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BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Continue Electric Integrated Resource Planning and Related Procurement Processes	Rulemaking 20-05-003 (Filed October 5, 2023)

REPLY COMMENTS OF THE NATURAL RESOURCES DEFENSE COUNCIL ON ADMINISTRATIVE LAW JUDGE'S RULING SEEKING COMMENTS ON NEED AND PROCESS FOR CENTRALIZED PROCUREMENT OF SPECIFIED LONG LEAD-TIME RESOURCES

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I. Introduction and Summary

The Natural Resources Defense Council (NRDC) submits these comments on Administrative Law Judge's Ruling Seeking Comments on Need and Process for Centralized Procurement of Specified Long Lead-Time Resources (henceforth known as "Ruling") filed on April 26, 2024. NRDC is a non-profit organization with more than 90,000 California members who have an interest in receiving reliable and affordable energy services while reducing their environmental impact and combatting climate change.

NRDC appreciates the robust effort the Commission has undertaken to establish a centralized procurement process and conduct cost-benefit analyses, and the thoughtful opening comments from other parties. A review of the opening comments reveals that parties are generally concentrated at both ends of a spectrum of what the Commission should establish as a need determination be for centralized procurement of offshore wind (OSW). In general, LSEs advocate for a lower need determination of 1-3 GW (or less), largely to minimize the risks of potential cost impacts on ratepayers. At the other end of the spectrum are parties advocating for a higher need determination, up to 10 GW, to provide sufficient market certainty to trigger investment and development of infrastructure necessary to support OSW. NRDC's suggested need determination of 5 GW by 2035, spread across both the northern California and central coast lease areas, balances all of these concerns. It should provide enough market certainty to spur development of OSW and its associated necessary infrastructure. At the same time, it leaves

some room for additional development in the existing lease areas in a more competitive manner to lower costs after an initial learning phase.

Many parties suggested establishing guardrails to further reduce the risk of cost overruns or other OSW industry challenges. Examples of guardrails put forward include an offramp, cost caps, and other mechanisms. NRDC is supportive of mechanisms that encourage price competition, but only if designed in a smart way that does not create insurmountable barriers for the OSW industry to establish itself in California. The suggestion for an offramp so the Commission can reverse course on OSW if costs are too high could, for example, could lead to sunk costs if the offramp option is invoked after significant other investments have been made. Establishing a public cost cap would likely lead to the clustering of bids just below a cost cap, or be too low and prevent any developers from being able to bid at that level. NRDC supports a cost cap only if kept confidential and developed through a process that incorporates the costs of alternate resources, the value of developing a market for new diverse energy resources, the future expectations of energy costs, and uncertainty in the bidding process.

NRDC's main objective is to create a competitive market for OSW through a sizeable initial investment, along with mechanisms to help reduce costs and promote competition over time. To that end, NRDC's overarching recommendations for centralized procurement are summarized as follows:

- The Commission should adopt an initial need determination of 5 GW of OSW spread across both lease areas by 2035.
- The Commission should update its cost-benefit analysis for OSW to incorporate the full life of the project, IRA incentives, model additional discount factor sensitivities, and fully account for economies of scale within a lease area. These elements do not appear to currently be captured in the analysis, likely leading to underestimation of the benefits of centralized procurement.
- The Commission should clarify that fossil or hydrogen-based electricity generation, including gas with carbon capture, are not resources eligible for centralized procurement under the AB 1373 statute.
- The Commission should consider adopting a confidential cost cap for OSW to encourage competitive bidding.

- The Commission should use non-ratepayer money as much as possible for investment in infrastructure needed for OSW development.

NRDC believes that establishing an initial 5 GW by 2035 need determination and these additional procurement policies will allow the OSW industry to develop, demonstrate, and lower costs, ultimately contributing to meeting the state's 25 GW by 2045 planning goals.

II. Discussion and responses to select questions

NRDC understands cost cap to mean the price over which a resource will not be procured. Cost caps can be designed in different ways, and can be public or confidential. NRDC supports using a confidential, pre-determined cost cap to promote competitive bidding in the OSW central procurement solicitation process. Confidential cost caps, in which the Commission would set a threshold cost based on various factors but not disclose that number to market participants, are a commonly used feature in procurement bidding. They can increase competition in markets where there may be few bidders and an additional incentive is desired to drive bidders to submit competitive bids that reflect the bidders' actual costs.[1] Given the relatively small California OSW market size, establishing a confidential cost cap is one way to promote competition in the bidding process.

As noted, it is crucial to design a cost cap in a careful way to avoid the significant concerns detailed in the opening comments. Here we summarize some potential pitfalls of establishing certain types of cost caps and the proposed solutions:

Publicly Disclosed cost caps create a focal point for bidders to bid directly below the cap:[2] This is a known pitfall of publicly disclosing caps. NRDC only supports the use of confidential cost caps.

Cost caps may result in no successful bids or limited bidding:[3] While cost caps do impose risks that no bid will be successful, the level at which they are set will increase or decrease the

[1] Cleary, K., & Ratz, H. B. (2021). *Experience with Competitive Procurements and Centralized Resource Planning to Advance Clean Electricity*. Working Paper. Washington, DC: Resources for the Future. https://www.rff.org/publications/working-papers/experience-with-competitive-procurements-and-centralized-resource-planning-to-advance-clean-electricity.

