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	R.11-10-023 (Filed October 20, 2011)

REPLY OF THE ALLIANCE FOR RETAIL ENERGY MARKETS

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CONSULTANT TO THE
ALLIANCE FOR RETAIL ENERGY MARKETS

April 15, 2013

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The Alliance for Retail Energy Markets [1] ("AReM") submits this reply to comments filed April 5, 2013, in accordance with *Administrative Law Judge's Ruling Resetting Schedule for Comments on Phase 2 Resource Adequacy Issued and Scheduling a Prehearing Conference*, issued by Administrative Law Judge David M. Gamson on March 11, 2013.

I. FOR THE LONG-TERM, CALIFORNIA NEEDS PROPER MARKET SIGNALS, INCLUDING IMPROVED ANCILLARY SERVICES MARKETS, A CENTRALIZED CAPACITY MARKET AND REVISED RETAIL RATE DESIGNS.

There is little dispute that increased use of intermittent resources require the availability of additional flexible resources to provide ramping, load following, and regulation services for safe and reliable grid management. AReM remains concerned, however, that the proposals of both the Joint Parties and the Energy Division to address and mitigate the demand profile pictured in the California Independent System Operator's (CAISO's) "duck curve" are not appropriately focused on providing market-based price signals that create incentives for the retention of existing and/or development of new resources to meet these needs efficiently and

[1] The Alliance for Retail Energy Markets is a California non -profit mutual benefit corporation formed by electric service providers that are active in the California's direct access market. This filing represents the position of AReM, but not necessarily th at of a particular member or any affiliates of its members with respect to the issues addressed herein.

cost-effectively. In short, instead of focusing on the development of market mechanisms that will allow buyers and sellers of the needed resources to transact for those resources efficiently and cost effectively, both the current proposals layer more command and control rules in the Resource Adequacy ("RA") program.

Throughout this proceeding, and in the CAISO stakeholder process where these same issues are under consideration, AReM has advocated the following:[2]

- Embedding the new flexible resource requirements in the RA program does not represent an efficient mechanism for procurement of those resources, and as such, if adopted at all, should have a specific sunset date. Beyond that sunset date, capacity requirements should be no more granular than they are today (system and local).
- The new flexible resource requirements should be integrated into the CAISO's biddable ancillary service markets where they can be transparently priced and procured.
- Integrating the flexible capacity requirements into the ancillary service markets will create the pricing transparency and a new revenue stream for resource owners that, along with energy and capacity revenues, will enable them to make economic investment decisions.
- Along with implementation of biddable ancillary service markets, the Commission, working collaboratively with the CAISO, should implement a centralized forward capacity market to provide additional pricing transparency and revenue certainty for the capacity component.

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[2] *Comments by the Alliance for Retail Energy Markets on Resource Adequacy Flexible Capacity Procurement Joint Parties' Proposal*, December 26, 2012, R.11-10-023, pp. 4-5.

- Proceeding in this manner will ensure that California's has competitive energy, ancillary service, and capacity markets that support economic and efficient investment in existing and new resources.

In addition, the Commission has the tools within its jurisdiction to partially address the "duck curve" by using retail rate design to encourage customers to shift demand, thereby reducing flexibility needs. Whether and how to use retail rates structures to meet the requirements of increasing intermittent resources is another area of ongoing activity that should be allowed to progress further before flexible RA procurement requirements are imposed.

In their opening comments in this phase of the proceeding, Shell Energy North America (US), L.P. ("Shell Energy"), California Wind Energy Association ("CalWEA") and Marin Energy Authority ("MEA") all echo AReM's comments that flexibility needs should be addressed through improvements to the CAISO's ancillary services market or other market mechanisms.[3] In particular, CalWEA points to market mechanisms in other organized markets that could be employed in California to reduce flexibility needs.[4] Integrating the flexible resource requirements into the ancillary service markets needs to be more fully explored and implemented where appropriate to ensure cost-effective and efficient solutions to California's flexibility needs.[5]

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[3] Shell Energy, p. 3 and 12; CalWEA, p. 15; MEA, p. 1.
[4] CalWEA, p. 15.
[5] This is all the more important now that the CAISO has executed the Memorandum of Understanding with Pacificorp to implement an Energy Imbalan ce Market ("EIM") across the footprints of both organizations. The CAISO's access to additional flexible resources outside it current footprint should improve the tools that the CAISO has to manage the growing need for flexible resources; the impact of these changes must be assessed before flexible resource requirements are imposed.

At the other extreme is the comment from the California Energy Storage Alliance ("CESA") that endorses the implementation of multi-year forward contracting for RA capacity, [6] while paying no attention whatsoever to the need for a centralized capacity market ("CCM"), which would promote price transparency and allow load-ser ving entities ("LSEs") to manage risk and effectively transact on a multi-year forward basis.

AReM emphasizes that the Commission and the CAISO must not allow the development of a CCM to languish. A CCM would significantly improve price signals, transparency, and efficiency for all RA market participants, and is regarded by many, including AReM members, as a critically needed market structure in California, whether the RA program is a one-year forward program or multi-year forward. LSEs, RA suppliers and retail customers would all benefit from such market improvements. AReM urges the Commission to devote the time and resources necessary to send the proper price signals and implement efficient and cost-effective market mechanisms for California.

