Pacific Gas and Electric Company®

Reliability Must Run (RMR) and Capacity Procurement Mechanism (CPM) Enhancements

Submitted by	Company	Date Submitted
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PG&E provides the following comments on the Second Revised Straw Proposal published December 12, 2018, and discussed during the stakeholder call held December 20, 2018.

While progress has been made in some areas of the Proposal, overall, PG&E is concerned that core elements remain unchanged from previous versions despite serious flaws which will undermine the intent of reforming backstop procurement and providing a "holistic" process for generation at risk of early economic retirement. In FERC's order rejecting the CAISO's risk of retirement tariff revisions, it expressed concerns that resources needed for reliability "would likely offer, in the bilateral resource adequacy market, no less than the payment [the resource] expected to receive"[1] from the CAISO's backstop procurement process. The CAISO's proposal does not address the ability of resources to self-select designations based upon the procurement mechanism that provides the highest compensation and which therefore are likely to exceed what the resource could earn in a competitive market. A more comprehensive package of reforms is needed to avoid significant negative impacts on the competitiveness of procurement under California's Resource Adequacy (RA) program.

As an example, PG&E has commented since the beginning of this initiative on the loopholes that allow a generation resource owner to declare an "intent" to retire a unit in order to be studied for a possible RMR, only to then rescind or otherwise alter that stated intent when either the unit is found not to be needed for reliability (and therefore is ineligible for an RMR designation), or otherwise receives a better price offer through a bilateral or CPM route. **This fundamental flaw in the backstop procurement design still exists in the form of the mothball request, which is non-binding and easily rescinded or reversed by the generator, as discussed further below.**

PG&E provides the following specific comments regarding individual elements of the Proposal, but reiterates the overall concern that the Proposal, as crafted, does not meet the objective of providing a "holistic" process and will do little to avoid additional costly backstop procurement

[1] *Order on tariff revisions,* 163 FERC ¶ 61,023, Docket No. Docket No. ER18-641-000, April 12, 2018, P. 17: https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=14887575

in the future, while also distorting and perverting the incentives for cost-effective compensation for units with locational (or other) market power.

Capacity Procurement Mechanism (CPM) Compensation

Generally, PG&E agrees with the CAISO's direction to retain CPM as a separate form of backstop procurement from RMR, with separate compensation principles, so long as the distinction is preserved in the use of the two instruments. Where the same unit can "test the waters" and pursue an RMR designation, by refusing a voluntary CPM award and then threatening to mothball or retire (without committing definitively to do anything irreversible), this distinction breaks down. Therefore, PG&E believes the CPM compensation should be tailored in such a way as to minimize the discretion afforded to generation owners with locational (or other) market power, and dampen the incentive for the owner of a needed unit that has some degree of market power to navigate the process towards the most attractive compensation.

Unlike RMR, which CAISO has stated should only be used for needed units at risk of retirement, the CPM compensation is available for a unit that is – absent further evidence -- still economically viable and may continue to participate in the CAISO market with or without a backstop award (that is, regardless of any such award, it will continue to be available to the CAISO through exceptional dispatch, up to any limits on the physical capability of the plant). The CPM is for a unit that has not been procured bilaterally for a given period of time but is determined by CAISO to be the most economical way to meet a specific deficiency in the RA portfolio.

In order to provide appropriate economic incentives and avoid "front-running" of the bilateral market, the CPM compensation requires that there be some degree of competition and uncertainty as to whether the individual unit owner will receive the award for a given period. Where there are multiple units that can provide the same needed service, the CPM award can be made on a competitive basis via the Competitive Solicitation Process (CSP) spelled out in the CAISO tariff. The concern with compensation therefore arises for those units that have some degree of market power, due to insufficient competition, and where the unit owner therefore has the ability to seek its best and highest compensation up to the soft-offer cap (or else, by declaring a mothball or retirement and receiving cost-of-service compensation under an RMR).

PG&E believes the soft-offer cap is an appropriate upper bound on compensation for shorter duration CPM awards, as any short-term gains are unlikely to weigh significantly in long-term decisions for the unit owner (i.e. with respect to bilateral RA market participation or a binding retirement or mothball of the unit), but the cap should not be the default compensation for annual CPM designations and any market revenues should be credited against the cost of the resource. For units with locational market power to receive annual CPM designations, the unit owner should be allowed to seek compensation up to the cost of service rate (that is, Schedule F of the RMR) **with a credit back** of any net market revenues. Resources that have going forward costs that are less than their cost of service should be allowed to compete with other

resources, when they do not have market power, for an annual CPM designation **with a credit back of any net market revenues.** This aligns incentives and reduces the potential attractiveness of withholding or "front running" the bilateral market (in hopes of getting a more lucrative award via CPM).

Use of RAAIM for RMR Availability

CAISO has repeatedly advocated for the adoption of the Resource Adequacy Availability Incentive Mechanism (RAAIM) for RMR resources in order to reduce the accounting and invoicing complexity associated with the current RMR contract structure. Although PG&E agrees that reduced administrative burden can be a worthy goal, we remain unconvinced that it outweighs the risks in this instance. PG&E notes that CAISO has provided no cost estimate or description of the burden that would allow parties to compare the cost of RMR contract administration, as against the potentially significant reliability impacts of any loss of RMR availability due to inadequate incentives to maintain unit availability to meet specific RMR needs.

