

# Escalation Factor and Inflation Rate in Buyer-Side Mitigation Rules: Review and Proposed Tariff Revisions

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**Business Issues Committee**

May 17, 2017, Rensselaer, NY



# Agenda

- **Introduction**
  - History
  - Objective
- **Review NYISO proposal**
- **Closing**
  - Summary
  - Next steps
- **Appendix**
  - Illustrative examples

# Background

Date	Working Group	Discussion points and links to materials
10-07-16	ICAP Working Group (ICAPWG)	First discussion on how to apply escalation and inflation in Buyer-side Mitigation (“BSM”). The NYISO presented several alternatives to current BSM rules in order to solicit input from stakeholders
01-27-17	ICAPWG	NYISO presented a proposal on applying escalation and inflation in BSM rules, developed from the previously presented alternatives and stakeholder input
3-8-17	ICAPWG	NYISO presented a proposal in response to stakeholder input
4-4-17	ICAPWG	NYISO reviewed the proposal and presented draft tariff revisions to achieve those proposals
5-11-17	ICAPWG	NYISO presented clarifying language on one tariff revision based on stakeholder input
Today	Business Issues Committee	The NYISO will review proposals for how to apply escalation and inflation in BSM rules and present proposed tariff revisions and a proposed motion

# Today's Objective

- Proposal
- Tariff Language

# Proposal–Enhance current tariff provisions on

- Inflation in BSM determinations
- Adjusting New Entrants’ Offer Floors to Year of Entry Dollars
  - 1) If Unit Enters Before Year 1 of a Mitigation Study Period (“MSP”)
  - 2) If Unit Enters After Year 1 of a MSP
- Annual Adjustments to Offer Floors

# NYISO's Proposal for Inflation in BSM Determinations

Use the most recently published ten year projections for inflation from the Survey of Professional Forecasters (or if no longer available, a similar suitable source) to identify:

- Examined Facility Unit Net CONE projected for a MSP, and
- The price on the ICAP Demand Curve projected for a MSP
  - Provides consistency between BSM tests
  - Removes more volatile and harder to predict cost data (i.e., turbine, materials, labor) used in Demand Curve escalation factor
  - Provides a transparent and reasonable forecast for future inflation expectations
  - Requires tariff change

# NYISO's Proposal for Adjusting New Entrants' Offer Floors to Year of Entry Dollars

- 1) If a unit enters into service prior to the first Capability Year of the MSP the NYISO will use the same long-run projection for inflation that has been proposed on the previous slide\* to deflate the entrants' Offer Floor
  - Provides consistency between BSM tests (i.e., same value used during BSM determinations)
  - Uses forecasted inflation to reasonably predict what future inflation would be
  - Tariff change required

*\* Same Long-run projection for inflation from the Survey of Professional Forecasters (or if no longer available, a similar suitable source) that was used at the time of determination*

# **NYISO's Proposal for Adjusting New Entrants' Offer Floors to Year of Entry Dollars *(continued)***

- 2) If a unit enters into service after the first Capability Year of the MSP the NYISO will adjust its Offer Floor using the relevant published Demand Curve inflation rate(s) that would have been used to make annual adjustment(s) had the unit entered into service in the first Capability Year of the MSP**
- Maintains assumed general inflation rate from effective Demand Curve escalation factor
  - Provides consistency with the Demand Curve annual updates

# Current Provisions for Annually Adjusting Offer Floor Levels

- Existing Offer Floors shall be adjusted annually using the most recent Demand Curve inflation rate
  - *MST Att. H 23.4.5.7*
- The NYISO is not proposing a change to this provision
  - Maintains assumed general inflation rate from effective Demand Curve escalation factor
  - Provides consistency with the Demand Curve annual updates

# Next Steps

- MC Vote on 5/31
- Tariff filing

# Feedback?

- The NYISO welcomes additional suggestions and feedback
- Email additional feedback to: [deckels@nyiso.com](mailto:deckels@nyiso.com)

# Questions?

We are here to help. Let us know if we can add anything.

