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PROJECT NO. 52373

REVIEW OF WHOLESALE ELECTRIC MARKET DESIGN	**§**	**PUBLIC UTILITY COMMISSION**
	§	
	§	**OF TEXAS**

SUMMER ENERGY'S COMMENTS

Summer Energy LLC ("Summer"), a retail electric provider holding certificate number 10205, submits the following comments in response to the October 25, 2021, memo in this proceeding:

I. INTRODUCTION

Summer appreciates the opportunity to comment on the Public Utility Commission of Texas' ("Commission") review of ERCOT's Wholesale Market Design. Winter Storm Uri caused unusually long forced outages, food and water shortages, disruption of business, and tragic loss of life. Summer supports the Commission's efforts to ensure that the grid remains reliable.

Until Winter Storm Uri, ERCOT's wholesale market design has been very successful, providing very competitive prices and reliable service since the advent of retail competition nearly 20 years ago. Winter Storm Uri presents an opportunity to improve on that design, improve reliability and ensure success of the competitive electricity market for the future.

Summer suggests that the Commission seek to identify and solve the problems that exist but avoid disrupting the aspects of the market that currently work well. Dr. William Hogan, in a speech at the ACCC/AER Regulatory Conference in Australia cautioned that "[a] post-mortem [of Winter Storm Uri] will provide many lessons. One challenge will be to learn the right lessons."[1]

Clearly, the Commission should examine and tackle low hanging fruit. Resolving issues relating to critical care customers is an example. Electricity supply to gas infrastructure required to deliver fuel to power plants should maintain the highest status of reliability. Another example is winterization. The legislature has given the Commission tools to deal with winterization[2] and the Commission should use them. However, there were issues related to market prices. Efforts to

[1] Electricity Market Design. (July 30, 2021) ACCC/AER Regulatory Conference 2021, Electricity Market Design Panel, Australia (https://scholar.harvard.edu/files/whogan/files/hogan_accc_073021.pdf)
[2] SB3 – Acts 2021, 87th Leg., R.S., Ch. 426, eff. June 8, 2021 ("The winterization bill").

resolve this issue is where the Commission must ensure that it is applying resolution to the "right lesson."

II. LOAD SERVING ENTITY ("LSE") OBLIGATION

Summer opposes any LSE Obligation for several reasons. In summary, an LSE obligation at best may result in a slight reduction in the financing costs of a prospective new generator. At worst it will end retail competition in Texas. There really is no reward for an LSE Obligation, only great risk.

A. LSE Obligations Do Not Add Value

The proponents of a 3 year forward will suggest that the contracting between LSEs and Resources will enhance the ability to finance a new generator. This argument is simply false. Typical power plants are financed over 30 years. Even if a developer was able to achieve contracts for 100% of the capacity of his project in 3 year forward obligations, that would only provide him revenues associated for a single year (or one thirtieth) of the financing.[3] That will not result in significant credit enhancement.

Furthermore, since the obligation is only 50% of an LSE's load ratio share in year 3, it's unlikely to enhance the forward price signal. Under the proposal, only half of total ERCOT Load must be contracted for in year 3. Theoretically, a prospective project would have to offer energy at prices less than 50% of existing generators before they would be competitive with the fleet on the ground. By definition, there is no scarcity with a 50% obligation.

Summer does not support Capacity Markets, however, the forward obligation of Capacity Markets is very different than a 50% obligation, because LSEs are required to purchase 100% of capacity plus a reserve margin. Consequently, a capacity market sends a strong forward price signal when a system is short because only a new project, or demand response can provide capacity in a short market.

Simply put, LSE Obligations at best, provide very little value in enhancing reliability.

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[3] Assuming a generator contracts with LSEs in Year ("Y") 1, and a 2-year construction period, power under the contract would flow on Y1 + 2 or Y3.

