



## Filing Receipt

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**PROJECT NO. 54335**

<b>REVIEW OF MARKET REFORM</b>	<b>§</b>	<b>PUBLIC UTILITY COMMISSION</b>
<b>ASSESSMENT PRODUCED BY</b>	<b>§</b>	<b>OF TEXAS</b>
<b>ENERGY AND ENVIRONMENTAL</b>	<b>§</b>	
<b>ECONOMICS, INC. (E3)</b>	<b>§</b>	

**VALERO COMPANIES' COMMENTS:**

**REVIEW OF MARKET REFORM ASSESSMENT PRODUCED**  
**BY ENERGY AND ENVIRONMENTAL ECONOMICS, INC. (E3)**

On behalf of the Valero family of companies ("Valero"), Valero Refining-Texas, L.P. thanks the Public Utility Commission of Texas for the opportunity to comment on Project No. 54335, Review of Market Reform Assessment Produced by Energy and Environmental Economics, Inc. (E3).

Valero is one of the largest employers and taxpayers in Texas, owning and operating seven refineries in Texas—five inside ERCOT and two outside ERCOT. These refineries have nearly a million barrels per day of combined throughput capacity, are key suppliers of refined products in Texas and the country, and are dependent on having a reliable, uninterrupted supply of high quality electricity available 24 hours a day, 365 days a year, at the lowest and most reasonable cost.

As one of the largest consumers of electricity in ERCOT, Valero views the ERCOT market's ability to provide reliable and competitively priced electricity as absolutely essential to Valero's competitiveness and success in delivering critical transportation fuels and energy resources to the people and businesses of Texas and the entire country. ERCOT is the only US-based administrative market that is not a collection of separately regulated generating utilities. While this structure brings special benefits, it also brings with it particular regulatory—and in today's market, reliability—risks.

Valero is deeply invested in ensuring that regulatory changes to the ERCOT market address and improve current reliability and cost issues, and we oppose any potential market design changes that are contrary to those goals.

Reliable and reasonably priced electricity supply is crucial to every Texan, yet ERCOT's prices continue to rise while we contend with an increasing lack of reliable and dispatchable generation that is critically needed to mitigate the reliability risks of intermittent generation. To be clear, Valero is very supportive of the PUC's efforts to implement appropriate market redesign to address the electricity needs of the state. To this end, we encourage the PUC to address several outstanding questions in its analysis of the Performance Credit Mechanism (PCM), and to also consider whether the Independent Market Monitor (IMM's) Uncertainty Product or competitively bid direct procurement (formerly called the "Berkshire Proposal") would be superior from a price and reliability perspective. We urge the PUC to carefully consider and understand all reasonable competing proposals before making a decision on ERCOT reform.

## **Responses to PUC's Questions**

**1. The E3's report observes that the Performance Credit Mechanism (PCM) has no prior precedent for implementation, does this fact present a significant obstacle to its operation for the ERCOT market?**

Yes, Valero thinks that lack of prior precedent is a significant concern with the PCM. Uncertainty around modeling decisions and outputs may be greatest with the PCM because it's the least tested.

**2. Would the PCM design incentivize generation performance, retention, and market entry consistent with the Legislature's and the commission's goal to meet demand during times of net peak load and extreme power consumption conditions? Why or why not?**

Valero's view is that it is premature to pick PCM as the preferred route without additional analysis and understanding of the PCM as compared to other E3 alternatives, the IMM's Uncertainty Product, and competitively bid direct procurement.

**3. What is the appropriate reliability standard to achieve the goals stated in Question 2? Is 1-in-10 loss of load expectation (LOLE) a reasonable standard to set, or should another standard be used, such as expected unserved energy (EUE). If recommending a different standard, at what level should the standard be set (e.g., how many MWh of EUE per year)?**

Any LOLE standard has a significant market impact (by creating an implied Value of Lost Load ("VOLL") that, in some cases, can be astronomically high) and should not be picked based only on historical practices or conventions. In fact, we think the proper LOLE standard is the most important decision in this market redesign project, because it is the variable against which everything else will be solved. 1-in-10 is a well-established standard with a long history, but it may not remain the best choice for ERCOT's unique and changing market with increased variability of supply and long-term demand growth. The PUC should seek separate input, regardless of what market design is chosen, from multiple stakeholders based on a realistic assessment of the implied VOLL.

**4. The E3 report examines 30 hours of highest reliability risk over a year. Is 30 the appropriate number of hours for this purpose? Should the reliability risk focus on a different measure?**

Even 30 hours may be too many, creating scenarios in which Performance Credits ("PCs") are awarded during hours when there's no real reliability risk to the grid. That's a downside of the PCM that cannot be designed out—the right number of hours is going to be, at best, an educated guess of how many "emergency" hours will exist in an average year, and by definition the guess will either be too low or too high. One idea that seems problematic would be to carve the reliability risk by calendar quarter. This would serve to create implied emergency conditions during moderate weather periods (spring and fall) when demand is usually much lower. Any standard must target known and expected periods of shortage.

**5. Over what period should the hours of highest reliability risk be determined? A year, a season, a month, or some other interval? At what point in time should that determination be made?**

See above at response 4. Any other model implying grid emergencies during periods where they don't exist would be counterproductive.

