BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

FILED
10-30-14
04:59 PM

Order Instituting Rulemaking to Consider Electric Procurement Policy Refinements pursuant to the Joint Reliability Plan.	Rulemaking 14-02-001 (Filed February 5, 2014)

THE OFFICE OF RATEPAYER ADVOCATES' COMMENTS IN RESPONSE TO ASSIGNED COMMISSIONER AND ADMINISTRATIVE LAW JUDGE'S RULING ISSUING STAFF REPORT & PROPOSAL

MATT MILEY
DIANA L. LEE
Attorneys

Office of Ratepayer Advocates
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Phone: (415) 703-4342
Fax: (415) 703-2262
Email: Diana.lee@cpuc.ca.gov

RADU CIUPAGEA
PETER SPENCER
YAKOV LASKO
Analysts

Office of Ratepayer Advocates
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Phone: (415) 703-1529
Email: Radu.Ciupagea@cpuc.ca.gov

October 30, 2014

TABLE OF CONTENTS

I. INTRODUCTION

Pursuant to the *Assigned Commissioner and Administrative Law Judges' Ruling Issuing Staff Report & Proposal* (Ruling) issued on October 2, 2014, the Office of Ratepayer Advocates (ORA) submits the following comments on seven of the eight questions posed in the Ruling[1] and issues raised in the "Joint Reliability Plan Track One Staff Proposal" (Staff Proposal). The Staff Proposal is attached to the Ruling. The questions posed in the Ruling and the Staff Proposal itself address issues related to the availability of flexible capacity, existing forward procurement practices, the risk of inefficient retirement of existing resources, the costs and benefits of multi-year resource adequacy (RA) for ensuring electric system reliability, and the feasibility and potential mechanics of a multi-year RA program.

The following list summarizes ORA's response to the issues raised in the Ruling:

1. ORA's Risk of Unplanned Retirement analysis and PLEXOS Production Cost Simulation study do not indicate that there are currently any generation resources that are both at risk of unplanned retirement and critical for reliability in the medium term.
2. The oversupply of both available and contracted capacity for the next three years along with the results of ORA's Risk of Unplanned Retirement analysis and PLEXOS Production Cost Simulation study indicate that adopting multi-year RA requirements at the present time is unnecessary.
3. While it is too early to conclude that the new flexible RA requirements are sufficient to encourage the retention of the existing flexible resources that will be needed in the next ten years, these additions to the existing reliability framework should enhance the reliability of the grid in the future.
4. If multi-year requirements for flexible capacity are adopted before better understanding the impact of new flexible RA requirements and improving the forecasting methods and subsequent requirements, the resulting regulatory uncertainty is likely to impose unnecessary costs to ratepayers.

[1] ORA's comments do not respond to question 8 of the ruling, but ORA may respond to the comments of others in its reply comments.

II. RESPONSES TO QUESTIONS IN THE RULING

1. Are there valuable generation resources that are not receiving any medium- or long-term contracts, and are therefore at risk of inefficiently retiring? (Refer to definitions in section II.C "Inefficient Retirements").

The Staff Proposal proposes the new term "inefficient retirement." As defined in the Staff Proposal, a "resource would be found to be inefficiently retiring if the resource is not receiving adequate payments from both the capacity market and the energy market"[2] to allow it to operate at a profit in the next five years or make upgrades necessary to either continue operating or provide an essential service to the grid. In addition, "this resource is valuable because it has unique characteristics that make it critical for reliability in the medium term."[3]

ORA appreciates the Staff Proposal's detailed description of what could constitute an inefficient retirement. However, it is not apparent that a resource with valuable unique characteristics that make it critical for reliability in the medium term would seek to actually retire even if it were to not operate at a profit in the next five years. The higher likelihood of obtaining capacity contracts as once through cooling (OTC) plants retire through 2020, the introduction of the new flexible RA requirement, the upcoming creation of a Flexible Ramping Product and the Availability Incentive Mechanism provide future revenue opportunities for the resources that may not necessarily operate at a profit in the next five years. For example, over a ten year period of time, valuable resources may be profitable even if they were to operate at a loss over the initial five year period. Therefore, such resources should not necessarily be considered at risk of inefficiently retiring.

