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PROJECT NO. 54335

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

CALPINE CORPORATION'S COMMENTS
IN RESPONSE TO COMMISSION QUESTIONS

Calpine Corporation ("Calpine") is headquartered in Houston and has a geographically diverse fleet and operations across 22 states with significant scale in the ERCOT, CAISO, and PJM competitive wholesale markets. Our Texas fleet utilizes combined cycle and cogeneration technologies and supplies approximately 9,000 MW of generation to the ERCOT wholesale market. We take great pride in owning and operating a modern, clean, environmentally efficient, and reliable fleet and seek to be a positive contributor in the communities where our plants are located. Calpine welcomes the opportunity to provide feedback to select questions.

I. GENERAL COMMENTS

Calpine appreciates the changes the Public Utility Commission of Texas ("Commission" or "PUCT") has undertaken through Phase I market design reforms to improve the reliability of the ERCOT market. As the Commission reviews Phase II reforms, Calpine encourages consideration of the following first principles for any market design changes: (1) continued reliance on market signals for creating private at-risk investment instead of moving toward a central planning mechanism with discriminatory side payments that erode investor confidence and create a cycle of ever-increasing side payments; 2) reforms should define a reliability standard to meet the needs of the ERCOT region and adopt a set of rules that achieve that standard; (3) ERCOT's market design should recognize capabilities and limitations of various resource types,

such that payments will occur based on the operational performance attributes of the resources the Commission is seeking to attract or retain, such as dispatchable resources; and (4) market design should be principle-based, durable, and predictable with clear rules that will allow risk capital to fund development.

Principle 1, above, is particularly important. Calls for discriminatory side payments to be made exclusively to new capacity, even if limited in scope, or for state-backed procurements should be rejected. These programs seek to allocate risks away from resource developers and impose them on consumers through non-bypassable charges, and also undermine competitive markets in the long term by chilling new investment and causing early retirements of resources that do not receive similar compensation. Calpine's experience in markets outside of Texas has confirmed that once out-of-market actions are implemented, there is a chilling effect on the use of risk capital to build new capacity. For example, Calpine has experience in other states where the state government has stepped in to execute long-term generation contracts directly with market participants in a process outside of the competitive market. Since that happened, no investment has been made in generation unless tied to a government guarantee or directive, at which point all risk is placed upon consumers. Calpine urges the Commission to reject these calls for discriminatory side-payments to preserve the efficiency found within robust competition and risk capital.

Calpine has also observed market complaints regarding operational issues associated with the use of reliability unit commitments ("RUC"), ancillary services ("AS"), and AS procurement quantities. These types of issues are operating issues and are different from long-term resource adequacy problems. Calpine encourages the Commission, ERCOT and stakeholders to continue to focus on both issues, but not to conflate solutions associated with real-time operation with

capacity solution signals for dispatchable resources that typically require multi-year development cycles. The market should proceed on both operational efficiency issues and signals for long-term capacity and make progress in parallel on both matters.

II. RESPONSES TO SELECT QUESTIONS

1. The E3 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?

No. Calpine believes that the best market redesign solution for ERCOT is one achieved through principled reforms that require developers and asset owners to bear risk through performance. While the PCM is an emerging concept, at its heart, it is straight-forward and requires market performance and availability to create the performance credits associated with a reliability standard. The ERCOT market has a long history of successfully implementing concepts nascent to Texas, including deregulation in 1999 through 2002, implementation of a nodal market, creation of a Renewable Portfolio Standard and a supporting compliance program, adoption of Competitive Renewable Energy Zones (“CREZ”) and selection of CREZ providers, and development of the Operating Reserve Demand Curve (“ORDC”). Texas has a proven history of successfully implementing new market measures akin to the PCM when they are right for Texas and can do it again if given the appropriate resources and Commission oversight during critical decision periods.

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?

