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Honesto Gatchalian
Energy Division
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Email: jnj@cpuc.ca.gov
FAX: 415-703-2200

Re: Draft Resolution E-4471

Dear Mr. Gatchalian:

The NRG Companies[1] submit the following comments on Draft Resolution E-4471 ("Draft Resolution"). The Draft Resolution directs the three Investor-Owned Utilities ("IOUs") (the Pacific Gas & Electric Company, the San Diego Gas & Electric Company, and the Southern California Edison Company), to enter into one or more contracts with the Sutter Energy Center ("Sutter"), an air-cooled combined-cycle located in the Sacramento Municipal Utility District's Balancing Authority Area ("BAA"). Sutter sells into the markets and BAA operated by the California Independent System Operator Corporation ("CAISO") via a "pseudo-tie".[2]

I. Introduction

The decision by Calpine to shutter the Sutter facility in 2012 suggests that California may be heading towards a reliability crisis, unless both the CAISO and this Commission take immediate actions to revamp California's hybrid markets. The NRG Companies respectfully suggest that the Commission's focus on retaining this one facility is misplaced. Instead, the CPUC's inquiry in this proceeding should focus on deficiencies in the existing market structure that have resulted in gas-fired generators, including the Sutter facility, being unable to remain financially viable.

Instead of adopting the Draft Resolution, the CPUC should address the flaws in its Resource Adequacy program in a systematic and transparent manner that will apply to all generators on a non-discriminatory basis. Experience has shown that relying on non-competitive *ad hoc* procurements has the potential to encourage more such *ad-hoc* procurements, to the detriment of ratepayers and the competitive market. For example, if the CPUC finds that its existing RA structure is not procuring sufficient flexible ramping capacity, then it should address any perceived reliability shortfall through an auction or Request for Proposals that will introduce the benefits of competition into the process, instead of mandating payments to one specific generating unit.

[1] The NRG Companies are NRG Power Marketing LLC, Cabrillo Power I LLC, Cabrillo Power II LLC, El Segundo Power, LLC, Long Beach Generation LLC and NRG Solar Blythe LLC.

[2] A "pseudo-tie" is an arrangement in which a generating located entirely within one BAA is deemed to be directly interconnected to another BAA.

Without a true fix to the revenue adequacy problems faced by California, the CPUC is likely to see a parade of Sutter-type units all arguing that they cannot survive without a CPUC-mandated contract. Such a situation is not desirable, and the CPUC should implement comprehensive reforms to its RA program as soon as possible and reject any non-competitively sourced system capacity contract.

Finally, the Commission should avoid addressing the issue of whether General Order 167 gives the CPUC authority to order a plant to remain in operation. The Sutter facility at issue here has not stated that it intends to imminently shut down, and there are significant procedures that will have to take place both before the CAISO, FERC, and this Commission. Thus, there is no reason for the CPUC to address the scope of its authority in this proceeding.

II. Comments

All parties appear to agree that California will need flexible, dispatchable, generation over the next ten years, particularly as the level of intermittent generation increases. The question is how – not if – California will meet its reliability requirements. NRG submits that competitive procurement principles should guide the Commission as it moves forward with reforms to its hybrid market structure, and that a one-off contract with a single market participant will not solve the larger issues facing California.

a. The Draft Resolution Fails To Establish A Legitimate Need to Contract With Sutter.

One of the more troubling aspects of the Draft Resolution is that it appears to conclude that there is a need for the system RA provided by Sutter. To the contrary, the Draft Resolution expressly acknowledges that Sutter is not required to meet any 2012 local area capacity requirements.[3] Likewise, the Draft Resolution observes that there has been no Commission finding of need for Sutter in 2020.[4] Lacking any official determination of need,[5] the Draft Resolution then proposes that the IOUs contract with Sutter anyway.

