

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE  
STATE OF CALIFORNIA**

Order Instituting Rulemaking to Oversee the  
Resource Adequacy Program, Consider  
Program Refinements, and Establish Annual  
Local Procurement Obligations.

Rulemaking 11-10-023  
(Filed October 20, 2011)

**PROPOSAL OF CALPINE CORPORATION  
ON PHASE 1 WORKSHOP ISSUES**

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January 13, 2012

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Pursuant to the *Phase 1 Scoping Memo and Ruling of Assigned Commissioner and Administrative Law Judge* issued December 27, 2011 (“*Phase 1 Scoping Memo*”), Calpine Corporation (“Calpine”) submits this proposal for adoption of a forward resource adequacy (“RA”) procurement requirement to be considered during the workshops scheduled for January 26-27, 2012. As discussed below, the addition of a forward procurement requirement to the current RA program is imperative to ensure the continued availability of existing resources needed to maintain system reliability going forward.

**I. INTRODUCTION & BACKGROUND**

California has reached a tipping point with respect to the near term economic viability of existing non-utility generation that the Commission assumes will be available to meet future system reliability needs. Current procurement policies and practices have created market conditions that do not provide uncontracted resources<sup>1</sup> with sufficient and stable enough revenue streams to recover going forward costs (including major maintenance costs). As a result, resources are becoming increasingly at risk of economic retirement. Absent action by the

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<sup>1</sup> “Uncontracted resources” refers to existing generation resources that are not under contracts to, or owned by, load serving entities (“LSEs”).

Commission in the near term, the continued availability of existing resources needed to maintain system reliability as early as 2017<sup>2</sup> will be in doubt.

Recently, Calpine requested that the California Independent System Operator (“CAISO”) designate the Sutter Energy Center (“Sutter”) as capacity at risk of retirement, pursuant to the CAISO’s Capacity Procurement Mechanism (“CPM”).<sup>3</sup> Calpine requested a CPM designation for Sutter because the plant does not have an RA capacity contract for 2012 and current and anticipated market conditions are not expected to provide the plant with reasonable opportunities to secure a sufficient revenue stream to continue operations. While Sutter is the first resource to request a CPM designation for risk of retirement, the market policies which led to Calpine’s decision affect all existing non-utility generation resources without RA capacity contracts.

Current procurement policies and practices that exclude existing resources from participating in long term resource solicitations limit market opportunities for these resources. The residual market opportunities that are available to existing resources yield low compensation that is expected to drop even further as a result of excess supply created by increased renewable generation resources and other procurement policies. Net revenues for combined cycle gas turbine units have been declining in recent years and, for 2010, were estimated by the CAISO to be less than one-half of the five year average.<sup>4</sup> The CAISO further projects that net revenues for conventional generation resources could decline even further as additional renewable resources come on-line.<sup>5</sup>

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<sup>2</sup> The continued availability of some uncontracted resources may be needed to maintain system reliability much earlier than 2017.

<sup>3</sup> See *California ISO Report on Basis and Need for CPM Designation for Sutter Energy Center* (December 6, 2011).

<sup>4</sup> CAISO *Market Issues and Performance Annual Report 2010* at 53.

<sup>5</sup> CAISO *Integration of Renewable Resources; Operational Requirements and Generation Fleet Capability at 20% RPS* at v (August 31, 2010).

Economic realities are that, if compensation from the markets available to existing resources is insufficient and/or insufficiently stable to ensure recovery of going forward costs, such resources should be expected to shut down. From a reliability perspective, however, the record in the Commission's long-term procurement proceeding ("LTPP")<sup>6</sup> and studies performed by the CAISO related to the Sutter CPM designation, demonstrate the need for the continued availability of uncontracted resources (beyond Sutter) to meet reliability needs going forward.

Sensitivity studies performed by Calpine in the LTPP show that if existing resources assumed to be available in CAISO modeling shut down, substantial amounts of new replacement resources will be necessary to maintain reliability (assuming new resources could be timely brought on-line), with a potential cost to ratepayers in the billions of dollars.<sup>7</sup> Under such circumstances, the potential for *economic* retirements demonstrates fundamental market structure problems that must be addressed - on the one hand, inadequate revenue streams place uncontracted resources at risk of economic retirement; while on the other hand, the continuing availability of these resources is critical for system reliability in the future.

In past RA proceedings, parties, such as the investor-owned utilities ("IOUs") and the CAISO, have supported adding a multi-year forward commitment to the RA program.<sup>8</sup> While the Commission has acknowledged that "the addition of a forward procurement obligation is a regulatory tool that could potentially benefit the RA program with respect to reliability, cost, and equitable allocation objectives," the Commission has, nevertheless, failed to take action.

In comments on CAISO's Sutter CPM report, many parties called on the Commission to address the fundamental market structure issues that put the availability of resources needed to maintain future reliability at risk. Pacific Gas and Electric Company, for example,

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<sup>6</sup> Rulemaking ("R.") 10-05-006.