B. LSE Obligations Are A Solution To A Problem That Does Not Exist

As stated above, proponents of forward obligations claim that they enhance the ability to finance new projects. This argument assumes there is no market for 3-year, 5-year or 30-year power contracts in ERCOT. While the volumes are minimal, anyone can currently purchase long term projects from highly liquid, financially stable power marketers or enter tolling agreements with developers. ERCOT enjoys the fact that virtually every major investment bank and numerous hedge funds participate in the electricity market. When the risk/reward ratio is appropriate, these entities will enter long term contracts and package them to sell to LSEs. An LSE Obligation will disrupt one of the biggest roles that Power Marketers play.

Additionally, the argument that credit enhancement is required assumes that finance markets don't understand how to price risk or time-value of money. These are basic functions of finance. The Commission need only ensure that prices are efficient, and the market will resolve all the remaining issues.

C. LSE Obligations Are Unmanageable For LSEs

An LSE Obligation will require an LSE to purchase energy for customers that are not under contract. For an LSE, energy is by the largest expense by a significant multiple. Assume an LSE has customers under contract for a weighted average 9 months, which is likely since most retail customers sign 1-year contracts. Also assume the LSE is 100% hedged for the term of those existing contracts. The LSE Obligation would require it to purchase nearly 60% of its energy for 15 months after its contracts expire.[4]

This is doubly problematic because the purchase must be made in advance. The LSE has to finance, at least the credit requirements for the additional purchases. It's highly doubtful that it can recover the cost of the 60% additional energy for 15 months and 15 months of the time-value on the credit requirement in the rates of its current customers. Yet, the LSE has no other way to collect that expense.

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[4] See Attachment 1. The LSE being completely hedged meets the 1 month and 6-month obligations fully but does not meet portions of the 1-year, 2-year and 3-year obligations. The additional supply that is required is over 60% of the LSE's load.

When you consider the problems associated with the LSE Obligation and the dire lack of benefits, it's clear that the Commission should reject the concept outright.

III. CHANGES IN ORDC/OFFER CAPS

Summer suggests that the appropriate way to resolve all these issues is adjusting the Operating Reserve Demand Curve ("ORDC"). As Dr. Hogan states "[a]n operating reserve demand curve developed from first principles would improve reliability, support adequate scarcity pricing . . ." and "[b]etter scarcity pricing would also contribute to long-term resource adequacy."[5]

ERCOT has a missing money problem caused by administrative actions, offer caps and renewable subsidies. This missing money problem appears in ERCOT's real time market, manifesting itself as reduced real time prices. This problem can be resolved by changing the Minimum Contingency Level ("MCL") of the ORDC, which also enhances reliability by providing dispatchable operating reserves in real time.

Real time prices, enhanced by an appropriately set ORDC will enhance the ability to finance new projects, by creating additional demand for real time operating reserves, and enhancing real time prices to resolve the missing money problem. Every action that occurs in the real time market flows through the term markets. Consequently, the increased demand and adders will actually support new construction, unlike the LSE obligation.

Adjustments to the ORDC that enhance the adder and increase demand for operating reserves, should be accompanied by a reduction in offer caps. Summer suggests a $5,000 offer reflects a reasonable estimate for the value of lost load.

IV. ANSWERS TO SPECIFIC QUESTIONS

1. **The ORDC is currently a "blended curve" based on prior Commission action. Should the ORDC be separated into separate seasonal curves again? How would this change affect operational and financial outcomes?**

[5] *Electricity Scarcity Pricing Through Operating Reserves*, William W. Hogan, (April 25, 2013).

The ORDC should be changed to seasonal curves. Seasonal curves will create higher adders during seasons where the probability of losing load is higher. This provides a better price signal than a blended curve.

2. **What modifications could be made to existing ancillary services to better reflect seasonal variability?**

Changes to the ORDC will resolve the price signal for seasonal variability. Ancillary service changes are unnecessary. Attempting to resolve these issues with AS changes is not preferable, as AS markets are illiquid and difficult to hedge. The ORDC is hedged with energy contracts, which are liquid. The ORDC also provides ERCOT with flexibility to convert the reserves into energy as needed rather than rely on the dispatch parameters of a particular AS.