# The Mission of the New York Independent System Operator, in collaboration with its stakeholders, is to serve the public interest and provide benefits to consumers by:

- Maintaining and enhancing regional reliability
- Operating open, fair and competitive wholesale electricity markets
- Planning the power system for the future
- Providing factual information to policy makers, stakeholders and investors in the power system



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# Appendix

- Description of Survey of Professional Forecasters Long –run Projection for Inflation
- Examples of adjusting Offer Floors to Year of Entry Dollars

# Survey of Professional Forecasters Long-Run Projections for Inflation – Q1 2017\*

Median Short-Run and Long-Run Projections for Inflation (Annualized Percentage Points)								
	Headline CPI		Core CPI		Headline PCE		Core PCE	
	Previous	Current	Previous	Current	Previous	Current	Previous	Current
<i>Quarterly</i>								
2017:Q1	2.2	2.5	2.2	2.4	1.8	2.0	1.8	1.8
2017:Q2	2.2	2.3	2.2	2.2	1.9	2.0	1.8	1.9
2017:Q3	2.2	2.3	2.2	2.1	1.9	2.0	1.9	1.9
2017:Q4	2.2	2.5	2.2	2.2	2.0	2.1	1.9	1.9
2018:Q1	N.A.	2.4	N.A.	2.3	N.A.	2.1	N.A.	2.0
<i>Q4/Q4 Annual Averages</i>								
2017	2.2	2.4	2.2	2.2	1.9	2.0	1.9	1.9
2018	2.2	2.3	2.2	2.3	2.0	2.0	1.9	2.0
2019	N.A.	2.3	N.A.	2.2	N.A.	2.0	N.A.	2.0
<i>Long-Term Annual Averages</i>								
2016-2020	2.13	N.A.	N.A.	N.A.	1.90	N.A.	N.A.	N.A.
2017-2021	N.A.	2.30	N.A.	N.A.	N.A.	2.03	N.A.	N.A.
2016-2025	2.22	N.A.	N.A.	N.A.	2.00	N.A.	N.A.	N.A.
2017-2026	N.A.	2.30	N.A.	N.A.	N.A.	2.10	N.A.	N.A.

\* <https://www.phil.frb.org/research-and-data/real-time-center/survey-of-professional-forecasters/2017/survq117>

# Survey of Professional Forecasters Long-Run Projections for Inflation – Q1 2017 *(continued)*

- **Headline inflation includes all aspects within an economy that experiences inflation. Core inflation removes components that can exhibit large amounts of volatility from month to month**
- **Consumer Price Index (CPI) and Personal Consumption Expenditures (PCE) are the two common measures for inflation**
- **The NYISO would take the average of the expected long-term annual averages for Headline CPI and Headline PCE inflation over the next 10 years**
  - For Example, if Headline CPI = 2.30% and Headline PCE = 2.10% then the NYISO would use the average = 2.20%

# Examples: Adjusting Offer Floors to Year of Entry Dollars

- Assume a Class Year 2017 generator is determined to have an Offer Floor in the first Capability Year of the MSP (i.e., year 2020) = \$10.00/kW-month
- Assume long-run forecast for inflation = 2.0%
- Assume most recent Demand Curve inflation rate = 1.5%
  - Example 1: Assume the generator enters into service in 2019 (i.e., 1 year prior to first Capability Year of the MSP)
    - NYISO deflates the Offer Floor from 2020 dollars to 2019 dollars using the long-run forecast for inflation of 2.0%
    - Offer Floor 2019 =  $\$10.00 / (1 + 2.0\%)$
    - Offer Floor 2019 = \$9.80/kW-month
  - Example 2: Assume the generator enters service in 2021 (i.e., 1 year after first Capability Year of the MSP)
    - NYISO inflates the Offer Floor from 2020 dollars to 2021 dollars using the most recent Demand Curve inflation rate of 1.5%
    - Offer Floor 2021 =  $\$10.00 * (1 + 1.5\%)$
    - Offer Floor 2021 = \$10.15/kW-month