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PROJECT NO. 40000

PUC RULEMAKING TO AMEND §
PUC SUBST. R. §25.505, RELATING TO §
RESOURCE ADEQUACY IN THE §
ELECTRIC RELIABILITY COUNCIL §
OF TEXAS (ERCOT) POWER REGION

PUBLIC UTILITY COMMISSION
OF TEXAS

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**COMMENTS OF THE ERCOT RELIABILITY ADVOCATES ON
THE BRATTLE GROUP'S PROPOSED POLICY OPTIONS**

The ERCOT Reliability Advocates include Calpine Corporation (“Calpine”), Exelon Generation Company, LLC (“Exelon”) and Next Era Energy Resources, LLC (“Next Era”) (collectively, the “Advocates”). We submit the following comments in response to the Public Utility Commission of Texas (“Commission”) request for comments on The Brattle Group’s report on proposed resource adequacy policy options, filed with the Commission on October 19, 2012.¹

The Commission has a unique opportunity to achieve a resource adequacy end-state befitting the State of Texas and in a timely and informed manner. The Commission already has recognized that the current energy-only resource adequacy model for ERCOT may not be capable of delivering the long-term reliability desired by the Commission and expected by Texans. The Advocates support the Commission’s effort to identify the problem and its continued consideration of the potential solutions from The Brattle Group (“Brattle”), the IMM and market participants. The Advocates urge the Commission to take informed decisive action in the very near term to adopt a resource adequacy framework to (1) support long-term consumer and business confidence in system reliability and (2) remove the current regulatory uncertainty that is dampening the financial signal needed by potential investors who are likely to invest in the very capacity resources needed in the next few years.

¹ The Brattle Group, “Resource Adequacy in ERCOT: ‘Composite’ Policy Options” (October 25, 2012 (hereinafter the “Composite Options”).

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The Advocates filed two sets of detailed comments with the Commission stating their positions on what is the best path forward to ensure long-term resource adequacy in ERCOT.² The Advocates continue to urge the Commission:

- Adopt a specific reserve margin requirement and
- Centralized forward capacity market, similar to the Forward Reliability Mechanism (“FRM”) proposed by the Advocates.³

The reserve margin requirement sets the reliability objective established by the Commission and ERCOT and the centralized forward capacity market is the resource adequacy implementing mechanism that ensures reliability at a competitive cost to consumers.

The Advocates generally support Brattle’s Composite Policy Option #2, the Texas Capacity Market because it meets the essential elements set forth in the Advocate’s proposal. The Brattle analysis clearly states the reasons the Texas Capacity Market is the better of the two composite policy options. The Advocates also believe Brattle has solidly framed a roadmap, including a timeline to move from approving to implementing the Texas Capacity Market in a deliberate and timely fashion.

Brattle Composite Option #1: Energy-Only Market with Support for Demand Response

The Advocates appreciate the fact Brattle was requested by the Commission to propose an energy-only option and we accept that Brattle believes this may be the best such option if, and only if, the Commission decides to modify the current energy-only market. Whatever the supposed merits of Composite Option #1, particularly as compared to the Texas Capacity Market, the Advocates view Composite Option #1 as an inferior method to achieve and ensure long term system reliability sought by this Commission and expected by consumers.

In previous comments, the Advocates highlighted the problems with each of the energy-only options offered in the Brattle Report. The Advocates believe the energy-only based Composite Option #1,

²Commission Project No. 40268, Initial Comments of the ERCOT Reliability Advocates (“Advocates’ Initial Comments”) (August 30, 2012) and Reply Comments ERCOT Reliability Advocates (“Advocates’ Reply Comments”) (September 25, 2012).

³Id.

particularly the demand response component suffers several inherent deficiencies as a viable long-term competitive market design option, including:

- Inherently discriminatory by creating a capacity market only for demand response. The better option is to adopt the Texas Capacity Market and let a market-driven auction, rather than administrative forces determine if demand resources are the quickest and most cost effective capacity resources.
- Destroys the commercial incentive for entry into the market by new “merchant” generation, unit up rates and avoided unit shutdowns as the reserve margin becomes tighter.
- High degree of uncertainty about how much demand response can be counted on to “show up” in the market. The Brattle analysis points to this as a significant issue.⁴ For example, while PJM has a relatively vibrant demand response market the Advocates understand that a significant percentage of demand response providers actually bought out of their positions for the 2012/2013 delivery year.⁵
- The proposed demand resource proposal has the potential to be a “dead-end” option; even if you could acquire enough DR resources to meet the needs for 2014 and 2015, then what? Assuming load keeps growing, ERCOT will still need a solution that looks like the FRM, but another several years will have passed without any action to implement such a market. Further, if the demand response program falters, as the Advocates believe it may, how do you timely implement the better alternative, the Texas Capacity Market? Brattle noted this as a serious concern about the energy-only alternatives during the September 6 Workshop.

The Advocates have previously raised concerns about proposals to increase operating reserves via an administrative withholding mechanism.⁶ The current proposal does nothing to cure those concerns.

⁴Brattle Composite Options, slides 13, 17.

⁵Brattle Composite Options, slide 34 (“DR potential is uncertain, so shortfalls are more likely if there is no administrative withholding.”).

⁶Advocates’ Initial Comments, p. 4 and Advocates’ Reply Comments, p. 2.