3. **Should ERCOT develop a discrete fuel-specific reliability product for winter? If so, please describe the attributes of such a product, including procurement and verification processes.**

    a. **How long would it take to develop such a product?**

    b. **Could a similar fuel-based capability be captured by modifying existing ancillary services in the ERCOT market?**

Changing the ORDC to seasonal and implementing the correct inputs should create appropriate winter price signals. To the extent that it doesn't the Commission can explore changing the MCL seasonally.

4. **Are there alternatives to a load serving entity (LSE) Obligation that could be used to impose a firming requirement on all generation resources in ERCOT?**

There is no appropriate way to create a firming requirement without either imposing undue risk on LSEs or forcing the obligations down to the customer level. Neither of these options are appropriate given the fact that the issues can be addressed by changing the MCL of the ORDC.

5. **Are there alternatives to an LSE Obligation that could address the concerns raised about the stakeholder proposals submitted to the Commission?**

The best alternative is to address issues relating to price signals directly with changes to the MCL of the ORDC, rather than making indirect attempts that are ineffective and cause more harm.

6. **How can an LSE Obligation be designed to protect against the abuse of market power in the wholesale and retail markets?**

   a. **Will an LSE Obligation negatively impact customer choice for consumers in the competitive retail electric market in ERCOT? Can protective measures be put in place to avoid a negative impact on customer choice? If so, please specify what measures.**

   b. **How can market power be effectively monitored in a market where owners of power generation also own REPs that serve a large portion of ERCOT's retail customers?**

   c. **What is the impact on self-supplying large industrial consumers who will have to comply with the LSE Obligation and will it impact their decision to site in Texas?**

   d. **What is the impact of an LSE Obligation on load-serving entities that do not offer retail choice, such as municipally owned utilities or electric cooperatives?**

   e. **Can market power be monitored in the bilateral market if an LSE Obligation is implemented in ERCOT? Can protective measures be put in place to ensure that market power is effectively monitored in ERCOT with an LSE Obligation? If so, please specify what measures.**

   f. **Should the LSE Obligation include a "must offer" provision? If so, how should it be structured?**

As discussed previously, the Proposed LSE Obligation will certainly harm retail competition. It will create an additional cost to LSEs that estimated conservatively would be a requirement to purchase 60% more energy for 15 months, without a single customer contractually obligated to purchase it. In the example, that would be essentially a cost equivalent to the original supply cost.

7. **How should an LSE Obligation be accurately and fairly determined for each LSE? What is the appropriate segment of time for each obligation? (Months? Weeks? 24 hour operating day? 12 hour segments? Hourly?)**

The only way to accurately and fairly determine an LSE Obligation would be limiting the obligation to customers under contract at their contract term. Any other methodology puts undue risk on the LSE.

8. **Can the reliability needs of the system be effectively determined with an LSE Obligation? How should objective standards around the value of the reliability-providing assets be set on an on-going basis?**
   a. **Are there methods of accreditation that can be implemented less administrative burden or need for oversight, while still allowing for all resources to be properly accredited?**

   b. **How can winter weather standards be integrated into the accreditation system?**

The reliability needs can be easily met by adjustments to the MCL of the ORDC. Those adjustments provide direct operating reserves to ERCOT, immediately improving reliability. The adjustments also provide a scarcity price signal, before reliability problems occur. That price signal is incorporated into forward markets which enhance the ability to finance new projects. This method is far superior to any other being considered.

9. **How can the LSE Obligation be designed to ensure demand response resources can participate fully and at all points in time?**

If the Commission adopts an LSE Obligation, it should also order ERCOT to develop demand response products that allow LSEs to contract with loads to meet the obligation. Those products must include the ability for an LSE to contract with a demand resource that it does not represent as an LSE.

10. **How will an LSE Obligation incent investment in existing and new dispatchable generation?**

As discussed above, the best case is a trivial change in financing costs for a new project. That benefit is dwarfed by, and made superfluous, by correcting real time price signals.

