeholders and market participants are confident that prices reflect market conditions and that the market is operating efficiently.

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<sup>1</sup> Jointly transmitted to the Federal Energy Regulatory Commission by the Edison Electric Institute, Electric Power Supply Association, Natural Gas Supply Association, Nuclear Energy Institute and America's Natural Gas Alliance.

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