



Memorandum

To: ISO Board of Governors and Western Energy Markets Governing Body
From: Anna McKenna, Vice President Market Design and Analysis
Date: September 19, 2024
Re: **Decision on Penalty Enhancements - Demand Response, Investigation, and Tolling (PEDRIT)**

This memorandum requires ISO Board of Governors and WEM Governing Body action.

EXECUTIVE SUMMARY

Management proposes tariff changes to update the Rules of Conduct that govern behavior by ISO market participants and stipulate sanctions for rule violations. Management proposes to: 1) remove the existing de minimis penalties for small meter data inaccuracies; 2) incentivize submittal of demand response baseline monitoring data; and 3) lessen the burden on ISO staff and market participants from administering the Rules of Conduct process.

These changes arise out of robust stakeholder participation and in large part address specific concerns raised by stakeholders during last year's Rules of Conduct update initiative. All stakeholders support or do not oppose the proposed changes. The proposed changes can be implemented by Q1 2025, pending FERC approval. Management recommends that the ISO Board of Governors and Western Energy Markets Governing Body approve the proposed changes to the Rules of Conduct as described in this memorandum.

Moved, that the ISO Board of Governors and WEM Governing Body approve the changes to the Rules of Conduct as described in the memorandum dated September 19, 2024; and

Moved, that the ISO Board of Governors and WEM Governing Body authorize Management to make all necessary and appropriate filings with the Federal Energy Regulatory Commission to implement the changes proposed in this memorandum, including any filings that implement the overarching initiative policy but contain discrete revisions to incorporate Commission guidance in any initial ruling on the proposed tariff amendment.

BACKGROUND

The ISO's Rules of Conduct establish guiding principles, delineate rules that market participants must follow, outline investigative procedures for potential violations, and create pre-determined financial sanctions. FERC maintains ultimate authority over the Rules of Conduct. Entities may appeal the ISO's Rules of Conduct decisions to FERC.

In response to stakeholder feedback and FERC penalty waiver requests submitted by market participants, the ISO included "Rules of Conduct Changes to Address Metering Penalty Issues" in its policy initiative roadmap in 2023. The ISO Board of Governors and WEM Governing Body jointly approved the Rules of Conduct proposal in September 2023, which changed the inaccurate meter data penalty from \$1,000 per trading day to the lower of: a) 30% of the error's absolute value; or b) \$1,000 per trading day.

At that time, the ISO also adopted three procedural enhancements to improve operational efficiency as follows: 1) replaced the ISO's annual penalty distribution filing at FERC with an informational report; 2) clarified existing eligibility requirements for penalty distribution; and 3) clarified how market adjustments for inaccurate meter data submitted but not processed through the settlement system apply in the Western Energy Imbalance Market.

After the approval of the three procedural enhancements, ISO staff and stakeholders continued to develop additional enhancements related to demand response resources' monitoring data penalty structure, streamlining penalty investigations, and providing a better method to toll penalties. This was done with the goal of addressing topics that stakeholders raised, but had been deferred to focus on updating quickly other changes such as the meter data penalty.

PROPOSAL

Remove penalties from meter data inaccuracies that fall below a de minimis threshold

An on-time meter data submission that is corrected after the allowable revision deadline is treated as the submission of inaccurate meter data in violation of the Rules of Conduct. As with all potential Rules of Conduct violations, where the ISO believes an inaccurate meter data violation occurred, it must initiate the Rules of Conduct investigative process outlined in the tariff. This can be a labor intensive and time-consuming process for both the ISO and the applicable market participant. If the ISO confirms through the investigative process that an inaccurate meter data violation occurred, then it penalizes the market participant at the lower of \$1,000 per trading day or 30% of the inaccuracy's value. This penalty structure is intended to incent submissions of timely and accurate meter data because accurate meter data is crucial for accurate market settlement. If market participants submit late corrections, market settlements must be revised in subsequent settlement statements, unduly burdening other market participants. Re-running market settlements increases costs for all market participants and increases the ISO's resource needs.

Stakeholders raised concerns that this penalty design is inappropriate for cases where the meter data correction addresses a small inaccuracy. They questioned whether small corrections warranted a penalty given they do not create meaningful disruptions to the market settlement process, and whether the burdens of administering an investigation for both the ISO and market participants was justified by whatever minimal disruption might be posed. Management agreed that small corrections do not warrant a penalty or the need for costly investigation.