ORA performed a Risk of Unplanned Retirement analysis to quantify the magnitude of potential unplanned retirements of existing resources that may be needed to meet future flexibility requirements. A generation resource is assumed to be at risk of unplanned retirement if it does not have a capacity contract through 2020 or the likelihood of that resource obtaining a capacity contract over the next few years through 2020 is not high. ORA's assumptions in the

[2] Staff Proposal, p. 15.

[3] Staff Proposal, p. 15.

Risk of Unplanned Retirement[4] analysis differentiate between generation resources that have a high degree of capacity revenue certainty and those that may not be able to obtain capacity contracts due to the current oversupply of generic capacity.[5] The latter are more at risk of unplanned retirement. ORA found that there were nine units potentially at risk of unplanned retirement, comprising approximately 2,412 MW of which 1,389 MWs are flexible.

Furthermore, as part of ORA's Risk of Unplanned Retirement analysis, ORA conducted a PLEXOS Production Cost Simulation study for year 2021 to understand the effect of unplanned retirements accounting for 2,412 MWs of NQC and 1,389 MWs of Effective Flexible Capacity on potential resource need.[6] ORA's study sought to identify whether the unplanned retirement of up to 2,412 MW of generation resources would jeopardize system reliability in 2021. Similarly to the Staff Proposal's second part of the definition for inefficient retirements, ORA's PLEXOS study sought to identify whether the generation resources at risk of unplanned retirement are critical for reliability in the medium term.

ORA's Risk of Unplanned Retirement analysis and PLEXOS Production Cost Simulation study do not currently indicate that there are any generation resources that are both at risk of unplanned retirement and critical for reliability in the medium term. Based on the analysis, ORA concludes that there are no generation resources at risk of inefficiently retiring. While there are nine units potentially at risk of unplanned retirement due to the fact that they are less likely to receive capacity contracts, ORA's PLEXOS Production Cost Simulation study does not indicate that these resources will be needed for reliability in 2021. This is due, in part, to the significant quantity of forward procurement contracted by CPUC Load Serving Entities (LSEs)[7] and the current oversupply of available capacity[8] as shown in the Staff Proposal.

---

[4] ORA's Risk of Unplanned Retirement and PLEXOS Production Cost Simulation study is available here: http://www.ora.ca.gov/general.aspx?id=2831. In addition, ORA attached the Risk of Unplanned Retirement and PLEXOS Production Cost Simulation study to its October 29, 2014 motion seeking its introduction into the record of this proceeding.

[5] Staff Proposal, p. 35.

[6] ORA's Risk of Unplanned Retirement and PLEXOS Production Cost Simulation study is available here: http://www.ora.ca.gov/general.aspx?id=2831

[7] Staff Proposal, pp. 18-24.

[8] Staff Proposal, pp. 20-22.

2. What would motivate such resources to inefficiently retire?

It is not apparent what would motivate generation resources to inefficiently retire. It is reasonable to assume that if a "resource is valuable because it has unique characteristics that make it critical for reliability in the medium term,"[9] the owners of that resource are aware of its high value and the opportunity for revenue in exchange for the unique characteristics that make the resource critical for reliability in the medium term. The higher likelihood of obtaining capacity contracts as OTC plants proceed to retire through 2020, the introduction of the new flexible RA requirement, the upcoming creation of a Flexible Ramping Product and the Availability Incentive Mechanism provide future revenue opportunities for the valuable resources and decrease the risk that they will seek to inefficiently retire even if they were to not obtain capacity contracts over the short-term.

