Stakeholder Comments Template

Subject: Capacity Procurement Mechanism, and Compensation and Bid Mitigation for Exceptional Dispatch

Submitted by	Company	Date Submitted
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Summary of PG&E's Comments

- PG&E supports a durable Capacity Procurement Mechanism (CPM) mechanism with an automatic mechanism for updating the CPM compensation.
- Supports the proposed $55/kW-yr compensation rate for CAISO procured backstop capacity.
- PG&E does not support expansion of CPM to include payments to generators at risk of retirement to stay online.

CPM - Detailed Comments

1. **Whether the tariff provisions should have a specific sunset date or be open-ended.**

   PG&E supports adoption of a durable backstop procurement mechanism with an automatic mechanism for updating the CPM compensation.[1]

2. **The ability to procure capacity for planned transmission and generator outages or sustained, significant less-than-planned-output of intermittent resources.**

   The CAISO argues that these two types of CPM procurement are authorized under its current tariff authority because they fall within the scope of its definition of "Significant Events". Specifically, the CAISO argues that a maintenance outage of a significant RA resource could constitute "material change in system conditions" and lower than expected

[1] The CAISO proposes to raise the CPM price from $41/kW-year to $55/ kW-year. The new price would be in effect for the period April 1, 2011 through December 31, 2012 and would be updated for the period January 1, 2013 through December 31, 2014. The price would subsequently be updated every two years to be effective on a calendar year basis.

output from an intermittent resource could constitute "a material difference from what was assumed in the RA program".[2]

While PG&E can see how planned transmission and generator outages or sustained, significant less-than-planned-output of intermittent resources could constitute a CPM Significant Event, we have concerns about the CAISO's broad authority to procure backstop capacity for these two types of events. For example, it's not clear to us what constitutes "less-than-planned" output or how many days does the resource have to be underperforming before the CAISO decides to purchase backstop capacity.

PG&E is not requesting any action at this time from the CAISO to address this general concern. However, PG&E will be monitoring the level of backstop procurement and may request the CAISO take action if the CAISO begins to procure significant amounts of backstop capacity related to planned outages or output from intermittent resources.

3. **The proposed treatment of procured capacity that subsequently goes out on planned outage during the period for which the capacity has been procured.**

PG&E agrees with the CAISO that it is inappropriate to pay an Exceptionally Dispatched resource for 30 days of capacity if it goes on a planned outage. PG&E supports the CAISO's proposal that such a resource be paid the CPM compensation for 30-days minus the number of days within the 30-day period that the resource is on its planned outage.

However, the methodology described above does not capture planned derates in which only a portion (not all) of a resource's capacity is unavailable. PG&E recommends that the CAISO account for planned derates as well.[3]

4. **Modification of the criteria under section 43.3 of the CAISO tariff for selecting capacity from among eligible capacity.**

The CAISO proposes two additional criteria when deciding what resources to procure for backstop capacity[4]: (1) a preference for non-use-limited resources over use-limited resources, and (2) consideration of specific operational characteristics of the resources.

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[2] The CAISO's asserts that its Significant Event tariff authority allows it procure backstop capacity when a substantial event, or a combination of events, result in a material difference from what was assumed in the resource adequacy program for purposes of determining the Resource Adequacy Capacity requirements, or produce a material change in system conditions or in CAISO Controlled Grid operations, that causes, or threatens to cause, a failure to meet reliability.

[3] For example, if an Exceptionally Dispatched unit with a capacity of 500 MW experiences a planned derate of 100 MW for 15 days of a 30-day month, then the resource should be paid the full CPM payment for the first half of the month and 80% of the full CPM payment the second half of the month.

[4] Section 43.3 of the CAISO Tariff currently allows for the selection of backstop capacity based on the following criteria: 1) the effectiveness of eligible capacity at meeting criteria specified in Section 43.1, 2) the cost associated with the eligible capacity, 3) the quantity of a resource's available Eligible Capacity, 4) the effectiveness of eligible capacity at meeting zonal or local constraints. The CAISO wishes to modify the criteria in such a way that would result in the selection of resources with special operational characteristics as well as the selection of non-use limited resource over a use limited resource.

PG&E is not opposed to the CAISO modifying the criteria used to select resources that will receive CPM designation, as long as the duration of the contract remains 30 days. PG&E believes the inclusion of operational characteristics, such as ramp rates and Ancillary Service (AS) capability, may be appropriate criteria that should be used to select the resources that will provide backstop capacity. To the extent that two units are equally capable of providing this service, PG&E believes it is reasonable for the CAISO to choose the more flexible or operationally desirable resource. This will ultimately allow more value to be derived from the backstop capacity payment.

5. Procurement of capacity that is needed for reliability and is at risk of retirement.

The CAISO has put forward a proposal to offer one year of backstop capacity payments to resources at risk of retirement which it deems could be critical in the future (as indicated by a CAISO technical study). It is PG&E's position that such a payment is unnecessary because there are current programs in place at the CAISO and CPUC to address this risk. There is no reason to create a complex and redundant third program.

