Stakeholder Comments Template

Submitted by	Company	Date Submitted
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1. Summary

Calpine supports RMR reform, but only in the context of, and only after we understand overall RA market reform. In fact, several significant modifications to the RA programs are under consideration (see CPUC R17-09-020) driven in part, by the significant use of CAISO backstop mechanism in 2018. That said, the CAISO backstop mechanisms did not appear to be broken and worked precisely as designed. The RA reforms hold the promise of greatly eliminating the need for backstop mechanisms by including the adoption of multi-year forward local capacity requirements, enforcement of sub-area requirements and considering a central procurement agent (a role that some have suggested be performed by CAISO.)

Many participants in the CAISO RMR/CPM stakeholder meeting would agree that CAISO modifications to RMR and CPM, if any are found to be just and reasonable and made in isolation, would make an insignificant difference in the retention and management of needed reliability resources. Rather, the CAISO should suspend this initiative and redouble its efforts to ensure that the RA mechanism (either as part of its own tariff, or the procedures delegated to the LRAs) secure the right resources. And importantly, the CAISO and CPUC should modify processes such that the resources are secured with a reasonable runway for the existing, just and reasonable backstop mechanisms to operate efficiently.

2. Comments on phase 1 draft final proposal to make RMR units subject to a must-offer obligation.

Calpine does not support the imposition of a must-offer obligation ("MOO") on Condition 2.

First, allowing or forcing a subsidized unit to run at incremental costs has a negative impact on energy prices and hastens the financial distress on other market-based units. Before imposing a MOO, the CAISO should simulate the price effects of rapid expansion of C2 units – for instance, by assuming that 5000 MW of thermal capacity was placed on C2.

Second, basing the imposition of a MOO on DMM's misplaced representation of a market "distortion" (because prices would rise without a MOO) is shortsighted, and is based on an improper characterization of FERC standards implying that rates are only "just and reasonable" as they relate to "consumers." Certainly, FERC's evaluation of what is just and reasonable considers all market participants, not just consumers. A MOO which drives down market prices to short-run marginal costs is good for consumers in the short run, but very bad for consumer costs in the long run.

Third, the ISO's primary, maybe sole motivation to "bolt on" a MOO to Condition 2 is "to make RMR units function more like RA." It seems nonsensical to pattern RMR to a mechanism that itself has failed to secure and compensate the resources needed for reliability.

Calpine does not object to a must-offer on Condition 1 units, as it is consistent with the market incentives inherent in C1.

3. Comments on phase 1 draft final proposal for ISO to provide notification to stakeholders that a resource is planning to retire.

Calpine does not object to disclosure of those units that are seeking an evaluation of the reliability-based need for that resource.

We do, however, assert that notice of "retirement" is too narrow and should include all forms of unavailability permitted under the tariff. This would include a notice of termination of the PGA, removal of units from the PGA schedule 1, mothballing, and repowering requests.

We also support a similar market participation notification when the reliability analysis is completed.

4. Counting Flex Attributes

The CPUC has suggested that as part of phase 1 that the CAISO establish a method for counting and allocating the flexible attributes of RMR resources. Calpine supports the proposal to reduce the overall demand for Flexible Capacity as a result of RMR contracting.

5. Comments on potential phase 2 items.

Calpine comments below on several, but not all of the proposed phase 2 items. Should the ISO choose to pursue these matters, Calpine will have more detailed comments.

Imposing MOO on Condition 2

Calpine believes that consideration of imposing a MOO on Condition 2 units should be deferred to a later phase of this initiative once more is known about the RA reforms.

Combining CPM and RMR

Calpine encourages the ISO to be more specific with respect to the tariff provisions it envisions might be subject to consolidation. If the ISO is suggesting that CPM Risk-of-Retirement designations (43A.2.6) be combined with RMR, Calpine supports that proposal. In fact, we believe that 43A.2.6 can be struck from the tariff with no ill consequences.

We continue to believe that all other designations under CPM (43A.2) continue to hold value and will be effective, and will operate better (if needed at all) if RA showings are required earlier in the calendar year (like June 1).

Review the Rate of Return in CPM and RMR

While Calpine does not object to an evaluation of the pre-tax Rate of Return ("RoR") built into the tariff, Calpine believes there are much higher reform priorities and this should be deferred. If the CAISO does reconsider the level of the "plug" RoR, it is likely that given the risks in this market Calpine will seek a higher, certainly not lower pre-tax RoR.

The 12.25 percent rate of return embedded in the RMR and CPM tariffs is a *pre-tax* number that cannot be compared directly with the commonly reported *after-tax*, debt/equity-adjusted IOU rate-of-return, or return-on-equity. In fact, to convert a *pre-tax* RoR to an *after-tax* RoR, the CAISO (and eventually, FERC) would have to determine the applicable tax rate of each project (not each entity), its debt costs, its equity costs and the ratio of debt-to-equity. It would also need to restructure Schedule F significantly in order to provide a "gross-up" for taxes. That is, since an after-tax RoR is subject to income taxes, the Schedule F formulas would have to be modified to increase the top line revenue requirement (Schedule F, Line 1(A)(1)) by this tax effect.

In addition, Calpine believes that the RoR for incremental capital expenditures would have to be significantly higher than 12.25 percent pre-tax to accommodate the related matters of highly accelerated depreciation and book-versus-tax timing differences.

<u>Simplify RMR Invoicing/Settlement</u>

After having navigated the RMR invoicing labyrinth, Calpine may be the most passionate advocate of RMR settlement simplification. The redundancy and administrative barriers drive to excessive transaction costs and delay. However, until the ISO has a better view of RA reforms – and the resultant demand for RMR contracting -- Calpine urges rational caution and reasonable expenditures on reform.

<u>Expand tariff authority under RMR</u>

Calpine does not object to a clarification of the ISO's authority to manage reliability, including, as necessary the acquisition of attributes (such as flexibility) necessary to manage reliability.

<u>Consider whether RMR Condition 1 and Condition 2 designations are still needed</u>

Calpine sees no need eliminate either Condition 1 or Condition 2 at this point. Consideration of such should only occur after a holistic review of RA reforms. In addition, the CAISO is currently evaluating operational options for storage (see Storage as a Transmission Asset) identical to the optional conditions of RMR. No limitations on RMR should be established that would be inconsistent with, or create undue discrimination with those proposed by the FERC Policy Statement on Storage Resources.

<u>Allow for capital additions</u>

As energy margins decline, it will be increasingly necessary to consider mechanisms to recover the costs of incremental capital. No rational business will invest incremental capital (for maintenance, flexibility or improvements) without a clear path to collect a return of (in the form of depreciation), and a return on (in the form of carrying costs, debt/equity) that investment. The ISO's backstop mechanism, whether RMR or a modified CPM, must include provisions to ensure that incremental capital earns a reasonable return.

6. Other Comments

No additional comments at this point.

Thank You.