Moreover, Brattle implicitly recognizes this is not a simple administrative solution in its statement that even “determining the right quantity is NOT straightforward”.⁷

In prior comments, Brattle and the IMM raised significant concern about using backstop generation: administrative withholding of generation.⁸The Advocates agree with those concerns and support Brattle’s recommendation against creating a backstop procurement mechanism as part of an energy-only market design.⁹

Brattle Composite Option #2: Texas Capacity Market

As the Advocates have stated previously, a centralized forward capacity market is the best mechanism to ensure ERCOT meets the reliability objectives established by the Commission. The Advocates will not use these comments to restate all of the reasons to support a centralized forward capacity market. The Advocates believe the Commission already has the benefit of the Advocates’ prior comments; the written and oral comments on behalf of Brattle, particularly their strong arguments debunking the myths about a centralized forward capacity market, and the comments by the IMM. In addition, other market participants have submitted comments that generally state their support for centralized forward capacity market.¹⁰

The Advocates strongly urge the Commission to approve, at least in concept, moving forward with the adoption of a centralized forward capacity market similar to the Texas Capacity Market. The Advocates are encouraged that the Texas Capacity Market is very similar in concept to the Advocate’s proposed FRM and meets the following minimum requirements:

⁷Brattle Composite Options, slide 14.

⁸Oral comments during the September 6 Commission Workshop by Sam Newell, The Brattle Group and Dan Jones, IMM/Potomac Economics.

⁹Brattle Composite Options, slide 15.

¹⁰ Several other market participants have filed written comments in Commission Project 40268 that support a centralized forward capacity market, including Direct Energy Services LLC and NRG Energy Inc. In addition, CPS Energy concludes, “If the Commission chooses [a reserve margin requirement versus a target], a centralized forward capacity market would be best.” CPS Energy Comments in Commission Project No. 40268, p. 5. (September 25, 2012).

- **Transparency:** Establishes a competitive auction administered by an independent entity to procure sufficient capacity that is equal to the forecast peak demand for the delivery year, plus the reserve margin requirement.
- **Forward:** Capacity is procured at least three-years before the delivery year.
- **Non-discriminatory:** (1) All qualified capacity resources are eligible to participate in the auction, including existing and new generation and price responsive demand and (2) all selected capacity resources must be subject to comparable performance metrics.
- **Mandatory:** All LSE's must participate in the auction.

The Texas Capacity Market meets the essential elements of the Advocates' proposal, but there are several differences worth addressing in these comments. First, the Advocates support two recommendations by Brattle: (1) The Texas Capacity Market should be a single-market and (2) a Minimum Offer Price Rule ("MOPR")¹¹ is not needed. As suggested by Brattle, the ERCOT market and the Texas economy are simply different than other markets that use a forward capacity market. The Advocates agree with the reasoning behind the Brattle recommendation and believe by adopting both recommendations the Commission will ensure a more efficient implementation of the new market design. Moreover, if the Commission approves the Texas Capacity Market, both of these issues can be revisited as warranted by a maturing market.

Second, Brattle addresses a key element to a forward capacity market: the demand curve. Brattle does a good job of identifying the relative merits of the sloped demand curve versus a vertical demand curve, but stops short of making a recommendation for the Commission.¹² As noted by Brattle, the sloped demand curve (1) moderates price volatility for the benefit of buyers and sellers, (2) reduces the likelihood of price manipulation and (3) recognizes the value of capacity resources in excess of the required reserve margin. As the Commission considers this issue, the Advocates strongly urge the Commission to choose the solution that provides the best set of long benefits for the market from the

¹¹ Although a full-fledged MOPR may not be required, the Advocates believe there may be a need for a rule at the outset that ensures against buyer-side market power.

¹²Brattle Composite Options, slide 22.

beginning. The Advocates' understand the sloped demand curve will require more work up-front by the Commission and market participants, but we included it in our FRM proposal in a belief it is the best option for the ERCOT market.

The Advocates recognize that even if the Commission approves the concept of moving ahead with the Texas Capacity Market or a similar proposal there are a number of other key decisions either the Commission and/or ERCOT stakeholders must address. An example highlighted in the Brattle analysis is how to address any transition period challenges regarding the timing of the initial auctions and auction prices.¹³The Advocates have not formed an opinion on this and other important design issues, but we look forward to the opportunity to move forward with a centralized forward capacity market and are willing to work with the Commission and its Staff and consultants, ERCOT and other market participants to create a consensus around this policy option.

Summary

The Commission should adopt a mandatory ERCOT annual planning reserve margin requirement and centralized forward capacity market similar to the proposed Texas Capacity Market and the Advocate's FRM proposal to ensure the Commission's established reliability objective is achieved. The Advocates believe the proposed change in market design is a natural evolution of the ERCOT market into a true long-term competitive market solution that can best provide sustainable reliability under a variety of market conditions.

Respectfully submitted,



William J. Taylor III
Vice President, Government & Regulatory Affairs
Calpine Corporation
717 Texas, Suite 1000
Houston, Texas 77002
Phone: (713) 830-8821
Fax: (713) 830-8705

¹³Brattle Composite Options, slide 30.

Kristy Ashley by gl

Kristy Ashley
Director – Market Design
Exelon Generation Company
1005 Congress Avenue, Suite 800
Austin, Texas 78701
Phone: (512)391-1962
Fax: (512) 479-4031

Brian Gedrich by gl

Brian Gedrich
Next Era Energy Resources, LLC
Director – Regulatory Affairs
823 Congress, Suite 1330
Austin, Texas 78701
Phone: (512) 439-0831
Fax: (512) 439-0835