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Houston Import Project

Calpine's Views in the Context of the Energy-Only Market

ERCOT Board of Directors Meeting
August 17th, 2010

Matters for Consideration – Houston Import Project

- The project is not necessary from a reliability standpoint,

"*It should be noted that the need to add additional import capacity into the Houston area was not considered to be necessary to meet reliability criteria in the timeframe of this analysis (2014) since the load in the area could reliably be served by generation in the Houston area and the existing import capacity.*" *Houston Import Project V.1.0, Introduction, pg. 3*

- No option met the economic planning criteria in all the alternative scenarios and Option #3 did not meet the economic planning criteria in the STP 3 and 4 scenario,

"*Option 3 was determined to be the preferred option. It was the only option that met the economic planning criteria in all alternative scenarios besides the STP 3 and 4 scenario.*"
Houston Import Project V.1.0, 4.4 Discussion of the Results, pg. 19

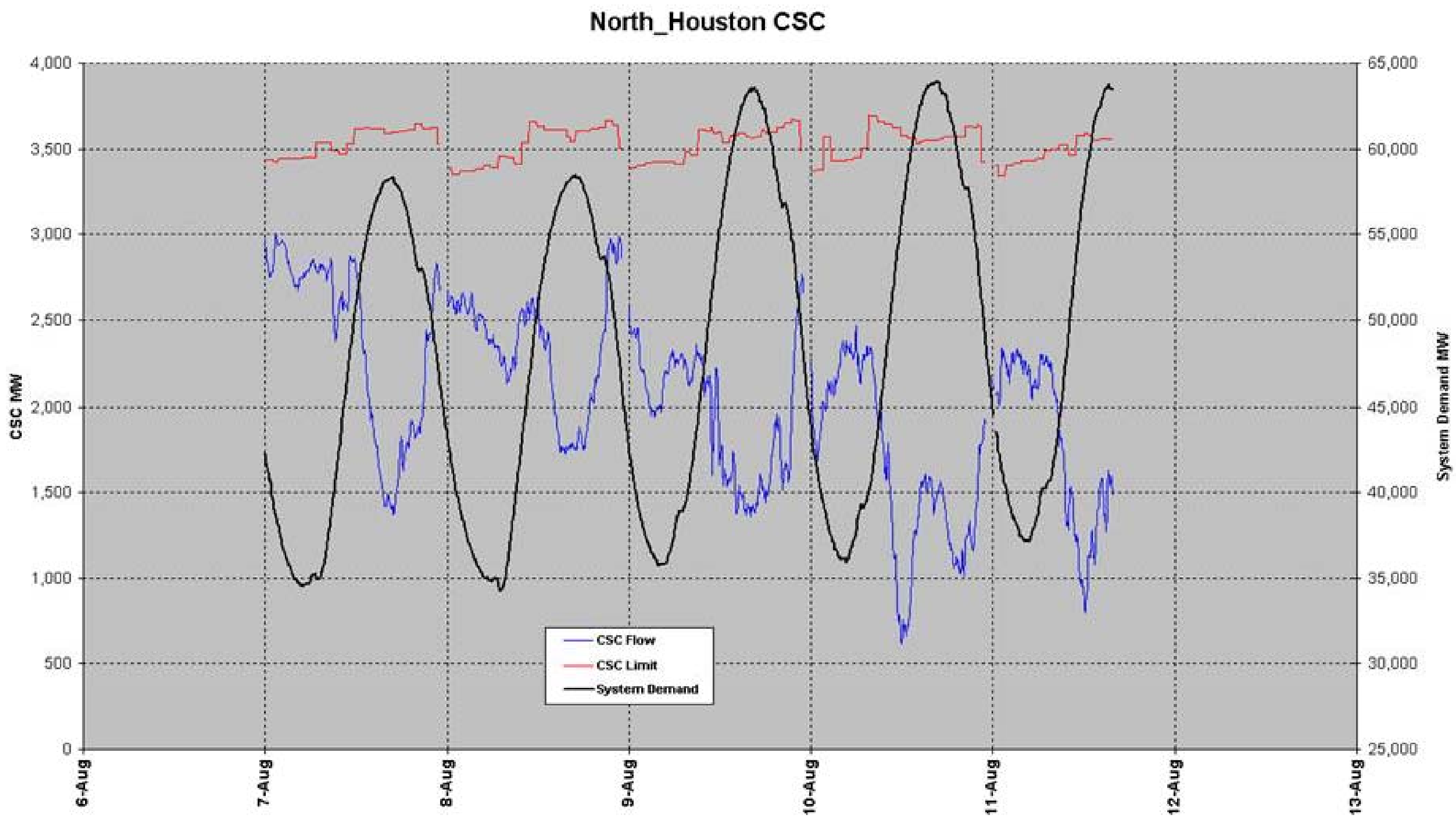
Matters for Consideration – Houston Import Project

- The sensitivity scenarios run in Phase III of the study indicate that new NG units were added in the Houston area in the model runs, yet the model assumptions did not appear to include the fact that the cost of new entry for simple cycle and combined cycle units have not been met in the Houston Zone recently,

"…the net revenue required to satisfy the annual fixed costs (including capital carrying costs) of a new gas turbine unit ranges from $70 to $95 per kW-year. The estimated net revenue in 2009 for a new gas turbine was approximately $55, $47 and $32 per kW-year in the South, Houston and North Zones, respectively. For a new combined cycle unit, the estimated net revenue requirement is approximately $105 to $135 per kW year. The estimated revenue in 2009 for a new combined cycle unit was approximately $76, $67 and $52 per kW-year in the South, Houston and North Zones, respectively." *Potomac Economics ERCOT State of the Market Report for 2009*

Matters for Consideration – Houston Import Project

- The North-Houston CSC rating has been more than adequate capacity during this summer's peak and a snapshot of recent data shows that the current week's load flows amount to less than half of the CSC's limit; these flows should be even further mitigated by the TNP One-East Bell County project that has an in-service date later in the year.



Matters for Consideration – Houston Import Project

- **The Houston Import Study's recommendation of Option #3 was based on estimated savings by in the reduction of generator revenue**

"…generator energy revenue savings greater than or equal to the approximate first year annual revenue requirement for the associated project." Houston Import Project, V1.0, 4.1, Phase 1, pg. 15

Calpine's overall observations:

1. *Using "reduced generator energy revenue" as the criteria for endorsing this project, within the context of an energy-only market design, is likely a flawed policy when reliability is not imminently at stake, and the ERCOT Regional Planning Group's Charter likely needs review and changes made.*

2. *Generator energy revenues, particularly true for the Houston Metropolitan Area, are part of "societal benefit" in the form of salaries, taxes and other contributions they make to the area's industrial base. To purposely attempt to reduce those revenues sends a counterintuitive market signal to investors and developers in this energy-only market.*

3. *As an initiative aimed singularly at reducing generator revenues, the Houston Import Project makes little sense with the advent of the Nodal design, which promises to significantly reduce generator revenues by itself through system-wide optimizations.* Should we not at least delay consideration of the project until we see what Nodal pricing does to the Houston Zone?

4. *The ERCOT Board of Directors should take a queue from the uncertainty of the TAC vote on this matter (20-0-9) and reject the project.*

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