3. Is the new flexible RA requirement sufficient to encourage retention of the existing flexible resources and/or investment in new necessary flexible resources that will be needed in the next ten years?

The new flexible RA requirements created by the Commission in Decision (D.) 14-06-050 are expected to provide the California Independent System Operator (CAISO) with flexible capacity attributes necessary to maintain grid reliability.[10] The demand for these attributes is predicted to increase in future years.[11] The CAISO will conduct an annual flexible capacity needs assessment to determine the need for capacity possessing the necessary flexible attributes for grid operation. The Commission adopts the CAISO assessment each year in the Commission's RA proceedings as a basis for assigning flexible capacity requirements to LSEs. The current year-ahead RA program assures that the CAISO will have sufficient flexible capacity from resources committed in RA contracts.

As pointed out in the Staff Proposal, "it is too soon to assess the effectiveness of the recently implemented flexible procurement requirements."[12] The flexible capacity RA requirements will begin in January 2015, and the first LSE filing complying with the new flexible requirements is not due until October 31, 2014. Due to an oversupply of flexible

[9] Staff Proposal, p. 15.

[10] D.14-06-050, p. 2.

[11] Staff Proposal, pp. 9-10.

[12] Staff Proposal, p. 2.

capacity in 2014,[13] which is likely to persist for the next few years, the premium price for flexible capacity may not be significantly higher than the price for generic capacity. In addition, due to the fact that forward procurement of flexible capacity is currently above the projected flexible capacity needs through 2016,[14] it is unlikely that multi-year flexible requirements will result in additional flexible capacity procurement through 2016.

The new flexible capacity requirements are a work in progress. The Commission will continue to evaluate the requirements in 2015 and is committed to making additional changes.[15] The Commission is expected to re-evaluate the flexible capacity framework in 2017, and the CAISO is expected to re-evaluate the associated CAISO tariff on Flexible Resource Adequacy and Must Offer Obligations in 2017. According to the CAISO, further studies are needed to define and quantify flexible attributes which will be needed in the future.[16]

It is therefore premature to conclude that the new flexible RA requirement is insufficient to encourage the retention of the existing flexible resources or investment in new flexible resources that will be needed in the next ten years. D.14-05-060 created new flexible requirements beginning in 2015 as an important step to enhance grid reliability. In the absence of either compelling evidence indicating a need for multi-year RA or data on the effectiveness of new reliability measures on the retention of and investments in flexible resources, the Commission should allow the new flexible RA requirement to address the need for flexible resources and reexamine the need for multi-year RA in 2017.

4. Will a multi-year RA requirement change the quantity of inefficient retirements, or the potential impact from such retirements?

As previously mentioned, ORA's Risk of Unplanned Retirement analysis and PLEXOS Production Cost Simulation study do not indicate that there are any generation resources at risk of inefficiently retiring. Thus, a multi-year RA requirement, at this point in time, would not change the quantity of inefficient retirements or the potential impact from such retirements.

[13] Staff Proposal, Figure 5, p. 22.

[14] Staff Proposal, Figure 5, p. 22 and Figure 6, p. 23.

[15] D.14-06-050, p. 19.

[16] R.13-12-10, CAISO Opening Testimony/Meeusen, August 13, 2014, pp. 19-20.

ORA agrees with the CPUC's determination that the "current reliability framework has provided for reliable operation of the transmission grid over the past decade."[17] The Staff Proposal correctly notes that:

> "[T]he RA and LTPP programs have, to date, adequately ensured that appropriate resources are procured by CPUC-LSEs both in the short and long term. Furthermore, in the instances in which California has experienced an unexpected event or outage, sufficient replacement capacity has come online in a timely manner, resulting in *de minimis* reliability impacts, if any. This fact also demonstrates the resiliency and adaptability of California's electric system, thanks to policies implemented via RA and LTPP proceedings, such as the planning reserve margin (PRM)."[18]

