BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

FILED
12/18/20
04:59 PM

Order Instituting Rulemaking to Oversee the Resource Adequacy Program, Consider Program Refinements, and Establish Forward Resource Adequacy Procurement Obligations.	Rulemaking 19-11-009 (Filed November 7, 2019)

COMMENTS OF POWEREX CORP. ON ASSIGNED COMMISSIONER'S AMENDED TRACK 3B.2 AND TRACK 4 SCOPING MEMO AND RULING

POWEREX CORP.
Mike Benn, J.D., B.ASc.
Energy Trade Policy Analyst
Suite 1300 – 666 Burrard Street
Vancouver, BC V6C 2X8
Telephone: (604) 891-6074
Email: mike.benn@powerex.com

Vidhya Prabhakaran
Tahiya Sultan
Davis Wright Tremaine LLP
505 Montgomery Street, Suite 800
San Francisco, CA 94111-6533
Tel. (415) 276-6500
Fax. (415) 276-6599
Email: vidhyaprabhakaran@dwt.com
Email: tahiyasultan@dwt.com

Attorneys for Powerex Corp.

December 18, 2020

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Oversee the Resource Adequacy Program, Consider Program Refinements, and Establish Forward Resource Adequacy Procurement Obligations.	Rulemaking 19-11-009 (Filed November 7, 2019)

COMMENTS OF POWEREX CORP. ON ASSIGNED COMMISSIONER'S AMENDED TRACK 3B.2 AND TRACK 4 SCOPING MEMO AND RULING

Pursuant to the December 11, 2020 *Assigned Commissioner's Amended Track 3B and Track 4 Scoping Memo and Ruling*, Powerex Corp. ("Powerex") submits these proposals and comments respecting Track 3B.2 of this proceeding.

The California Independent System Operator's ("CAISO") experience during the August heat wave has highlighted the pressing need for the California Public Utilities Commission ("Commission") to take immediate steps to ensure that the Resource Adequacy ("RA") program achieves its objective of committing sufficient supply on a forward basis to allow CAISO to operate the grid reliably. This includes preventing California load-serving entities ("LSEs") from relying on import RA contracts that are not backed by a forward commitment of physical capacity and transmission ("paper capacity") to meet their RA obligations.

As explained in Powerex's August 7 comments, Powerex strongly supports CAISO's proposal to modify import RA requirements to prevent external marketers from selling paper capacity to California LSEs.[1] CAISO's proposed changes to the import RA framework would help achieve this result by requiring verification that all import RA contracts are backed by a forward commitment of genuine physical supply and transmission rights sufficient to ensure deliverability. The Commission should use this proceeding to align its import RA requirements with CAISO's proposal in advance of summer 2021. As discussed further herein, the

[1] *See* Comments of Powerex Corp. on Track 3.B Scope (August 7, 2020).

Commission should also use this proceeding to address other elements of the existing RA framework that are preventing it from achieving its objectives. In particular, the Commission should:

1. Shift to the use of a seasonal System RA requirement to ensure that California LSEs are able to more effectively compete with external LSEs to obtain forward commitments of the physical supply necessary to meet reliability needs;

2. Increase the penalties associated with RA deficiencies to ensure that LSEs do not view noncompliance with RA requirements as an "economic option"; and,

3. Implement a framework to protect against the reliability risks associated with the "double counting" of capacity.

I. The Commission Should Modify the RA Program to Require Seasonal Procurement

At the same time that California is experiencing supply challenges, numerous LSEs outside of California are also facing growing capacity challenges due to the continued retirement of existing fossil fuel resources. As a result, LSEs inside and outside California are increasingly competing with each other to obtain forward commitments of the limited surplus supply that remains available. To address these challenges, the Commission should expect LSEs *outside* of California to turn to seasonal, yearly, and multi-year commitments with suppliers in regions, such as the Pacific Northwest, that continue to have excess supply available.

Thus, the Commission should modify the RA program to ensure that California LSEs are able to compete more effectively to obtain forward supply commitments. At minimum, the Commission should modify the System RA framework to require California LSEs to meet RA requirements on a seasonal basis—i.e., with contracts that cover a minimum of the entire summer season—and to demonstrate that they have complied with this requirement on a year-ahead basis. Adopting a seasonal System RA requirement would have several advantages over the existing framework:

- *Alignment with External LSE Longer-Term Purchases* – The use of a seasonal framework for the duration of the System RA requirements will enable California LSEs the flexibility to match the longer-term purchases external LSEs are executing. This will help reduce the likelihood that California LSEs will be "last in line" and unable to

obtain forward commitments of the external capacity needed to meet California's reliability needs.

- *Reduction in Forecasting Errors* – Establishing a seasonal procurement requirement would also reduce the risks associated with forecasting errors in the precise month in which the summer peak load in California occurs. In recent years, actual system peak demand has fallen outside of the same month as the forecast peak. This misalignment between a monthly forecast of demand and actual system needs is increasing reliability risks and exacerbating the supply challenges facing CAISO. Moving to a framework that requires LSEs to procure sufficient capacity to meet seasonal peak load would help mitigate these risks by ensuring that CAISO has the capacity necessary to meet system needs across the summer period.
- *Regional Diversity in Peak Load Between Seasons and Reduction of Costs* – Enabling a seasonal rather than a full year-long contract will allow California LSEs and California ratepayers to benefit from regional diversity in peak load between California's summer-peaking system and those external entities that experience a peak load in the winter. Such a framework would ensure that California LSEs can take advantage of this regional diversity and reduce the total costs of meeting California's reliability needs.