The CAISO proposal to apply RAAIM to RMR would provide RMR unit owners exactly the same incentive as applies for resources under RA and CPM contracts that are compensated quite differently. If the assessment incentives are identical then there is no basis for inconsistent compensation across the procurement platforms. PG&E agrees with Southern California Edison's repeated statement during multiple stakeholder meetings: ratepayers are paying a premium for a superior product with RMR; they should be getting that superior product in terms of unit availability.

PG&E's recent experience backs this up. The RMR resources in PG&E's territory were each designated for a specific distinct need -- either a local reliability contingency based on a specific local load profile or voltage support need. These specific needs do not necessarily coincide with the system needs for which the RAAIM assessment hours are developed and there is no reason to assume that a unit which is available only for the RAAIM hours would provide the reliability for which the RMR was designated.

PG&E contends that the RMR units, which are compensated at their full cost of service, should have a stronger incentive to be available at the specific times that match the specific needs for which they are being retained and not allowed to retire. These same units may then provide additional value through market participation at other times, leading to a reduction in overall RMR costs borne by customers. However, market participation of RMR units should only be allowed to the extent that doing so does not in any way impair or reduce their availability to meet the specific reliability need for which they were designated as RMR.

Rate of Return for RMR

PG&E agrees with the CAISO proposal to require the resource owner to propose and defend its rate of return in filing its individual RMR rate schedules at FERC.

RMR for system and flexible needs

The CAISO proposal seeks to clarify CAISO tariff authority to make RMR designations for units that meet system and flexible (and not only local) needs. PG&E continues to respectfully disagree with this aspect of the CAISO proposal. PG&E understands the use of RMR to be for resources without which the CAISO cannot reliably operate the grid. Under the current use for local resources, the CAISO has established a well-defined set of criteria and evaluation methodology to determine whether a specific resource is absolutely needed for reliable operation of the grid. However, the CAISO has not established (or even proposed to establish) a similar set of reliability criteria for flexible or system services, nor a methodology to evaluate the absolute necessity of a specific resource providing those services without which reliability would be compromised. PG&E does not believe it is prudent for the CAISO to have unfettered and unchecked discretion regarding capacity procurement that the CAISO is seeking with this request and opposes the expansion of CAISO procurement authority.

PG&E believes that, to the extent CAISO goes ahead with the current Proposal and asserts its authority to issue an RMR for system and/or flex in order to retain a specific unit, it should further specify a different cost recovery mechanism for such an RMR award. PG&E believes the costs of system and flex generation procurement should properly be allocated to load, akin to CPM, and unlike the current RMR treatment, which allocates costs via transmission charges to all customers in the relevant PTO's Transmission Access Charge (TAC) area. PG&E notes that there would be significant distortionary impacts among CAISO market participants if large amounts of generation procurement costs are to be contracted directly by CAISO and socialized to all customers via transmission charges.

Bridge Year RMRs

The CAISO proposal seeks authority to issue RMR designations for "year two" forecasted needs with bridge compensation in year one. This proposal not only results in over-procurement during year one but the "year two" need could fail to materialize when re-evaluated at the end of year one, leading to payments for unneeded capacity. PG&E objects to this element of the CAISO proposal.

"Mothball" Notification and Attestation for RMR

The CAISO proposes that mothball requests will be studied for RMR designation, identically to retirement requests. PG&E disagrees with this aspect of the Proposal.

Although CAISO proposes to require the same attestation by a Company officer as for a retirement, there is nothing definitive about a mothball request, which can either be rescinded

at any time prior to the effective date of the mothball[2], or the unit may mothball and then come out of mothball status with as little as a 30 day turnaround.[3] The CAISO proposal to treat a mothball request equivalently to a retirement for purposes of RMR assessment therefore permits price discovery for resources seeking to earn more than they would in a competitive market.

Additionally, as PG&E noted in previous comments, the timing to file mothball requests is inconsistent with the timing to file RMR agreements at FERC and the ability to rescind the request even with an officer attestation imposes minimal effort. The CAISO has not proposed additional rules that hold resource owners accountable for the attestations provided when alternatives are subsequently identified and the deficiency is mitigated without contracting for the unit in question.

For the above reasons, PG&E is concerned that the mothball request remains a significant loophole that risks undermining a more "holistic" backstop procurement process. If left as is, it is likely to lead to continued gaming by resource owners and unnecessary and excessive costs being borne by customers.

[2] On July 5, 2018, CAISO published for the first time its "Announced Mothball and Retirements List" spreadsheet, which included the request by Calpine to mothball the Gilroy Cogeneration unit, effective January 1, 2019. On or about November 26, CAISO updated the spreadsheet to reflect that its study work was complete and that the request to mothball the unit was granted (i.e. the unit was not found to be needed for reliability and no backstop contract would be awarded). It is PG&E's understanding that the unit owner, Calpine, was then able to immediately rescind its mothball request, before it had ever taken effect.

[3] Verbal statement of Carrie Bentley, WPTF, during the December 20 stakeholder meeting, in response to a question by PG&E, as to the minimum time for a resource to shutdown for mothball and then return to service.