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**DOCKET NO. 24770**

**REPORT OF THE ELECTRIC  
RELIABILITY COUNCIL OF TEXAS  
(ERCOT) TO THE PUCT  
REGARDING IMPLEMENTATION  
OF THE ERCOT PROTOCOLS**

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**BEFORE THE  
PUBLIC UTILITY COMMISSION  
OF TEXAS**

2003 APR -3 PM 12:09  
PUBLIC UTILITY COMMISSION  
FILING CLERK

**RESPONSE OF THE CITY OF AUSTIN D/B/A AUSTIN ENERGY TO ORDER  
No. 18 REQUESTING COMMENT ON EXTENDED OFFER CAPS AND A  
MODIFIED COMPETITIVE SOLUTION METHOD**

NOW COMES The City of Austin d/b/a Austin Energy, ("Austin Energy") and  
files these Comments in the above docket as follows:

**Extension of Offer Caps Beyond July 2003 Expiration Date**

Austin Energy does not oppose extending the effective date of the offer caps for  
balancing energy or ancillary services beyond the current year's July expiration date.  
Austin Energy suggests that the Commission may wish to extend the caps for one year  
and establish a procedural schedule beginning in the Spring/Summer of 2004 for  
revisiting the issue of the termination of the caps.

**Competitive Solution Method for Ancillary Services and Balancing Energy**

Austin Energy has filed previously extensive comments on the Staff's proposed  
Competitive Solution Method (CSM) for ancillary services.<sup>1</sup> The Staff's proposal to

<sup>1</sup> Docket No. 24770, *Comments of the City of Austin d/b/a Austin Energy on Commission Staff's October 11, 2002 report entitled Application of Competitive Solution Method to Data from ERCOT Ancillary Capacity Services*, November 22, 2002; *Reply of the City of Austin D/B/A Austin Energy to the Commission Staff's December 13, 2002 Response to Comments on Staff's October 11, 2002 Report Entitled Application of Competitive Solution Method to Data from ERCOT Ancillary Capacity Services*, January 6, 2003; and *Final Comments of the City of Austin D/B/A Austin Energy to the Commission Staff's October*

expand its market mitigation method to balancing energy in no way alters the issues and positions articulated in our earlier comments. Policy proposals such as the Competitive Solution Method raise questions of economics and market design that should be investigated through rigorous empirical analysis prior to adoption. Austin Energy urges the commissioners, first, to review those earlier comments and the Staff's responses, as the fundamental questions at issue here are already addressed in those filings, and second, to direct the MOD to conduct the rigorous economic analysis needed for the Commission to make an informed decision on this issue.

In brief, the fundamental issue is as follows: Do price spikes serve as price signals that induce new resources to enter the market?<sup>2</sup> If the answer to that question is yes, then will the Staff's proposed CSM create an equivalent inducement? This is not a trivial question. Successful markets may be successful because of delicately balanced design characteristics, and the impacts of changes among those characteristics may be fickle and difficult to fully anticipate. Decisions about isolated market design issues can have consequences in other parts of the market and can ultimately influence the success of retail competition.

A worst-case scenario in this instance could be as follows: The Commission imposes the CSM for ancillary services and modified CSM for balancing energy. These policies reduce the market incentives for new supply to enter the market. As a result, the market does not respond with sufficient new generation when the current supply glut diminishes. Because the market does not respond adequately, the Commission is forced to impose a

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*11, 2002 Report Entitled Application of Competitive Solution Method to Data from ERCOT Ancillary Capacity Services, January 23, 2003.*

regulatory solution—some variation on ICAP as is already under investigation in Project No. 24255—to bring more supply to the market. Such policies can be quite costly, as the REPs in the Texas market have articulated in Project No. 24255 and elsewhere.<sup>3</sup> Higher costs reduce headroom, and have a negative impact on competition.

The risk of the Commission's piecemeal modifications of the wholesale market design is that the higher costs that could arise will have a negative impact on the retail market. Despite today's overwhelming supply glut in the wholesale market, many retail customers are not receiving significant savings, in part because new costs arising from the restructured market are being passed through to retail customers—offsetting the wholesale market savings that they would otherwise be sharing. Until new costs are curbed, many retail customers will not benefit from the wholesale power glut.

Do the Staff's CSM proposals reduce or raise costs? Presumably price spikes will be mitigated in the short run, but will new and higher costs arise in the long run? That question is ripe for empirical analysis. However, before even looking at the available evidence, the current Staff recommendation jumps to the conclusion that the modified CSM is beneficial, although the data and resources available to investigate the question have not been exploited. The Commission will soon have at its disposal the resources to perform such an analysis, once it contracts with the consultants recommended by MOD. What is after all the role of MOD and its consultants if not to rigorously evaluate the market to help inform the Commission in its decisions on market design?

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<sup>2</sup> As explained in Austin Energy's previous filings, the data presented by the Staff in its own assessment of the CSM suggest that—at least in the short term—the answer to this question is yes.

<sup>3</sup> See for example Project No. 24255, Rulemaking Concerning Planning Reserve Margin Requirements, *ARM Comments Regarding Staff's Revised Strawman*, February 27, 2003.

Austin Energy's comments today are filled with questions, but no answers. Order No. 18 asks commentors to provide a variety of information to the Commission—proposed procedural schedules, proposed Protocol revisions, identification of ERCOT system changes, and so on. Austin Energy believes that the request is premature in light of the assessments that should be performed prior to decision. Fundamental questions of economics and market design are at issue. Without conducting a rigorous analysis, it is difficult for the market participants, Staff, and Commission to truly know whether these policies will achieve their aims or instead created unintended consequences.

Austin Energy urges the Commission first to review the comments filed previously in this docket on the Staff's proposed CSM. Austin Energy urges the Commission second to defer making a decision on this issue until the MOD's new consultants can conduct a rigorous analytic study of the impacts of price spikes on supply response using the robust data set available from the first year and one-half of wholesale market operations. Following the consultant's report, the market participants and the Commission Staff can conduct an informed debate upon which the Commission may then make an informed judgment.

Respectfully submitted,

**CITY OF AUSTIN d/b/a Austin Energy**

By: 

Bob Kahn  
Vice President, Legal Services  
State Bar No. 11074230  
721 Barton Springs Road Suite 500  
Austin, Texas 78704-1194  
(512) 322-6572  
(512) 322-6521 (FAX)

**CERTIFICATE OF SERVICE**

I hereby certify that a true and correct copy of the foregoing document was served on all parties of record in this proceeding on this the 3rd day of April 2003, by facsimile, first class, U.S. Mail, postage prepaid, or by hand delivery.

  
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Bob Kahn