11. **How will an LSE Obligation help ERCOT ensure operational reliability in the real-time market (e.g., during cold weather events or periods of time with higher than expected electricity demand and/or lower than expected generation output of all types)?**

An LSE Obligation will not help operational reliability in real-time, unless the minor change in financing costs results in a project being built, that would not be built, but for the minor change in financing costs. This is highly unlikely. As discussed, the change in financing costs would be trivial under the absolute best conditions.

12. What mechanism will ensure those receiving revenue streams for the reliability services perform adequately?

The only mechanism is enforcement of the contract entered into by the LSE.

13. What is the estimated market and consumer cost impact if an LSE obligation is implemented in ERCOT? Describe the methodology used to reach the dollar amount.

Summer provided an estimate based on conservative numbers. Attachment 1 outlines the calculations and includes a reasonable estimate of potential impacts. The cost of an LSE Obligation can easily be a contractual obligation for the LSE to contract for significant amounts above the 100% of the supply the LSE is contracted to provide.

14. How long will the LSE Obligation plan take to implement?

If the Commission adopts an LSE Obligation, it should phase it in over a period of no less than 5 years.

15. If the Commission adopts an LSE Obligation, what assurances are necessary to ensure transparency and promote stability within retail and wholesale electric markets?

There is no way to ensure stability with the LSE obligation being proposed. That obligation will disrupt the retail market resulting in extraordinary risk being forced on LSEs.

16. Are there relevant "lessons learned" from the implementation of an LSE Obligation in the SPP, CAL-ISO, MISO, and Australian markets that could be applied in ERCOT?

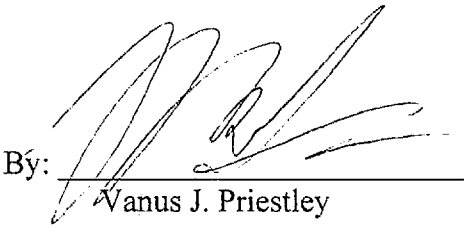
Summer suggests the Commission review capacity markets, which are similar to the LSE Obligations proposal. Both have forward contracting requirements. However, a capacity market typically only requires a purchase of installed capacity and not a complete energy hedge. The installed capacity obligation is typically only an obligation contract with a resource that is required

to make an offer within certain parameters. As problematic as capacity markets are, in this aspect they are an improvement to the LSE Obligation proposal.

The marginal cost of an obligation to make an offer, is much less than the marginal cost to provide energy. Consequently, an LSE holding installed capacity contracts won't take the same loss as an LSE holding energy contracts when prices fall.

To be clear, Summer opposes the implementation of an installed capacity market. Capacity markets, very much like the LSE Obligation proposal, result in unnecessary, sometimes extraordinary costs without a tangible reliability benefit.

Respectfully Submitted,



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	Time (Months)	Hedges in Place	Required Additional Purchases to Meet Obligation (Months)	Required Obligation (% of Load Under Current Contract)	Additional Purchases Required
LSE Weighted Average Term of Existing Contracts	9	100%	N/A	N/A	N/A
LSE Obligation					
1 Month Obligation	1	100%	0	0	0
6 Month Obligation	6	95%	0	0	0
12 Month Obligation	12	90%	3	90%	10%
24 Month Obligation	24	70%	12	70%	31%
36 Month Obligation	36	50%	12	50%	22%
Total Additional Purchases Required Above Contracted Load					**63%**

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SUMMER ENERGY'S EXECUTIVE SUMMARY

Any issues relating to Electricity Markets are corrected by accurate Real Time price signals. The ORDC (and Ancillary Services to a certain extent) create a buffer of reserves between typical and emergency conditions. The benefit of the ORDC, is the system can maintain reliability while incorporating price signals that show scarcity beyond the buffer, promoting conditions for new entry.

The clear, effective and obvious solution to the missing money problem is increasing the size of the buffer, which increases reliability by adding operational reserves, and improves scarcity pricing, enhancing long term resource adequacy.

The Load Obligation concept:

1. will not improve operational reliability;
2. will not materially change the factors used to calculate a hurdle rate; and
3. will create unnecessary burden and risk on Load Service Entities.

The burden's created by the proposed load obligation could easily end retail competition in Texas as we know it.