The Commission does not have sufficient evidence to conclude that there is a reliability need for the Sutter facility. The reliability need identified by the CAISO is for generic flexible system capacity, and is not expected to occur until 2018. Construction of new resources would be one way to meet the projected shortfall by 2018.[6] Another would be to contract with existing resources capable of supplying generic system RA capacity on a least-cost basis. While NRG agrees that the consequences of aggressively moving forward to meet renewable portfolio

[3] Draft Resolution, Finding 6 ("The CAISO did not find deficiencies in the 2012 Resource Adequacy Plans.") In fact, Sutter is not located within any of the Local Capacity Areas under the CPUC's RA program.
[4] Draft Resolution at 5.
[5] The NRG Companies share others' skepticism regarding the CAISO's initial results of the four Commission-approved scenarios that show no need for any new generation for 2020. As a result, the NRG Companies joined the Offer of Settlement in R. 10-06-006 that calls for additional CAISO study work prior to an official determination of need (or lack thereof).
[6] Several other markets, including PJM and ISO New England, rely on three-year forward capacity procurements. Even given California's long permitting and construction lead times for new capacity, there are many means to meet the reliability challenges projected by the CAISO other than giving out a non-competitive contract to Sutter.

standard goals while also failing to address the attendant operational challenges could be dire, the Draft Resolution is not a viable alternative.

Moreover, the NRG Companies strongly agree that it is wrong to assume that resources that do not have an RA or other bilateral capacity contract, and must rely solely on CAISO energy and ancillary market revenues to remain in operation, will be available to provide flexibility in the 2018-2020 timeframe.[7]

b. **The Draft Resolution Fails To Provide a Framework For Addressing the Underlying Problems**

The situation surrounding Sutter highlights many relevant issues:

- The inability of CAISO energy and ancillary service markets to sustain existing flexible generation, without capacity contracts above and beyond those available through the standard RA process.

- The lack of a transparent process to sustain existing flexible generation, or to encourage the development of new flexible generation.

- The uncertainty (at least the conflicting assertions) regarding the need for flexible generation in the 2018-2020 time frame.

The Draft Resolution only offers a band-aid. It does nothing to address the underlying need for reforms to the competitive market structure in California, and in reality, does nothing to improve system reliability. Adding another layer of out-of-market capacity procurement to a hodge-podge of seemingly uncoordinated capacity procurement mechanisms does nothing to address the fundamental issues at hand.

There are several efforts intended to address various aspects of these issues underway:

- The CAISO's continued study work to identify renewable integration needs as part of R. 10-05-006;

- The CAISO's promised forward flexible capacity procurement stakeholder process;[8]

[7] *See, e.g.,* Sutter Report at pages 5, 7.
[8] See http://www.caiso.com/Documents/NewStakeholderProcess-FlexibleCapacityForwardProcurement.htm.

- The current Resource Adequacy process, which includes consideration of both the CAISO's proposal to incorporate flexibility requirements into the RA requirements and the need to update RA rules to account for procurement changes related to the 33% Renewable Portfolio Standard;[9]

- The CAISO's Renewable Integration and Market Product Review Phase 2;[10]

- The CAISO's Flexible Ramping Product Stakeholder process;[11] and

- The promised CAISO stakeholder process to re-evaluate how the costs of its markets and products are allocated.[12]

Rather than focusing its energy and limited Staff resources on a one-off extra-market procurement, the Commission should focus on working with the CAISO to develop durable, transparent and market-based approaches to dealing with the real issues that the Sutter situation surfaces. These approaches will not be developed overnight, and ultimately getting the right structures in place will be difficult. Yet it is that path, not forced extra-market procurement that aligns neither with existing CAISO or CPUC market structures, which should be pursued.

c. The Draft Resolution Does Not Need to Address Whether It May Order Sutter to Remain in Operation Without Adequate Compensation.