In response to stakeholder concerns, Management proposes to introduce a de minimis tolerance band for inaccurate submissions so that inaccuracies that fall below 3% or 3 MWh per day are not violations of the Rules of Conduct. Because they will be defined as not being a violation, these small meter data corrections will not be subject to a penalty and they will not trigger an investigation. Market participants would still be required to report inaccuracies, and any resulting market settlement adjustments would continue to apply.

Incentivize demand response resources to submit monitoring data

Demand response resources must submit monitoring data used for monitoring, compliance, and auditing purposes. However, the ISO does not issue penalties for failure to submit monitoring data. The Rules of Conduct include a \$500 penalty for every day that tariff-required information is submitted after the applicable deadline. Because neither the tariff nor any business practice manual creates a deadline for submitting monitoring data, the ISO cannot apply the penalty in this case.

Without a submission deadline, the Department of Market Monitoring has observed significant and ongoing problems with some demand response providers failing to submit required monitoring data. These failures hamper the ability of the Department of Market Monitoring and other parts of the ISO to monitor demand response resources' self-reported reduction in load performance.

In 2022, the ISO proposed a Demand Response Business Practice Manual change (Proposed Revision Request 1444) to establish a monitoring data submission deadline at 52 days after the trading day (T+52B), allowing the ISO to penalize late submissions. Stakeholders requested that the ISO adjust penalties in tandem with setting a deadline because the penalties applied per resource for each day late and for each data file. One stakeholder indicated that with over 60 resources in their demand response portfolio, late submission of two required monitoring data files would result in a \$60,000 penalty for each day needed to resolve the issue. One minor system failure could cause such a scenario.

Stakeholders also observed that a per-resource penalty for late or missing demand response baseline monitoring data would expose scheduling coordinators to penalties that exceeded the penalties for late or missing meter data. These stakeholders questioned that disparity given that meter data is actually used in the market settlement process whereas the demand response baseline monitoring data is used for after-the-fact evaluation. In their view, late, inaccurate, or missing meter data is a more serious

violation and should face higher penalties than late, inaccurate, or missing demand response baseline monitoring data. Based on stakeholder feedback, the ISO withdrew Proposed Revision Request 1444 to focus instead on developing an appropriate penalty structure for demand response baseline monitoring data.

As a result of further stakeholdering of these issues, Management proposes changes to largely align the demand response resource monitoring data penalty structure with the settlement quality meter data penalty structure.

Monitoring data would be required on the same deadline as meter data, and the penalties for late and missing monitoring data would match the penalties for late and missing meter data. Monitoring data submitted after T+52B would be penalized a flat \$1,000 per trading day. Monitoring data submitted after T+214B would be penalized an additional flat \$3,000 per trading day, for a total of \$4,000. Importantly, the penalty would apply on a per-scheduling coordinator basis and not a per-resource basis. As monitoring data is submitted alongside settlement quality meter data and used to validate and audit resource performance calculations, it is appropriate to align late and missing demand response baseline monitoring data penalties with existing late and missing meter data penalties. However, unlike late changes to meter data, which are subject to a penalty, late changes to demand response baseline monitoring data are inappropriate because changes do not impact settlements. If late changes to baseline monitoring data result in the recalculation of performance measurements, penalties for late changes to meter data would apply. An additional penalty for late changes to monitoring data would result in an inappropriate double penalty for the same incident. Therefore, Management sees no justification for leveling an additional penalty for late changes to monitoring data.

In response to stakeholder requests, Management also proposes defining the monitoring data requirement as 45 historical days prior to the trade date. Under most of the demand response baseline methodologies, 45 historical days is the maximum number of days that could be used to calculate the performance baseline. Standardizing compliance enforcement at 45 historical days across baseline methodologies allows the ISO and DMM to streamline their monitoring efforts. However, because some less frequently used baseline methodologies may need more than 45 days of historical data to establish a baseline, Management also proposes keeping the ability to request additional information as needed for monitoring purposes, but not for data submittal compliance purposes.

Lessen Three Administrative Burdens

Management proposes three additional changes to ease both ISO and market participant administrative burdens. When the ISO identifies a Rules of Conduct violation, it initiates an investigative process. The investigative process consists of processing three separate notifications: a notice of review, a notice of results, and a notice describing penalties.