The CAISO states that it needs this procurement authority in order to maintain reliability. However, the current RMR process provides out of market payments to revenue constrained resources that are needed for reliability. Section 43.1 of the CAISO tariff states:

> *In addition to the Local Capacity Technical Study under 40.3.1, the CAISO may perform additional technical studies, as necessary, to ensure compliance with Reliability Criteria. The CAISO will then determine which Generating Units it requires to continue to be Reliability Must-Run Units, which Generating Units it no longer requires to be Reliability Must-Run Units and which Generating Units it requires to become the subject of a Reliability Must-Run Contract which had not previously been so contracted to the CAISO.*

However, the CAISO indicates it would prefer to use CPM over RMR, because CPM units have a must-offer requirement that can increase market liquidity. This justification to use CPM is inappropriate. The CPM backstop exists to address significant reliability events not to increase liquidity. Market liquidity issues should be addressed by other means. The CAISO has failed to show why RMR is inadequate to address the reliability issues created by a possible unit retirement.

Moreover, the CPUC's General Order 167 requires generators to notify the CPUC 90 days before it plans to shut down.[5] The CPUC can review the importance of retaining the unit to maintain system reliability. If it is deemed critical, the CPUC can require that an

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[5] The operating standard requiring notice before plant retirements and/or mothballing are in General Order 167, Operating Standards (OS) 22-24. OS 24 says that there must be a mechanism in place to compensate the plant for remaining online.

Investor Owned Utility (IOU) to sign a contract with a sufficient capacity value to keep the plant online.

It appears that CPUC General Order 167 as well as Section 43.1 of the CAISO tariff is specifically designed to address the reliability concerns created by a possible unit retirement. Therefore, PG&E sees no need to expand the CAISO backstop procurement authority by allowing it to provide these types of resources with an annual backstop capacity payment.

6. **The compensation methodology for resources procured under CPM and Exceptional Dispatch.**

PG&E strongly supports the CAISO's proposal to continue backstop capacity pricing based on going-forward fixed cost. In its January 18, 2008 Board Memo regarding its ICPM proposal, the CAISO described its decision to use the going-forward fixed cost proposal as the culmination of a lengthy and rigorous stakeholder process which attempts to strike a reasonable balance between the divergent views of stakeholders. The current proposal strikes a similar balance, and there is no need to change the methodology used to determine the price of backstop capacity.

The updated CPM rate of $55/kW-year seems reasonable based on the CEC study. The 10% adder and no deduction for energy rents should provide sufficient recovery of the fixed going-forward costs for almost all units.[6]

Some stakeholders argue that the CPM should be designed with the intent of incenting new investment in capacity. However, doing this would be inconsistent with the goals of the CPUC's procurement and reliability planning. The long-term reliability objective of facilitating development of new generating capacity is addressed by the CPUC's Long Term Procurement Plan (LTPP) the RA program in a manner that is consistent with PUC Code Section 380.[7]

In its August 23, 2010 stakeholder meeting, the CAISO correctly asserted that even if the backstop capacity price was based on the CONE, it would not incent investment in new capacity because CPM contracts usually last for only 30 days. This combined with the infrequency in which the CAISO relies on backstop capacity does not result in the necessary long-term revenues needed to incent investment.[8] The result of paying

[6] Additionally, if a resource that believes CPM price is insufficient, it has the opportunity to file at FERC for a higher price.

[7] Public Utilities Code Section 380 directs the CPUC to establish resource adequacy requirements applicable to investor-owned utilities and other load-serving entities in order to facilitate development of new generating capacity and retention of existing generating capacity that is economic and needed for reliability.

[8] According to Page 11 of the CAISO's Draft Final Proposal, as of August 16, 2010 backstop capacity was only procured 16 times since March 31, 2009.

backstop capacity a price based on the CONE only results in excessive payments without enhanced reliability or assurance of investment in capacity.

Exceptional Dispatch

1. **Linking compensation for Exceptional Dispatch to the CPM Payment.**

   PG&E does not see a need to change the current payment structure for Exceptional Dispatches.[9]

2. **Extending the existing bid mitigation.**

   Currently, the CAISO mitigates Exceptional Dispatches in the two following situations:

   - A supplier is exceptionally dispatched to address a contingency on a non-competitive transmission path.

   - A supplier is exceptionally dispatched to address the Delta Dispatch. As a result of environmental restrictions on certain resources in the Bay Area, the CAISO must manually dispatch combinations of resources in a particular order during the same period of time every year (i.e. the operator of some units known with a high degree of certainty that it will be dispatched regularly during this period, creating the potential for a very high price bid for energy, thus exercising market power).

PG&E strongly supports the continued mitigation to address the two circumstances described above because they deter uneconomic bidding during times when a resource is capable of or exercising market power.

[9] Resources without a capacity contract have a month-to-month choice between 1) accepting an ICPM designation and 2) earning hourly, bid-based compensation pursuant to the MRTU Tariff. Resources that choose Option 2, which is referred "Supplemental Revenue" option, are paid similarly to unmitigated resources until it receives revenues up to the level of the ICPM payment.