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January 31, 2012

25388-7

Mr. Honesto Gatchalian
Energy Division
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Re: **Draft Resolution E-4471**

Dear Mr. Gatchalian:

In accordance with the instructions set forth in the Energy Division's letter dated January 17, 2012, the following parties: Energy Users Forum ("EUF");[1] Alliance for Retail Energy Markets ("AReM");[2] Direct Access Customer Coalition ("DACC");[3] Retail Energy Supply Association ("RESA");[4] Marin Energy Authority ("MEA");[5] and Shell Energy North America (US), L.P. ("Shell Energy") submit their opening comments on the above-referenced draft Resolution ("DR"), which was issued by the Energy Division on its own motion. The DR recommends that the Commission direct the three investor-owned utilities ("IOUs") to enter into negotiations with Calpine Corporation ("Calpine") to offer a contract with the Sutter Energy

[1] EUF is an ad hoc group that represents the interests of medium and large bundled service and direct access (DA) customers in California, with locations in either investor-owned utility and/or municipal utility service areas, primarily taking service on rate schedules for accounts with demand above 100 kW.

[2] AReM is a California mutual benefit corporation formed by electric service providers that are active in California's direct access market. The positions taken in this filing represent the views of AReM but not necessarily individual members or the affiliates of its members with respect to the issues addressed herein.

[3] DACC is a regulatory alliance of educational, commercial, industrial and governmental end-use customers that utilize direct access for all or a portion of their electricity load requirements.

[4] RESA's members include: Champion Energy Services, LLC; ConEdison *Solutions*; Constellation NewEnergy, Inc.; Direct Energy Services, LLC; Energetix, Inc.; Energy Plus Holdings, LLC; Exelon Energy Company; GDF SUEZ Energy Resources NA, Inc.; Green Mountain Energy Company; Hess Corporation; Integrys Energy Services, Inc.; Just Energy; Liberty Power; MC Squared Energy Services, LLC; Mint Energy, LLC; NextEra Energy Services; Noble Americas Energy Solutions LLC; PPL EnergyPlus, LLC; Reliant and TriEagle Energy, L.P.. The comments expressed in this filing represent the position of RESA as an organization but may not represent the views of any particular member of RESA.

[5] MEA is the not-for-profit public agency formed by the County of Marin and the eleven towns and cities in Marin County that administers the Marin Clean Energy program.

Center ("Sutter") for a term that ends by December 31, 2012. The DR recommends that the CPUC approve the payment of up to $29.5 million in 2012 for the Sutter capacity.

The DR should be rejected for the following reasons:

1. Testing the Merits of Pseudo-Tie Agreements is Not a Sufficient Basis to Expend Millions of Ratepayer Dollars: The DR's rationale for spending up to $29.5 million of ratepayer money on capacity that is not needed for system (or local) reliability until 2017, at the earliest (see DR at p. 3), rests solely on the idea that having the Sutter plant remain in service will "provide valuable information" to the Commission, the CAISO and stakeholders regarding the role of pseudo-tie agreements in connecting to the grid using the CAISO's dynamic transfer tariff. DR at p. 7. Consideration of the "strengths, weaknesses and capabilities" of connecting to the grid through a pseudo-tie agreement does not justify the payment of up to $29.5 million to Calpine or to any other generator.

Moreover, it is not clear what the Sutter plant will add to the ongoing discussion regarding pseudo-tie and dynamically scheduled units as those discussions, for the most part, are dealing with issues associated with renewable resources – which Sutter is not. Finally, it is noteworthy that Calpine has initiated efforts at the WECC to reform its interconnection so that it will be directly connected to the CAISO, rather than connected through a pseudo-tie arrangement. The signatories to this filing have not been able to ascertain when that process may be completed, but even if the need exists to keep a pseudo-tie facility in place as a "test case" for modifications to pseudo-tie arrangements, Calpine's efforts to end its pseudo-tie arrangements call into serious question whether the Sutter plant would be a suitable candidate for that purpose.

2. The "Pick and Choose" Process Reflected in the DR Lends Itself to Potential Abuse: The DR states that the purpose of its recommendation is to keep the Sutter plant online in 2012. DR at p. 1. The DR states that Calpine has advised the Commission that it does not have an RA contract for 2012 and that "wholesale market revenues alone are insufficient to keep the plant in operation." DR at p. 4.

The DR fails to state whether the Commission or the Energy Division has confirmed that the Sutter plant will be retired in the absence of action by the Commission. Furthermore, the DR does not indicate the steps taken by the Energy Division to ascertain whether and how the Sutter unit was offered for RA capacity, and if so, why Calpine was unable to obtain an RA contract for the Sutter plant for 2012.

If the Commission is going to mandate that the IOUs enter into a capacity contract with a generation facility, the Commission must exercise due diligence in determining whether the owner offered the facility for RA and if so, the circumstances under which the owner did not --

or was not able to -- secure an RA contract. This process raises a further concern, however: The Commission's involvement in assessing the economic basis for a plant owner's inability to obtain an RA contract could have the unintended consequence of encouraging capacity owners to ignore the existing Capacity Procurement Mechanism ("CPM") process and seek a preferential payment as proposed through this DR.

Calpine's request could be the "tip of the iceberg" that would alter the strategy of some generators participating in the RA market. Approval of the DR could encourage arbitraging of market based activity against this "backstop" procurement alternative. The potential for this unintended consequence should be avoided.