[2] See Public Advocates Office at the California Public Utilities Commission comments on Rulemaking 20-05-003 (May 24, 2024), p. 28.

[3] See American Clean Power comments on Rulemaking 20-05-003 (May 24, 2024), p. 29.

potential for eliminating bids. The confidential cost cap should be flexible and set on the Commission's best understanding of the aggregate costs of alternate resources that LSEs would have to procure if OSW wasn't procured, and also consider other factors such as the hard-to-monetize value of developing a market for new diverse energy resources, future expectations of energy costs, and uncertainty in the bidding process.

Cost caps are redundant as DWR and the Commission reviews can eliminate high bids:[4] While DWR and Commission review can evaluate the bids, without a set confidential cost cap, that review is unlikely to serve the purpose of incentivizing bids at the actual costs. While potentially a minor concern with the bidding and solicitation process, bidding at actual cost has been problematic in past procurements in other locations.[5]

It should be noted that a well-designed cost cap goes some way towards addressing many of the concerns of what PAO termed "market power" in the bidding process.[6] In these opening comments, they suggest that due to the low number of bidders and limited lease sites, bidders could potentially inflate bids above their actual costs. However, this is more likely due to the increased probability of noncompetitive bidding amongst the relatively small number of bidders who may be able to coordinate bids above their actual cost of providing the resource. A confidential cost cap would provide some counteracting force against inflated bidding while not providing the same focal point as a disclosed cap, which they have argued against.

2. Should other resource types (beyond OSW, OOS wind, geothermal, and LDES) also be considered for centralized procurement through DWR at this time? Provide rationale if you suggest other resources should be included.

UCS requested the Commission to clarify that it has no intention to and is statutorily prohibited from using DWR central procurement mechanism to procure gas with CCS.[7] NRDC agrees that gas plus CCS is not eligible for central procurement based on the SB 1373 statute and that the Commission should clarify that point.

[4] See American Clean Power comments on Rulemaking 20-05-003 (May 24, 2024), p. 3.
[5] IRENA and CEM (Clean Energy Ministerial). 2015. Renewable Energy Auctions: A Guide to Design. https://www.irena.org/-/media/Files/IRENA/Agency/Publication/2015/Jun/IRENA_Renewable_Energy_Auctions_A_Guide_to_Design_2015.pdf.
[6] See PAO comments on Rulemaking 20-05-003 (May 24, 2024), p. 10.
[7] See UCS comments on Rulemaking 20-05-003 (May 24, 2024), p. 2.

6. Comment on the cost-benefit analysis conducted, including the analysis presented in the slide deck posted on the Commission's web site. Does the analysis serve as a reasonable basis for a need determination? Specify how and why.

In addition to the points NRDC included in opening comments, the cost-benefit analysis also does not appear to capture the benefit inherent to centralized procurement of there being one buyer and many sellers, as opposed to typical contracting done in a bilateral way. As TURN argues, "Selling the entire output of a large project to a single centralized creditworthy buyer reduces risk to the developer, minimizes transaction costs, and can lead to lower overall pricing.[8] Moreover, the absence of competing buyers under a central procurement model can place additional pressure on developers to offer cost-based (rather than opportunity cost-based) pricing." These are important points that further support the benefits of centralized procurement.

8. What need determination for centralized procurement should the Commission make before the September 1, 2024 AB 1373 deadline and why? Specify which resource types, in what amount, and by when.

NRDC still recommends that the Commission make a need determination of 5 GW of OSW by 2035 spread across both call areas. Multiple parties, including the IOUs and the CCAs, incorrectly recommend smaller targets of around 1 GW. The problem with a target this small is twofold: it is cost-ineffective and doesn't achieve California's broader policy goals.

As explained in NRDC's opening comments, Commission's cost-benefit analysis is likely conservative because it doesn't completely account for factors like the full timeline of resource life, sensitivity to discount rates, and economies of scale in building infrastructure for OSW, among others. Infrastructure for OSW, especially transmission and ports, displays large economies of scale; i.e., the additional costs of building slightly more transmission and port capacity are much smaller than the costs of building capacity to install the first few-hundred MW of OSW. Building too little OSW, especially when CAISO is already planning for transmission buildout to two call areas, risks making the whole endeavor cost ineffective.

Inherent to California's broader policy goals is developing competitive markets and creating knowledge for new clean energy resources. A competitive market for OSW, once developed, will benefit California's ratepayers and workforce for decades to come. However, developing that

[8] See TURN comments on Rulemaking 20-05-003 (May 24, 2024), p. 2.

competitive market requires an initial investment in the order that NRDC recommends while ensuring that each call area has enough transmission capacity to accommodate additional OSW through competitive bidding.

Knowledge creation through California's initial investments in clean energy is a worthy and necessary policy goal. California's power sector has an outsized impact in fighting climate change not (solely) because of the GHGs that California has reduced, but because of the creation of knowledge and new markets for clean energy that everyone benefits from.

IV. Conclusion

NRDC appreciates the Commission's work in establishing a process for central procurement and its consideration of our views.

Respectfully submitted,

Dated: June 5, 2024

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