II. The Commission Should Strengthen the Penalties Associated With RA Deficiencies

To ensure the success of the RA program, California LSEs must not have an "economic option" to forego procuring the capacity necessary to meet System RA obligations. In other words, the Commission must ensure that the consequences associated with non-compliance are sufficiently severe such that LSEs would never choose to fail the RA program's showing requirements. Otherwise, California LSEs may simply elect not to procure capacity when the cost of doing so exceeds the penalties that they will face due to an RA deficiency.

The existing penalties associated with System RA deficiencies are inadequate to deter California LSEs from making the economic choice not to commit the capacity necessary to meet reliability requirements. Currently, the financial exposure of a California LSE that fails to commit sufficient capacity during peak months is limited to the sum of: (1) the Commission's deficiency penalty of $8.88/kW-month;[2] and (2) an allocation of the costs of procuring backstop capacity through CAISO's Capacity Procurement Mechanism ("CPM"), which is limited by the

[2] 2021 Filing Guide for System, Local, and Flexible Resource Adequacy Compliance Filings, R.19-11-009 at 41 (issued Oct. 2, 2020).

CPM soft offer cap reflecting 1/12 of the annual going forward costs of a hypothetical thermal resource ($6.31/kW-month). In practice, this means that a California LSE will be discouraged from bearing RA costs greater than approximately $15.19/kW-month to meet its System RA requirements. In light of the tightening conditions across the West and the increasing competition between California LSEs and external LSEs for limited surplus, there is an increasing probability that California LSEs will choose to pay the deficiency penalty during critical months. To make matters worse, CAISO's reliance on monthly commitments through its CPM framework, with compensation at the monthly soft offer cap, limits its ability to compete to commit the capacity necessary to address RA deficiencies, serving to further increase reliability risks.

Comparing the penalties applied to a California LSE with the penalties applied to LSEs participating in the Southwest Power Pool ("SPP") market highlights the inadequacy of the existing RA deficiency framework. Like CAISO, SPP relies on a bilateral contracting framework to ensure that it has access to the resources necessary to operate its grid reliably. However, rather than relying on last-minute backstop procurement mechanisms to resolve capacity shortfalls, SPP ensures that LSEs comply with their RA contracting obligations upfront by applying robust consequences to any LSE that fails to meet its requirement. Specifically, SPP will assess LSEs that fail to meet their summer resource adequacy requirements deficiency charges based on:

- The *annual* cost of capacity, rather than 1/12 of the annual cost;
- A capacity cost based on the *full* cost of new entry ("CONE"), rather than only the "going forward" costs included in the CAISO soft offer cap; and
- A penalty factor that ranges from 125% to 200% depending on the overall level of reserve margin within the market.

The Commission should use this proceeding to modify the RA deficiency framework to ensure that LSEs have an economic incentive to commit the capacity necessary to meet System

RA requirements. More specifically, the Commission should modify its penalties to reflect at least the full annualized CONE—or even a reasonable multiple of CONE—consistent with the approach used in SPP.

III. Additional Safeguards Are Necessary to Verify That Capacity Supporting RA Commitments Have Not Been Committed to Meet Other Needs

Numerous parties have explained the reliability risks associated with import RA contracts that are not backed by physical supply in this proceeding. It is important to recognize, however, that the reliability risks associated with paper capacity are not limited to instances where a supplier does not have the physical supply necessary to meet its commitment. To the contrary, even where an import RA contract is backed by physical supply, there is a risk that import RA resources may fail to perform to the extent that the supply supporting the contract is also being relied upon to meet the sellers' forward commitments to other regions. Unfortunately, the RA program lacks any framework to ensure that the resources backing import RA commitments are not being relied upon by the seller to also meet the reliability needs of other regions—creating the risk that deliveries to California may be curtailed if and when such capacity is needed by the seller for another purpose.

Experience with import supply this summer suggests that there continue to be import RA suppliers that may be entering into commitments that far exceed the quantity of supply they have secured in advance to meet their obligations. For instance, from its review of publically available information, Powerex believes that it is likely that a material portion of the exports to the Southwest that were curtailed by CAISO during the August heat wave were associated with marketers that made advanced sales to both regions (i.e., prior to the CAISO day-ahead market), for a total quantity that exceeded the quantity of supply those entities had actually secured in advance. In some cases, these marketers may have been scheduling imports into the CAISO BAA—including to meet their forward firm energy and/or standalone RA must-offer

commitments—while simultaneously attempting to export energy in the same hours from the CAISO BAA to meet their advanced sales commitments to external Southwest LSEs.

The failure to verify that forward purchases are supported by real, physical supply that has not been "double counted" increases the risk that the capacity committed to meet RA requirements may not be available and capable of performing when needed by CAISO. Importantly, this is not a matter of other regions leaning on the capacity that has been committed to meet the needs of California; to the contrary, where both California LSEs and external LSEs have not taken sufficient steps to verify that the capacity supporting a commitment has not been committed elsewhere, it is unclear whether the California LSE or the external LSE should have priority to the associated supply. What is clear, however, is that the there is no current framework to ensure that the supply supporting an import RA contract is exclusively to meet the CAISO's needs. This gap is increasing reliability risks and further exacerbating the supply challenges facing CAISO.

The Commission should use this proceeding to modify import RA requirements to prevent the double counting of capacity. At minimum, the Commission should require that any import RA requirement must include a representation that the physical generation capacity (or system resources) supporting the import RA contract is both surplus to the needs of the source balancing authority area and has not been committed to any other balancing authority area or LSE.

Respectfully submitted,
/s/

Vidhya Prabhakaran
Tahiya Sultan
Davis Wright Tremaine LLP
505 Montgomery Street, Suite 800
San Francisco, CA 94111-6533
Tel. (415) 276-6500
Fax. (415) 276-6599
Email: vidhyaprabhakaran@dwt.com
Email: tahiyasultan@dwt.com

December 18, 2020

Attorneys for Powerex Corp.