Based on the proven track record of the existing reliability framework, the current level of forward procurement conducted by CPUC LSEs[19] and the current oversupply of available capacity,[20] in conjunction with ORA's analysis and PLEXOS study, we conclude that, at this time, the estimated quantity of inefficient retirements is zero. ORA's Risk of Unplanned Retirement analysis indicates that there are nine units potentially at risk of unplanned retirement, comprising approximately 2,412 MW of which 1,389 MWs are flexible. ORA's PLEXOS Production Cost Simulation study did not indicate that the unplanned retirement of these nine units would jeopardize system reliability in 2021. Thus, a multi-year RA requirement, at this time, is unnecessary to change the quantity of inefficient retirements, or the potential impact from such retirements.

5. Is it reasonable and appropriate to develop and implement multi-year RA requirements at the present time, and why or why not?

The CPUC's regulated LSEs significant quantity of forward procurement[21] limits the magnitude of the risk of unplanned retirement. The current oversupply of flexible capacity provides a buffer against any reliability issues stemming from the unplanned retirement of up to nine units comprising 2,412 MW with 1,389 MWs of flexible capacity. Based on its Risk of

[17] R.14-02-001, p. 3.

[18] Staff Proposal, p. 5.

[19] Staff Proposal, pp. 18-24.

[20] Staff Proposal, pp. 20-22.

[21] Staff Proposal, pp. 20-23.

Unplanned Retirement analysis and PLEXOS Production Cost Simulation study, ORA concludes that implementing multi-year RA requirements at the present time is unnecessary.

For system RA requirements, ORA recommends that the Commission implement "Option 4: No additional requirement."[22] There is an "overabundance of generic system capacity"[23] and a "significant quantity of forward procurement."[24] Thus, a multi-year RA procurement requirement for system capacity is not necessary to ensure reliability and would result in unnecessary costs to ratepayers.

For local RA requirements, ORA recommends the Commission adopt "Option 2: No additional requirement (status quo)."[25] The local area capacity prices are generally higher than system capacity prices.[26] This price premium reflects the scarcity of resources in many local areas, "where the supply is exactly equivalent to forecasted demand from year to year."[27] Therefore, it is reasonable to conclude that necessary local resources will receive capacity contracts from year to year going forward. In addition, the new generation resources authorized in D.13-02-015 and D.14-03-004, the LTPP Track 1 and 4 decisions, and "new transmission upgrades should improve certain local reliability concerns in local areas in Southern California."[28] Therefore, a multi-year RA procurement requirement for local capacity is not necessary to ensure reliability and would likely result in additional upward price pressures for local capacity.[29]

For flexible RA requirements, ORA recommends the Commission adopt "Option 3: No action until 2017."[30] Modifications expected to the new flexible RA requirements and improvements to the forecasting of flexible needs[31] support a delay in the consideration of multi-year flexible RA requirements at this point in time. In addition, the oversupply of both available

---

[22] Staff Proposal, p. 32.

[23] Staff Proposal, p. 35.

[24] Staff Proposal, p. 24.

[25] Staff Proposal, p. 41.

[26] CPUC Staff's 2012 Resource Adequacy Report, issued April 2014, Table 12, p. 27. Available at http://www.cpuc.ca.gov/PUC/energy/Procurement/RA/

[27] Staff Proposal, p. 44.

[28] Staff Proposal, p. 44.

[29] Staff Proposal, p. 34.

[30] Staff Proposal, p. 35.

[31] Staff Proposal, p. 41.

and contracted flexible capacity over the next three years[32] along with the results of ORA's Risk of Unplanned Retirement analysis and PLEXOS Production Cost Simulation study do not indicate that adopting multi-year RA requirements at the present time is reasonable and appropriate.

6. How should uncertainty be dealt with in setting multi-year RA requirements, and how might this proceeding mitigate the effects of regulatory uncertainty?