Yes. The key to achieving the goal of meeting demand at all times is for the Commission to adopt a reliability standard and implement a fair, non-discriminatory market construct to achieve that standard. While various mechanisms can attract investment and retain generation performance, including shifting the ORDC as has previously been advocated by Calpine, the PCM

could also work and, critically, it puts policy makers in control of the level of reliability they want to achieve through adoption of a standard that is linked to a demand curve. The PCM includes many favorable attributes including better control of the reliability dial through the process to establish the PCM demand curve. It also eliminates issues associated with forecasting reliability contributions of different resource types since payment is based on actual performance. Additionally, the PCM can be technology-neutral and non-discriminatory. From a cost perspective, the PCM creates incentives for customers to reduce costs through demand response during key measurement periods.

In the meantime, if there are concerns about the PCM implementation timeline and potential implications for reliability, the Commission can adopt a non-discriminatory interim step to bolster reliability by implementing enhancements to the ORDC, such as increasing the value of X, while the PCM and underlying compliance system is established.

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)?

Calpine supports a reasonable LOLE standard that is in-line with societal expectations for reliability. Such a standard may also be enhanced by an expected unserved energy standard to limit the depth of an LOLE. Calpine recommends that the Commission explore these concepts in a more fulsome manner through a separate project in early 2023 to evaluate the appropriate metrics that should determine what constitutes Resource Adequacy. Calpine believes that the separate project can be run simultaneously with market design reforms to implement the PCM, since a reliability standard would be an input to the amount of PCM that ERCOT would need to clear. The key is to determine the standard for reliability and *then* adopt market mechanisms to ensure the reliability standard is achieved. This project can also be used to “stress test” a standard against

reformed resource adequacy reports and decide what assumptions are appropriate to include in reporting.

Calpine does not provide any comments with respect to Question Nos. 4 – 12 enumerated in the PUCT's Public Notice of Request for Comments.

III. CONCLUSION

Calpine appreciates this opportunity to present our views on this very important matter and will remain engaged as this rule develops. We will make available representatives to discuss these positions if helpful to the Commission.

Respectfully submitted,

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EXECUTIVE SUMMARY OF CALPINE CORPORATION'S COMMENTS
IN RESPONSE TO COMMISSION QUESTIONS

- Calpine encourages the Commission to consider the following first principles for any market design changes: (1) continued reliance on market signals for creating private at-risk investment instead of moving toward a central planning mechanism with discriminatory side payments that erode investor confidence and create a cycle of ever-increasing side payments; 2) reforms should define a reliability standard to meet the needs of the ERCOT region and adopt a set of rules that achieve that standard; (3) ERCOT's market design should recognize capabilities and limitations of various resource types, such that payments will occur based on the operational performance attributes of the resources the Commission is seeking to attract or retain, such as dispatchable resources; and (4) market design should be principle-based, durable, and predictable with clear rules that will allow risk capital to fund development.
- Any calls for discriminatory side payments to be made exclusively to new capacity, even if limited in scope, or for state-backed procurements that remove developer risk are myopic and undermine ERCOT's competitive markets in the long term. Calpine's experience in markets outside of Texas has confirmed that once out-of-market actions are implemented, there is a chilling effect on the use of risk capital to build new capacity.
- While the PCM is an emerging concept, at its heart, it is straight-forward and requires market performance and availability to create the performance credits associated with a reliability standard. The ERCOT market has a long history of successfully implementing concepts nascent to Texas and can do it again with the PCM if given the resources and appropriate oversight during critical decision periods.
- Calpine believes PCM can put policy makers in control of the level of reliability they want to achieve through adoption of a standard that is linked to a demand curve. The PCM includes many favorable attributes, can be technology-neutral and non-discriminatory, and will create incentives for customers to reduce costs through demand response during key measurement periods.
- Calpine supports a reasonable LOLE standard that is in-line with societal expectations for reliability. Such a standard may also be enhanced by an expected unserved energy standard to limit the depth of a LOLE. Calpine recommends that the Commission explore these concepts in a more fulsome manner through a separate project in early 2023 to evaluate the appropriate metrics that should determine what constitutes Resource Adequacy, which can run in parallel with implementation of the PCM. The key is to determine the standard for reliability and *then* adopt market mechanisms to ensure the reliability standard is achieved.