

## Stakeholder Comments Template

| Submitted by | Company | Date Submitted |
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| Mark J Smith | Calpine | August 7, 2018 |

### **Summary:**

Calpine appreciates the opportunity to comment on the CAISO’s plan to review the RMR and CPM process. We continue to believe that capacity compensation and the CAISO’s use of backstop must be viewed holistically, and that the CAISO has the necessary and independent authority within the four corners of its tariff to make substantive and beneficial changes to efficiency and effectiveness of overall capacity commitment and compensation. In this regard, we refer to Calpine’s presentation of May 30<sup>th</sup>, attached, which recommends comprehensive changes to the Resource Adequacy timeline and CAISO’s backstop auction. These proposals facilitate a multi-year forward RA requirement, enforcement of local sub-areas, create a reasonable runway for generation-owner retirement/operating decisions and affirmatively places the CAISO in the position of a central buyer for unmet reliability needs. While Calpine is concerned that the CAISO has deferred decision-making on these matters to the CPUC, Calpine appreciates that the CAISO has reflected many of these positions in its comments in the CPUC RA dockets.

With that, we offer the following comments on the CAISO’s more-narrow proposals to reform RMR and CPM.

## **RMR and CPM**

- a. Provide notification to stakeholders when a resource informs ISO it is retiring

### **Comments:**

Calpine supports pro-active resource-owner communications with the CAISO, particularly with respect to asset disposition. Calpine will continue to keep the CAISO informed whenever the ongoing near-term operation of a generation resource is in question. However, it is unlikely that final decisions on the disposition of the hard assets (e.g., “retirement”) would be made prior to such notifications. Therefore, such notifications may indicate that the asset is being made “unavailable for dispatch” and may be seeking retirement, decommissioning, mothballing, repowering, replacement, or other options. Calpine will not object if the CAISO releases the notice of potential unavailability publicly, but believes that any prospective plans (e.g., redevelopment, repowering, decommissioning) should be held confidential until the resource-owner decides to make them public (e.g., by filing at the CEC).

We do note, however, that multi-year forward contracting requirements may reduce the frequency of these notifications as resources will know, much further in advance, their contractual status.

- b. Clarify when RMR procurement is used versus CPM procurement

### **Comments:**

Calpine believes that RMR should be a last-gasp reliability tool. It should be used when unforeseen circumstances arise that drive to a long term reliability need for a resource. However, significant reforms of the RA timeline and degree of forward contracting are necessary to achieve this vision as a last-gasp tool.

The current timeline for resource-owner decision-making has forced the CAISO to appropriately use RMR well in advance of decisions made in the RA and CPM

processes (note the recent authorizations by the CAISO Board for Moorpark NRG assets). At least three things are needed to make RMR a true backstop.

First, a longer runway for decision-making must be in place. Calpine would support independent action by the CAISO (if necessary) to adjust annual RA timelines to provide a reasonable runway for CPM to operate as designed. We would support either our initial proposal to move forward the RA “showings” to June, or the CAISO’s proposal submitted to the CPUC to leave “showings” in October, but slide the start-date of the compliance to April. In addition to moving the process timeline, a multi-year forward requirement would assist in creating more efficient retirement and decommissioning process.

Second, there must be a Central Buyer established to procure capacity that is needed, including sub-area local requirements, but not contracted. Calpine believes that as the reliability agent, the CAISO must be the buyer of last resort and it is inefficient and unnecessary to have another entity assume this role.

Third, as described in our presentation of May 30, the ISO should consider changes to the Competitive Solicitation Process to facilitate efficient procurement with the CAISO as the Central Buyer.

These three elements would position CPM / CSP as the primary backstop to bilateral transactions and RMR as merely a circuit-breaker when all else fails. Each of these elements is currently under consideration by the CPUC, but could be implemented squarely within the four corners of the CAISO tariff. The CAISO appears to have designed this stakeholder initiative schedule to allow for the incorporation of any CPUC decisions in its final design proposal (currently scheduled to be circulated in early 2019). However, we encourage the ISO to consider independent and autonomous action to implement these provisions, as necessary.