<sup>7</sup> Track 1 Direct Testimony of Calpine Corporation (R.10-05-006), Calpine/Barmack, Exh. 601 at 12-13.

<sup>8</sup> See Decision 10-06-018, mimeo at 32.

acknowledged the need for the Commission to reform certain aspects of the current RA program to address long-term reliability:

The [Commission] needs to modify the current Resource Adequacy (“RA”) structure and issue LTPP decisions to address the long term needs of the system.<sup>9</sup>

The California Wind Energy Association similarly agreed that the Commission should work with the CAISO and stakeholders to consider how best to retain “the services of efficient existing plants that are left with no method of economic subsistence.”<sup>10</sup> The Independent Energy Producers Association,<sup>11</sup> Western Power Trading Forum<sup>12</sup> and Dynegy<sup>13</sup> among others each raised similar issues in their respective comments to the CAISO.

In the LTPP, Calpine requested that the Commission direct the IOUs to hold intermediate term resource solicitations to procure capacity from existing resources as an interim measure to ensure the continued availability of such resources over the next 3-5 years. The Commission, however, has not acted on Calpine’s proposal and it is unclear when it will do so.

The *Phase 1 Scoping Memo* notes that “parties have identified several areas of overlap between RA rules and procurement rules” and requests comment on issues that should be

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<sup>9</sup> Comments of Pacific Gas and Electric Company on the California ISO Report on Basis and Need for CPM Designation for Sutter Energy Center (December 16, 2011) at 1.

<sup>10</sup> Comments of the California Wind Energy Association on the December 6, 2011 CAISO Report on Basis and Need for CPM Designation of Sutter Energy Center at 3.

<sup>11</sup> Comments of Independent Energy Producers regarding CAISO Report on Basis and Need for CPM Designation for Sutter Energy Center at 1. (“The CAISO’s proposal is indicative of a problem in the California energy markets that has persisted too long . . . . The CPUC has failed so far to facilitate the means by which LSEs may secure cost-effective, capacity of any vintage resource needed to meet current and mid-term reliability and operational needs.”)

<sup>12</sup> Western Power Trading Forum Comments in Response to CAISO Proposal for Waiver Request for Sutter at 1. (“The Sutter Energy Center (SEC) situation should be seen as direct evidence of our collective failure to have addressed capacity compensation in the past.”)

<sup>13</sup> Dynegy Comments in Response to Proposed Risk of Retirement CPM Designation for Sutter Energy Center at 1. (“The Sutter designation highlights significant shortcomings in CAISO markets and [Commission] procurement policy, including the lack of a comprehensive set of markets and procurement policies focused on ensuring future system reliability. The CAISO and the [Commission] should take this opportunity to examine and address these shortcomings.”)

addressed in the near term.<sup>14</sup> For the reasons discussed above, adoption of a multi-year forward RA procurement requirement is an important near term issue that should be addressed during the workshops scheduled for January 26-27, 2012.

## **II. PROPOSAL FOR MULTI-YEAR FORWARD RA PROCUREMENT**

The following are the key characteristics of Calpine's multi-year forward RA procurement proposal:

- The multi-year procurement requirement would extend 5 years forward. For example, need determinations and associated procurement for 2017 would be undertaken in 2012;
- The multi-year procurement requirement will not disrupt or replace the current year- and month-ahead RA compliance obligations but rather introduce a new element into the existing RA program structure (*i.e.*, the obligation to procure RA capacity 5 years in advance);
- Forward need will be determined by the CAISO using studies similar to the studies performed by the CAISO in the LTPP;
- Need determinations and associated procurement will take place annually;
- The forward procurement requirement will be for generic megawatts of RA capacity, with locational elements and operational characteristics potentially added in the future;
- A load serving entity's ("LSE") forward procurement obligation will be proportional to the LSE's peak load share in the forward procurement timeframe;
- LSEs will be allowed to trade out of forward positions to accommodate load migration; and
- Upgrades to, or expansion of, existing resources could be procured on a forward basis to the extent that the upgrade/expansion is completed prior to the compliance obligation.

The adoption of a forward procurement requirement to the current RA program is critical to ensuring the continued availability of existing resources needed to maintain system reliability

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<sup>14</sup> *Phase 1 Scoping Memo* at 5.

going forward. Calpine believes the above characteristics provide a meaningful starting point for parties to consider and discuss the adoption of such a multi-year forward procurement requirement during the upcoming workshops.

Respectfully submitted,

/s/

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Attorneys for Calpine Corporation

Dated: January 13, 2012

## VERIFICATION

I am the attorney for Calpine Corporation, and I have been authorized to make this verification on the behalf of Calpine Corporation. Said party is located outside of the County of San Francisco, where I have my office, and I make this verification for said party for that reason.

I have read the foregoing document and based on information and belief, believe the matters in the proposal to be true.

I declare under penalty of perjury that the foregoing is true and correct and executed on January 13, 2012, at San Francisco, California.

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/s/  
Jeffrey P. Gray