While the NRG Companies do not support the Draft Resolution's proposed approach to direct the IOUs to contract for a resource outside of existing market structures and processes, the NRG Companies are concerned about the implications of the proposed approach, namely, that the Commission can order a generating facility, that cannot cover its operating costs, to remain in operation indefinitely.[13]

Fortunately, as discussed below, the CPUC does not have to address this thorny issue at this time. There are several FERC, CAISO and CPUC proceedings which will have to be completed before Calpine would have any financial incentive to retire the facility. All of these are expected to take several months (if not longer) to unfold, and in the meantime, the Draft Resolution should refrain from creating needless litigation over its theoretical ability to order a generating facility to remain online.

NRG notes that the provisions of Operating Standard 24 of General Order 167 state that the obligation to maintain a unit in operation applies "only to the extent that the regulatory body

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[9] *Phase 1 Scoping Memo and Ruling of Assigned Commissioner and Administrative Law Judge*, issued December 27, 2011 in R. 11-10-023 at pages 4-5 (available at http://docs.cpuc.ca.gov/efile/RULC/156371.pdf).
[10] Documents available at http://www.caiso.com/informed/Pages/StakeholderProcesses/RenewableIntegrationMarketProductReviewPhase2.aspx.
[11] Documents available at http://www.caiso.com/informed/Pages/StakeholderProcesses/FlexibleRampingProduct.aspx.
[12] See Flexible Ramping Product Second Revised Straw Proposal at 27 (http://www.caiso.com/Documents/FlexibleRampingProductSecondRevisedStrawProposal.pdf).
[13] Draft Resolution at 8.

with relevant ratemaking authority has instituted a mechanism to compensate the GAO [generation asset owner] for readiness services provided." In this case, the only "mechanism" the Commission has instituted is a requirement that the large IOUs negotiate with Calpine for a possible agreement with an unknown price that provides no assurance that Calpine will be adequately compensated for all of the expenses incurred to maintain Sutter's readiness for service.

While the Draft Resolution applies narrowly to the Sutter facility, the implications of ordering any generating unit that is not recovering its costs to remain in operation are ominous. Yet the Commission can, and should, steer clear of these particular rocky shoals.

III. Recommended Changes

The Commission should withdraw the Draft Resolution and focus on working with the CAISO to develop a durable, forward-looking market framework that supports the continued operation of existing flexible generation and the development of new flexible generation. As NRG recommended to the CAISO, the California markets should:

1. Establish a long-term capacity procurement mechanism that ensures that sufficient capacity is available to meet its needs, both now, in the near future, and beyond the next RA year.

2. Reduce reliance on out of market procurement and ensure that the California energy markets are sending appropriate price signals. The continued use of out-of market mechanisms prevent proper price formation, which in turn reduces the revenues needed for cost recovery.

3. Work with the CAISO to implement additional market products that reward flexible dispatch characteristics and provide the opportunity for facilities such as Sutter to recover their costs.

NRG is sympathetic to Sutter's reluctance to wait for these market reforms. A market structure that provides generators adequate compensation has been a long time in coming, and certainly has not arrived yet. However, it is problematic for the CPUC to propose to provide this type of financial support to a single market participant without establishing a comprehensive approach to fixing the underlying revenue issues.

IV. Conclusion

The present circumstances, in which existing market structures, products and processes do not fit well with the projected future needs, are uncomfortable. Much work remains to be done to build the future needed frameworks. Extra-market procurements under any jurisdiction do not meaningfully advance California towards processes that will satisfy the state's renewable goals at least cost. The NRG Companies respectfully urge the Commission to pursue its recommended approach.

Respectfully submitted,

Abraham Silverman (BC)

Abraham Silverman
Assistant Generation Counsel
NRG Energy, Inc.
211 Carnegie Center
Princeton, NJ 08540
Office: (609) 524-4696
Abraham.Silverman@nrgenergy.com

cc: President Michael Peevey
Commissioner Mark Ferron
Commissioner Michel Florio
Commissioner Catherine Sandoval
Commissioner Timothy Simon
Ed Randolph, Director, Energy Division
Karen Clopton, Chief Administrative Law Judge
Frank Lindh, General Counsel
Robert Strauss, Energy Division (via email)
Nathaniel Skinner, Energy Division (via email)
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