- c. Explore whether Risk of Retirement CPM and RMR procurement can be merged into one procurement mechanism

**Comments:**

Calpine supports the elimination of CPM RoR, and the retention of RMR.

- d. Evaluate compensation paid for RMR and CPM services

**Comments:**

The CAISO proposes several changes to the compensation for CPM. As a first principle, Calpine believes that resources required for reliability, but not otherwise contracted must have, pursuant to foundational court decisions on regulatory economics (*Hope, et. al.*) a reasonable opportunity to recover their costs-of-service including a return of (depreciation), and on (rate of return), its investment.

In this regard, the CPUC Staff has raised a question whether CPM should allow for the filing of full costs-of-service when the resource-owner does not believe that the CPM soft cap provides sufficient compensation. In this regard, Calpine supports the existing tariff (that FERC has found to be just and reasonable) which provides the opportunity (but not the obligation) to seek “Schedule F” cost recovery.

However, we agree with the CPUC Staff that if in fact, an entity seeks “Schedule F” costs (Section 43A.4.1.1.1), the CAISO should reconsider the provision allowing the entity to retain market revenues as well as such full cost of service payments.

To address this issue the ISO proposes to limit the cost recovery for all types of CPM (and CSP bids) to going-forward-fixed costs (“GFFC”) plus 20 percent. The CAISO claims that this 20 percent adder should be sufficient to perform long-term maintenance or make environmental upgrades. We disagree. These “sufficiency” assertions are unfounded and unsupported by data or analysis. Calpine does not support this proposal, as it does not allow for a reasonable opportunity to recover significant major maintenance (such as the \$20 MM that forced our Metcalf facility to

seek alternative solutions) and, in direct conflict with *Hope*, to recover the full cost of service.

Rather, Calpine proposes that the resource owner should retain the right to file its full cost-of-service at FERC, but if they do seek recovery of costs above the soft cap, that any market revenues, must be returned to the CAISO. This makes the CPM compensation similar to that of an RMR condition 2 unit.

Finally, the CAISO proposes (at p17, section 6) that if a resource declines a CPM designation, unless told differently, it will assume the unit is available and it will use Exceptional Dispatch to commit that unit if a reliability need arises rather than considering RMR. An RMR would only be used if the unit owner submits a “retirement letter”.

Calpine views this proposal as an unjust and unreasonable free call-option. That is, the CAISO is relying on a unit to meet a defined reliability need (as proven by the CPM offer) but does not compensate the unit *a priori* for providing that service. Calpine proposes that if the CAISO affirmatively intends to use ED to meet otherwise unmet reliability needs that it adopt several complementary changes to yield a just and reasonable market structure: (1) that the uncontracted portion of the unit has no must offer obligation even though the ISO deems the unit as “available”; (2) that the energy bids of that unit are *not subject to local market power mitigation* (bid caps still apply); (3) if dispatched, the unmitigated bids are allowed to set the LMP and (4) if dispatched, the ISO would be obligated to compensate that resource at CPM or its FERC-filed rates.

## **RMR**

- e. Develop interim pro forma RMR agreement, i.e., change termination and re-designation provisions

### **Comments:**

Calpine still sees no need for these piecemeal changes. Nonetheless, we appreciate the CAISO's pledge that the CAISO's unilateral and interim termination provision will not be a part of the changes to the pro-forma contract submitted at the conclusion of this initiative.

- f. Update certain terms of pro forma RMR agreement
  - i. Remove AS bid insufficiency test and revise dispatch provisions to align with current market design

### **Comments:**

Calpine believes that any modification to AS bid insufficiency tests, or more generally, modifications to Section 4.1 ("CAISO's Rights to Dispatch") must be coordinated with (1) the must-offer obligations (if any), (2) the continuing existence of Condition 1 and Condition 2 and (3) any related the market power mitigation.