**6. Would a voluntary forward market for generation offers and a mandatory residual settlement process for Load Serving Entity procurement provide additional generation revenue sufficient to incentivize resource availability in a way that improves reliability?**

Any proposed forward market must incentivize reliable dispatchable generation at a reasonable cost. For the reasons noted above, Valero remains skeptical that the PCM is the best alternative.

**7. Does a centrally cleared market through ERCOT sufficiently mitigate the risk of market power abuse? Should additional tools be considered?**

A new forward generation market introduces new opportunities for market power abuse. FERC has tackled similar concerns with rules around independent trading/marketing vs. operations functions, including affiliate standards of conduct. Such rules would be a novel undertaking for the PUC.

**8. If the commission adopts a market design with a multi-year implementation timeline, is there a need for a short-term "bridge" product or service, like the Backstop Reliability Service (BRS), to maintain system reliability equivalent to a 1-in-10 LOLE or another reliability standard? If so, what product or service should be considered?**

Texas needs relief now through some version of a shorter timeline product. A proposal for competitively bid direct procurement of power (formerly called the "Berkshire Proposal") and the IMM's Uncertainty Product merit a full evaluation to determine whether, in whole or in part, they would be adequate interim and incremental steps to improving cost and reliability. Valero notes that direct procurement is the only way to truly guarantee "steel in the ground" in the form of new reliable dispatchable generation.

**9. If implementing a short-term design as a "bridge" delays the ultimate solution, should it be considered? Is there an alternative to a bridge solution that could be implemented immediately, using existing products, such as a long-term commitment to buy the additional 5,630 MW of Ancillary services necessary to achieve the 1-in-10 LOLE reliability standard?**

Yes, the costs and benefits of such a hybrid proposal should be fully quantified and considered. All options should be on the table. Texas deserves nothing less.

**10. What is the impact of the PCM on consumer costs?**

This has yet to be answered. What we do know is that it will be expensive—the E3 report estimates \$5.7B per year, but the real cost is not known. E3's view that those costs will be

mostly offset relies on market assumptions and modeling (essentially educated guesses), which may be inaccurate especially regarding retirements and new generation installation. Valero understands that reliability has a cost, particularly in the context of overcoming risks associated with intermittent generation. But we urge the PUC to carefully consider alternatives cited above to ensure the PCM is really the least expensive way to achieve stated reliability benefits.

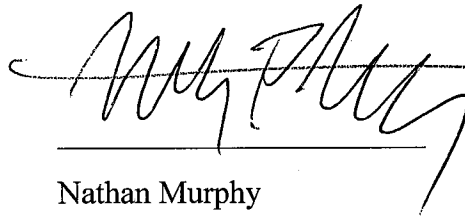
**11. What is the fastest and most efficient manner to build a "bridge" product or service, such as the BRS, in order to start sending market signals for investment in new and dispatchable generation, while a multi-year market design is implemented by ERCOT? Please provide specific steps.**

The IMM's Uncertainty Product, if ultimately chosen, could be implemented rapidly, although we note again that its benefit has yet to be proven and needs to be further studied. The direct procurement plan might be delayed—maybe significantly—because of the permitting that would be required. A reasonable path to encourage timely agency review and approval would be a crucial feature to enhance the direct procurement alternative.

**12. In what ways could the Dispatchable Energy Credit design be modified through quantity and resource eligibility requirements, e.g., new technology such as small modular nuclear reactors, in such a way that it incentivizes new and dispatchable generation?**

Valero agrees with E3 that the Dispatchable Energy Credit is not the preferred alternative. By favoring new builds at the expense of existing builds, it seems likely the DEC proposal would accelerate retirements and take dispatchable reliable generators off the grid just when they are needed most.

Respectfully Submitted,

A handwritten signature in black ink, appearing to read 'Nathan Murphy', is written over a horizontal line.

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<b>REVIEW OF MARKET REFORM</b>	<b>§</b>	<b>PUBLIC UTILITY</b>
<b>ASSESSMENT PRODUCED BY</b>	<b>§</b>	<b>COMMISSION OF TEXAS</b>
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**EXECUTIVE SUMMARY OF VALERO COMPANIES' COMMENTS:**  
**REVIEW OF MARKET REFORM ASSESSMENT PRODUCED**  
**BY ENERGY AND ENVIRONMENTAL ECONOMICS, INC. (E3)**

- Valero is a major consumer in ERCOT and very concerned that ERCOT provides reliable power at the lowest reasonable cost. Regulatory changes to the ERCOT market must address and improve existing cost and reliability issues.
- Valero does not oppose E3's PCM proposal at present, but does think there are several open questions to be answered before it should be chosen as the preferred alternative for Texas. These questions include:
  - The risk created by the lack of prior precedent;
  - Whether putting more money—even well-targeted money—into the market will incentivize new reliable dispatchable generation or prevent historical assets from retiring, instead of simply creating rent-seeking opportunities for existing resources;
  - Whether the historical 1-in-10 LOLE standard remains relevant in ERCOT's variable market;
  - How to prevent generators from gaming the system; and
  - How well E3 has forecast the costs the PCM would impose on Texas consumers.
- In light of these open questions, Valero also encourages the PUC to continue studying the PCM and also study whether the IMM's Uncertainty Product or competitively bid direct procurement might be superior from a price and reliability perspective.