3. Because No Near-Term Need Exists for the Sutter Plant Capacity, the Costs of Sutter Capacity Should Not be Borne by DA or CCA Customers: The DR recommends that the Commission find that the "identified need [for] the Sutter plant is system wide," and that "any benefits and costs should be applied via a non-bypassable charge to all benefitting customers." DR at p. 10, Finding No. 19. This proposed finding should be rejected. As noted above, there is no demonstrated "need" for Sutter plant capacity in the near term for RA purposes or otherwise. Even the CAISO acknowledges, based on the most conservative assessment, that a need for Sutter capacity does not arise until 2017. See DR at p. 3. If the Commission instructs the IOUs to procure additional RA capacity, all LSEs will be forced to sell back unneeded RA capacity to an oversupplied market at rock bottom prices or hold the excess capacity in their portfolios, thereby creating a stranded cost burden.

In addition, the Commission has yet to establish a methodology for determining when the cost allocation mechanism ("CAM") should be used, as is proposed here. See D.11-05-005 (May 5, 2011) at p. 17. Competing LSEs that have procured their own RA capacity in compliance with existing RA requirements must pass these costs on to their customers. Forcing a DA customer in southern California to pay for capacity in northern California when its LSE has procured the capacity that is required under existing regulations would be duplicative and punitive. Unless it becomes clear that ESPs and CCAs have failed to meet their 2012 RA obligations, there is no basis for assigning, to DA or CCA customers, any portion of the cost of additional capacity that is not needed by the CAISO to meet system reliability needs. If the Commission decides, in spite of this and other objections, to require the IOUs to enter into a contract with Calpine for the Sutter plant, the costs should be borne exclusively by the IOUs' bundled sales customers.

4. The Commission Does Not Have the Technical Expertise to Pick and Choose the Plants Required for System Reliability: The DR's recommendation to require the IOUs to enter into contracts for the Sutter plant, if adopted, would place the Commission in the position of favoring one generator over another, creating the potential for unlawful discrimination. Some

generation facilities in California have been shut down without intervention by the Commission. Other plants are in the planning stages and will be brought on-line between now and 2017. Many of these plants may be better able to provide RA capacity and renewable integration than the Sutter plant.

5. The DR Fails to Acknowledge That the Greatest Value of the Sutter Plant is Achieved Through the Sale of Energy, Not Capacity: A combined cycle power plant with a low heat rate should obtain much of its fixed cost recovery through energy markets, yet this is not happening for the Sutter plant and for many other combined cycle power plants in the State. When considering whether to provide out-of-market compensation to a particular power plant, the Commission must ask why the energy market, in combination with a capacity payment, fails to provide an adequate cost recovery mechanism to keep the plant in the market. The DR fails to address this issue. Although there may be many reasons why the market does not provide adequate cost recovery, one explanation is the excess supply of generation in California.

6. The DR Does Not Address Whether it Makes Economic Sense to Enter into a Capacity Contract with the Sutter Plant Rather than with Another Generation Facility: The Commission has authorized the IOUs to enter into contracts for the construction or purchase of energy and capacity from numerous large power plants. Under the "hybrid" market structure embraced by the Commission, Calpine has determined that "current and anticipated market conditions are not expected to provide the [Sutter] plant with reasonable opportunities to secure a sufficient revenue stream to continue operations."[6] Calpine's situation, which is not unique, raises an important issue regarding the most cost-efficient means to meet long-term capacity needs.

Rather than adopt the mandatory contracting approach recommended in the DR, the Commission should evaluate whether an IOU's application for a new plant, such as the Oakley plant, should be approved, or whether it is more cost efficient for an IOU to issue an RFP for new RA capacity as an alternative. Under an RFP, Sutter and other non-RA contracted capacity would be able to bid to provide capacity. A competitive process is likely to result in a lower cost outcome for ratepayers. The DR's proposal to require the IOUs to contract for capacity with a specific generation facility oversteps the Commission's authority and does not produce the most cost efficient result.

[6] R.11-10-023, "Proposal of Calpine Corporation on Phase I Workshop Issues," p. 2 (filed January 13, 2012).

The Commission should reject DR E-4471.

Respectfully submitted,

John W. Leslie
of
Luce, Forward, Hamilton & Scripps LLP
Attorneys for Shell Energy North America (US), L.P.

And on behalf of:
Alliance for Retail Energy Markets
Direct Access Customer Coalition
Energy Users Forum
Retail Energy Supply Association
Marin Energy Authority

JWL/sc

cc: All Commissioners
Ed Randolph, Director, Energy Division
Karen Clopton, Chief Administrative Law Judge
Frank Lindh, General Counsel
All parties on the service lists in R.10-05-006 and R.11-10-023
Dawn Weisz, MEA
David Orth, SJVPA
Mike Campbell, CCSF
Robert Strauss, Energy Division
Nathaniel Skinner, Energy Division

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CERTIFICATE OF SERVICE

I hereby certify that I have served, this day, a copy of the foregoing **COMMENTS ON DRAFT RESOLUTION E-4471** on Honesto Gatchalian, Energy Division, by electronic mail and Federal Express, and on all individuals listed on the letter and on all parties on the service lists for R.10-05-006 and R.11-10-023 by electronic mail only.

Executed on January 31, 2012, at San Diego, California.

Sue Pote

CALIFORNIA PUBLIC UTILITIES COMMISSION
Service Lists

PROCEEDING: R1005006 - CPUC - OIR TO INTEGR
FILER: CPUC
LIST NAME: LIST
LAST CHANGED: JANUARY 27, 2012

PROCEEDING: R1110023 - CPUC- OIR TO OVERSEE
FILER: CPUC
LIST NAME: LIST
LAST CHANGED: JANUARY 30, 2012