In particular, we continue to believe that RMR and RA are dissimilar products. To avoid price suppression, RMR Condition 2 units (particularly) should have no ubiquitous must-offer obligation and bids should be inserted and the unit should be dispatched only when reliability requirements demand its operation. As such, the "bid insufficiency test" may still be a necessary trigger for RMR dispatch.

- ii. Update Schedule M and Schedule C to include GHG compliance cost calculation, DAM and RTM gas price index, and updated SC charge calculation

**Comments:**

Calpine supports changes to the RMR schedules that represent undeniable variable costs of operations such as those suggested above. As such, GHG costs must be included as well as any necessary modifications to represent current gas-price indices and GMC charges. In addition, we support the CAISO developing a bid insertion tool, particularly for units under Condition 2. For these units, which recover their full costs of service, Calpine does not object to insertion of variable-cost-based bids when the unit is needed for a defined reliability event.

- iii. Update Schedule M to be consistent with bidding rules in ISO tariff and BPM

**Comments:**

See comment above.

- iv. Seek input on defining a heat rate curve formula in Schedule C for multi-stage generator resources

**Comments:**

Calpine supports, above all, consistency in the formulations of bid components between the contract and Masterfile. In particular, since the Masterfile contains the parameters used in market-clearing optimizations, Calpine supports the primacy of those Masterfile values. We are not convinced that Schedules A, C or M need to duplicate (as in schedule C1-7a, heat rates) any of the line items that are contained within the Masterfile. While the contract must contain sufficient data to calculate an RMR “rate”, it seems more efficient that the Schedules merely refer to values embedded within the Masterfile.

- g. Update allowed rate of return on capital for RMR compensation

**Comments:**

Calpine does not believe a review of the pre-tax “allowed rate of return on capital” included in Schedule F of the pro-forma contract is necessary. Further review is unnecessary because (1) the current value yields and *after-tax* rate-of-return that is reasonable and (2) to Calpine’s knowledge, every single RMR contract ever approved by the Commission has been the result of extensive negotiation which allows the parties to make adjustments to the revenue requirement they deem reasonable.

However, if the CAISO pursues that review, it must first recognize the significant differences between the Schedule F, pre-tax rate-of-return and referenced after-tax values. The rate-of-return identified in Section 5 of Schedule F is an estimate of the *pre-tax* weighted-average, rate-of-return, and includes an adjustment should interest rates exceed those established in the original settlement. The Straw Proposal conflates pre- and post-tax values when it references California IOU’s *after-tax* return-on-equity, and *after-tax* cost-of-capital.

These two definitional “rates-of-return” are very different, as highlighted by Mr. Murtaugh verbally in the stakeholder meeting and subsequently with the Market Surveillance Committee. One cannot directly compare a 12.25 total *pre-tax* rate-of-return and a 10.57 *after-tax* return on equity without also knowing the project specific leverage, cost of debt, deferred tax implications, and tax rates. In fact, assuming California and Federal tax rates of 11 and 21 percent, respectively, a 12.25 *pretax* rate-of-return would yield only an 8.33 *after-tax*, rate-of-return ( $12.25 * (1 - (.11+.21))$  or 8.33 percent) before any further adjustments.

Even though Calpine believes the 12.25 percent pre-tax rate to be just and reasonable and needs no further consideration, Calpine cautions consideration of the refinement of a “proxy” after-tax, rate-of-return for RMR units. Doing so would require substantial changes to Schedule F, including the specific identification of tax rates and a revenue requirement “gross-up” representing the tax effects.

Of the proposals offered, we specifically and vigorously object to any obligation to establish, from a blank slate, an after-tax rate-of-return for each RMR on a case-by-case basis. This proposal would significantly increase the burden on both the resource-owner prior to filing and on the CAISO/PTO during RMR negotiations. In addition, it would require substantial modifications to the Schedule F.

- h. Make RMR resources subject to a must offer obligation

**Comments:**

As we have indicated in several comments, Calpine believes that a MOO applied to Condition 1 (where the unit-owner is depending upon market revenues) is complementary to the inherent incentives and therefore not objectionable. We also agree that in the case of Condition 1, the bids submitted by the unit owner can be at any level, subject only to bid caps.