After the notice of review, the scheduling coordinator has 30 days to provide relevant information to the investigation. After the notice of results, the scheduling coordinator has 30 days to provide information relevant to the penalty calculation. At FERC's direction,

the ISO made all penalties objective. Since the ISO can now determine penalty amounts from information provided during the investigative process, Management proposes including the penalty description with the notice of results and eliminating the third notice.

The ISO collects financial penalties after the final notice. Penalties imposed by the ISO can be appealed to FERC. If the penalty is appealed to FERC in a timely manner and disputed with the ISO by the dispute deadline, the ISO returns the collected penalty, pending FERC decision. Management proposes deferring penalty settlement until 30 calendar days after the final notice. Management also proposes that if the market participant appeals to FERC and the scheduling coordinator informs the ISO, the ISO will further defer penalty settlement until 30 days after the FERC ruling. The market participant may still appeal ISO investigation and penalty conclusions to FERC after 30 calendar days, with the penalty refunded if the appeal is successful.

This update reduces the administrative burden of collecting and returning the penalty amount. The proposal also eliminates the reputational risk to a market participant, which may stem from its upfront payment of a large fine that FERC ultimately waives.

Finally, the ISO cannot impose sanctions on federal entities. If a federal entity violates the Rules of Conduct, the ISO reports the incident to the U.S. Secretary of Energy. Federal entities already receive notice during investigations, including a letter outlining findings. Management proposes eliminating the ISO's extra report to the Secretary of Energy.

Stakeholder Feedback

All stakeholders who commented support or do not oppose the proposed changes. Management's proposal incorporates three rounds of verbal and written stakeholder feedback.

The ISO held an initial workshop on June 7, 2023, to solicit stakeholder feedback and received ten sets of written stakeholder comments, which informed the initiative's scope, track prioritization, and straw proposal development.

The revised straw proposal was further shaped by additional feedback during the April 3, 2024, straw proposal meeting and subsequent submission of an additional seven sets of written stakeholder comments. The draft final proposal further reflects the stakeholder input from the June 3, 2024, revised straw proposal meeting and six sets of additional comments. Four stakeholders provided final proposal comments.

Two stakeholders proposed a materiality threshold or first-offense waiver for meter data violations. Management's proposal introduces a materiality threshold for the inaccurate meter data penalty instead of the waiver option, as the materiality threshold appropriately addresses the core stakeholder concern of small meter data corrections leading to full investigations for small penalties. First-offense waivers could waive major inaccuracies that should be dis-incentivized because of the impact they would have on settlements.

Management's proposal includes one stakeholder's recommendation to reduce the requirement for historical monitoring data from 90 days to 45 days, with the ISO maintaining the ability to request additional information as needed for monitoring purposes.

Upon approval of Management's proposal discussed in this memorandum, Management also agrees to the following three stakeholder requests that do not require changes to the tariff:

- 1) Introduce a courtesy warning ahead of potential exposure to monitoring data penalties.
- 2) Enhance training, use of examples, and a template guide to support market participants in deciding whether a contestation falls under the ISO's purview ("issues of fact") or FERC purview (all other issues).
- 3) Open a single customer dispute ticket at the investigation's start. The ticket closes when no violation is found or after the penalty is processed.

In final proposal comments, the Department of Market Monitoring noted that the proposed penalty for monitoring data may not incentivize a scheduling coordinator to submit all demand response resource data in a timely manner, particularly if the scheduling coordinator is having issues providing data for a small number of demand response resources in its portfolio. Proceeds from Rules of Conduct penalty revenue in a given year are allocated to all market participants that do not have violations in that year. Any scheduling coordinator that is late in submitting demand response baseline monitoring data for any market participant demand response resources they represent would cause all other represented market participants to unnecessarily violate the requirements for timely submittal of monitoring data. These violations would render the scheduling coordinator's market participants ineligible for that year's disposition of proceeds from Rules of Conduct penalty revenue. Additionally, FERC's market behavior rules (18 CFR § 35.41(b)) require market participants to exercise due diligence to prevent submission of false or inaccurate information to an ISO or RTO. Management believes scheduling coordinators have sufficient incentive for correct and timely submittal of monitoring data in the above scenario.

CONCLUSION

Management proposes to update the Rules of Conduct to remove penalties from meter data inaccuracies that fall below a de minimis threshold, incentivize demand response baseline monitoring data submittal, and lessen administrative burden associated with the Rules of Conduct enforcement process. All stakeholders support or do not oppose the proposed changes. Management recommends that the ISO Board of Governors and WEM Governing Body approve the proposal and related tariff changes as described in this memorandum.