II. FOR THE 2014 RA COMPLIANCE YEAR, THE COMMISSION SHOULD CONDUCT A TRIAL RUN.

The majority of parties filing comments do not support the imposition of flexible capacity requirements as part of the Resource Adequacy (RA") program for 2014. [7] Instead, several parties, including the Western Power Trading Forum ("WPTF"), have advocated that the 2014 RA compliance year serve as a trial run for the inclusion of flexible requirements in the RA program.[8] AReM supports this concept of a trial run and the detailed proposal for implementing the concept as set forth by WPTF. A trial run would allow the Commission and the CAISO time

[6] CESA, p. 7.
[7] See, for example, California Large Energy Consumers Association, p. 17; Sierra Club,p. 9; and MEA, pp. 2-3.
[8] See, Western Power Trading Forum, pp. 3 -5; Division of Ratepayer Advocates, pp. 14 -16; The Utility Reform Network, pp. 9-10.

to evaluate alternative approaches to meet flexibility requirements, such as improved ancillary services markets and a CCM, or in the alternative, to work out remaining program details involving counting rules, must offer requirements, non-compliance sanctions and penalties, and revisions to existing contracts to the extent that become necessary. In fact, Pacific Gas and Electric Company's ("PG&E") opening comments provide a particularly useful snapshot of the many details still to be resolved before flexible capacity requirements can be included in the RA program.[9]

If the trial run approach is adopted, AReM recommends that the Commission initiate it for the fourth quarter of 2014 and begin with the submission of the monthly RA filings for the October 2014 RA compliance month on August 19, 2014. The CAISO has indicated that the largest flexibility needs occur in the shoulder months and the months of November and December have the highest needs of the year.[10] Therefore, initiating the trial run in October 2014 will provide useful information to the CAISO and Commission on the extent to which the existing fleet of resources can meet the flexibility needs during the most critical time of the year. After the trial run, the Commission and CAISO can use the results to develop final details for implementation in the 2015 compliance year and thereafter, if appropriate.

III. ALLOCATION OF ANY FLEXIBILITY REQUIREMENTS SHOULD FOLLOW COST CAUSATION PRINCIPLES.

An element of including flexible requirements in the RA program that needs further attention is manner in which the requirements will be allocated to LSEs. The opening comments reflect of a range of possible approaches. For example, the California Large Energy Consumers ("CLECA") argues that the proposed allocation method, which is based on peak requirements,

[9] See, Pacific Gas and Electric Company, pp. 17-28.
[10] CAISO April 5 Comments, Attachment A, slide 15.

does not follow cost causation principles [11] based on the CAISO's demonstration that the highest flexibility needs occur in the shoulder months, well outside of the peak months in California. In fact, CLECA suggests that the Commission should assign the flexibility requirement based on the characteristics of each LSE's resource portfolio, which would better reflect cost causation. [12] Ormat Technologies, Inc. ("Ormat") notes that allocating flexibility requirements to LSEs without regard to the characteristics of their resource portfolios "creates a strong disincentive for procuring more stable and predictable renewable resources." [13] Ormat suggests, as a long-term solution, imposing the costs on the intermittent generators creating the flexibility needs through a contract adder. [14] AReM does not have a view at this time as to whether either the CLECA or Ormat approaches are appropriate or practical, but the fact that there is still a wide divergence as to the correct allocation mechanism is further evidence that more work is needed before any implementation can "go live." AReM urges the Commission to determine the optimal approach for proper cost causation and to adopt that approach for the long term.

However, AReM recognizes that, until an improved cost allocation system can be devised, any established flexibility requirements and associated costs will be imposed directly on LSEs and their customers. The Joint Parties[15] and Energy Division[16] propose allocating flexibility requirements to LSEs using the same method used today to allocate system RA requirements, which is allocated based on an LSE's load at the time of the system peak (*i.e.* "coincident peak approach"). AReM supports this allocation method in the interim until an

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[11] CLECA, p. 16.
[12] CLECA, pp. 15-16.
[13] Ormat Industries, p. 4.
[14] Ormat Industries, p. 4.
[15] *Phase 2 Scoping Memo and Ruling of Assigned Commissioner and Administrative Law Judge*, R.11-10-023, December 6, 2012, Attachment A, p. 10.
[16] *Administrative Law Judge's Ruling Resetting Schedule for Comments on Phase 2 Resource Adequacy Issued and Scheduling a Prehearing Conference*, R.11-10-023, March 11, 2013, Attachment, p. 4.

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allocation method is developed that complies with cost causation principles.

IV. CONCLUSION.

As detailed above, AReM respectfully requests that the Commission take the following actions:

- Devote the time and resources necessary to address flexibility requirements by sending the proper price signals and implementing efficient and cost-effective market mechanisms for California, such as improved ancillary services markets, a centralized capacity market and revised retail rate designs.
- For the 2014 RA compliance year, adopt a trial run, as described by WPTF in its opening comments, to be initiated in the fourth quarter of 2014, which is the critical time for meeting flexility requirements in California.
- Determine and adopt a method for allocating flexibility requirements that reflects proper cost causation and sends appropriate signals to the market to ensure development and procurement of resources that minimize flexibility needs.
- Use the coincident peak method to allocate flexibility requirements to LSEs in the interim, until an allocation method that complies with cost causation principles is developed and implemented.

Respectfully submitted,

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