However, we also believe that in the case of Condition 2 units, where a unit-owner is indifferent to market revenues because of the market revenue claw-backs, forcing the resource to bid at costs all hours would unduly suppress energy market prices. As such, we support bid insertion for Condition 2 units, but only when a reliability need is in evidence. FERC has found (in *Devon Power*) that use of RMRs, alone, has a deleterious effect on markets. A continuous must offer obligation multiplies those effects, particularly when the unit is not needed by any reliability requirement:

“[E]xtensive use of RMR undermines effective market performance. In addition, suppressed market clearing prices further erode the ability of other generators to earn competitive revenues in the market and increase the likelihood that additional units will also require RMR agreements to remain profitable.”

- i. Make RMR resources subject to the Resource Adequacy Availability Incentive Mechanism

**Comments:**

Calpine agrees that RMR resources should have availability incentives. RAAIM is an example of an incentive which creates both rewards for and penalties associated with the economic bidding process. It only indirectly encourages physical availability (that is, if a unit is forced out, it cannot bid.) Tailoring this mechanism to an RMR is incongruous and would require changes to the long-delayed and technically detailed RAAIM process.

First, an RMR *must* self-schedule when the market does not support operation, but the unit is required for reliability. Because it is not considered an economic bid, a self-schedule would unjustly expose the resource-owner to penalties when complying with an ISO Dispatch Order. Second, to the extent that bid-insertion is in place during hours of need, a resource-owner could receive RAAIM incentive payments (for high availability) in addition to other fixed cost recovery. Moreover, unlike an RA unit, an RMR unit has no ability to substitute in order to manage or avoid RAAIM.

Calpine believes that the incentives in the current RMR pro-forma are better tailored to RMR units. In fact, the current Section 8.5 (Schedule B) Availability Charges have a direct and immediate effect on capacity payments if a unit experiences outages beyond those considered and negotiated as part of the agreement.

Under no circumstance would Calpine support exposure to both RAAIM and the pro-forma's Availability Charges.

- j. Consider whether Condition 1 and 2 options are needed for RMR

**Comments:**

Calpine sees no reason to eliminate Condition 1, especially given that the CAISO proposes the discretionary right to allow Condition 1. We also support the continued availability of Condition 2 and the unit-owner’s discretion to choose between the two options.

- k. Ensure RMR designation authority includes system and flexible needs

**Comments:**

Calpine supports the CAISO’s proposal to use RMR to designate any resource at any time. As the fleet of gas-fired resources is systemically culled, virtually all remaining resources will be needed to meet some reliability requirement. Calpine supports the proactive expansion of the CAISO’s designation authority to include both System and Flexibility needs. This expansion of authority, while important, would be exercised highly infrequently if Calpine’s holistic reforms are implemented and RMR becomes the “last gasp” alternative.

- l. Allocate flexible RA credits from RMR designations

**Comments:**

Calpine supports an allocation of all attributes (flex, local or system) of backstop contracts to loads, based, in the first instance, on unmet requirements or purposeful short-positions and second, on actual load ratio shares.

- m. Streamline and automate RMR settlement process

**Comments:**

Yes. Please.

- n. Lower banking costs associated with RMR invoicing

**Comments:**

Yes. Please.

## **CPM**

1. Evaluate year-ahead CPM local collective deficiency procurement cost allocation to address load migration

### **Comments:**

See above. Allocations should be based on deficiency, first, then based on actual load ratio shares.

2. Evaluate if load serving entities are using CPM for their primary capacity procurement

### **Comments:**

Calpine understands that several LSEs in the San Diego load pocket sought waivers of the local requirements, and that ultimately CPM was used to acquire capacity. We agree with the ISO that these events do not constitute a cause for opening the CPM settlement or pricing conditions.

## **Other Comments**

Please provide any additional comments not associated with the items listed above.

### **Comments:**

None at this time.

Thank you.