Regulatory uncertainty is likely to create unnecessary costs to ratepayers if multi-year requirements for flexible capacity are adopted before better understanding the impact of new flexible RA requirements, improving the forecasting methods and refining the resulting requirements.[33] Wise investments and sound procurement decisions are enhanced by minimizing regulatory uncertainty.

In the meantime, the CAISO continues to refine the definitions of flexible capacity in order to secure the attributes necessary to reliably operate the grid. As noted in the Staff Proposal, "Recent discussions between the Commission Staff and CAISO, both through the RA and JRP proceedings, have focused on flexible characteristics and whether the three categories of Flexible RA are sufficient."[34] Additionally, more work needs to be done in forecasting potential flexible capacity needs and the CAISO plans to assess flexibility needs by studying the years 2018, 2021 and 2024.[35] However, it is unlikely that the effects of uncertainty will be minimized before 2017 through the improvement of forecasting methods and flexible RA requirements. Therefore, the adoption of multi-year flexible requirements ahead of clearly defined flexible attribute needs could result in procurement that does not meet needs.

Rather than creating three-year forward requirements while flexible studies and refinements are being developed, it would be prudent to defer consideration of the need for flexible capacity multi-year requirements until 2017. By 2017, the studies and refinements should be completed, thereby decreasing the potential for regulatory uncertainty that imposes unnecessary costs on ratepayers.

---

[32] Staff Proposal, p. 36.

[33] Staff Proposal, p. 41.

[34] Staff Proposal, p. 11.

[35] I Staff Proposal, p. 11.

7. What method could be used to ascertain the ratepayer cost from additional forward procurement for each proposed option in section III?

Ratepayer costs from additional forward procurement can be calculated as the product of additional incremental RA capacity that would need to be procured by each CPUC-jurisdictional LSE and the forecasted RA capacity price adjusted by the estimated price elasticity of additional procurement. The additional incremental RA capacity that would be procured for each RA product is the difference between the newly imposed RA obligations for each year and the amount of RA capacity that is already under contract by the LSEs. Forecasted RA capacity prices for years two and three would need to be adjusted by a price elasticity assumption because any additional capacity procured on the forward basis by one LSE could potentially impact RA capacity prices upward for other LSEs by limiting the available supply in the market. In addition, a publicly known mandate to procure forward capacity would likely allow suppliers to extract higher capacity prices.

Due to the fact that the current year-ahead RA program results in significant forward procurement beyond the one-year requirement, it is reasonable to assume that a three-year forward RA program would result in forward procurement beyond the three-year timeframe for hedging purposes. Therefore, additional costs would result from this procurement beyond the required timeframe. The cost from additional forward procurement would need to be adjusted for the time value of money to determine the additional costs in today's dollars. Therefore, any additional forward procurement costs in years two and three and beyond would need to be multiplied by an appropriate discount factor to obtain the present value of those costs.

III. CONCLUSION

ORA's Risk of Unplanned Retirement analysis and PLEXOS Production Cost Simulation study do not currently indicate that there are any generation resources that are both at risk of unplanned retirement and critical for reliability in the medium term. The oversupply of both available and contracted capacity for the next three years along with the results of ORA's Risk of Unplanned Retirement analysis and PLEXOS Production Cost Simulation study indicate that adopting multi-year RA requirements at the present time is unnecessary. While it is too early to conclude that the new flexible RA requirements are sufficient to encourage the retention of the existing flexible resources that will be needed in the next ten years, the Commission should re-evaluate the need for multi-year flexible RA requirements in 2017, when the definition of

flexible capacity requirements will be more settled and the effectiveness of new RA requirements will be more apparent.

Respectfully submitted,

/s/ DIANA L. LEE

Diana L. Lee
Attorney

For the Office of Ratepayer Advocates

California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Telephone: (415) 703-4342
Fax: (415) 703-2262
Email: Diana.Lee@cpuc.ca.gov

October 30, 2014