



April 29, 2013

Mr. Gerry W. Cauley
President and Chief Executive Officer
North American Electric Reliability Corporation
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Suite 600, North Tower
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Subject: Your Letter of January 7, 2013

Dear Mr. ~~Cauley~~, *Gerry*

Thank you for your visit on March 5, 2013 to discuss your letter dated January 7, 2013. It was a pleasure to meet your Board Chair, Mr. Fred Gorbet, and your Board members Mrs. Jan Schori, and Mr. Roy Thilly.

ERCOT has been well aware of the concerns expressed. In recent years, ERCOT's long-term Capacity, Demand and Reserves report has indicated that planning reserve margins could drop well below our 13.75 percent target within the coming years without investment in new generation resources and demand response in this region.

As we discussed, the staff and Board of ERCOT consider electric reliability and future resource adequacy our top priorities. ERCOT and the Public Utility Commission of Texas (PUC) recognize our critical role in ensuring the lights stay on in a variety of conditions, and we continue to explore policy and market-based solutions to address future resource adequacy concerns.

As Chair Nelson described, our PUC and ERCOT have taken decisive action to address these issues. I've attached a copy of the list of actions taken and items currently under consideration that she shared with you.

Since our meeting, the PUC conducted initial workshops and requested stakeholder feedback on policy options for improving scarcity pricing signals, encouraging demand response, and developing alternatives for reports on current and future capacity and demand data. The ERCOT Board approved Emergency Response Service (ERS) demand response pilot projects for weather-sensitive loads and for loads able to respond in 30 minutes. ERCOT will review the efficacy of the pilot programs after the conclusion of the summer peak period.

I've also attached a copy of the graph I shared showing the upward trend of interconnection activity we have observed in the last twelve months.

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We are preparing to release our next Capacity, Demand and Reserves report on May 1. We currently anticipate a reserve margin slightly above our target for summer 2014. That's up from 10.9% in our December 2012 report. Since only a few generation projects have progressed to this level of certainty, we still see reserve margins below our target in the coming years. However, the future outlook has continually improved since 2011.

There is still work to be done on this complex issue, and there are no simple solutions. ERCOT and the PUC remain focused on future resource adequacy within the ERCOT region. I propose sharing updates with you approximately every six months on additional actions taken and the results we are seeing. Let me know if additional details are needed at this time.

Thanks,



H. B. "Trip" Doggett
President and CEO

Attachment A - Resource Adequacy Actions

Attachment B - Generation Interconnection Activity by Fuel

cc: W. Lane Lanford, President and CEO, Texas RE
The Honorable Donna L. Nelson, Chair, Public Utility Commission of Texas
The Honorable Kenneth W. Anderson, Jr., Commissioner, Public Utility Commission of Texas

Attachment A - Resource Adequacy Actions

The Commission and ERCOT are currently working on the following items related to the resource adequacy issue:

- Consider whether additional action is needed on demand response. The Commission is holding a workshop on this issue on March 14, 2013.
- Consider whether changes should be made to the methodology or inputs for the Capacity, Demand, and Reserves report. The Commission is holding a workshop on this issue on March 14, 2013.
- Consider whether to implement an operating reserve demand curve. The Commission is expected to discuss the procedural process for this issue at its March 28, 2013 open meeting.
- Consider whether to implement a pilot project for a weather sensitive loads ERS program. The ERCOT Board is expected to consider this issue at its March 2013 meeting.
- Set the target reserve margin in light of ERCOT's new loss of load probability study. The ERCOT Board is expected to address this issue in 2013.

The Commission and ERCOT have already taken the following actions to improve market signals and encourage investment in additional generating capacity:

- Impose offer floors for On-Line and Off-Line Non-Spinning Reserve capacity to minimize the impact of reliability-driven administrative interventions on the market. ERCOT implemented this change on January 5, 2012 (Nodal Protocol Revision Request (NPRR) 428).
- Release On-Line Non-Spinning Reserve energy to Security-Constrained Economic Dispatch without the need for ERCOT to issue a Non-Spin deployment instruction. ERCOT implemented this change on January 5, 2012 (NPRR 426).
- Impose offer floors for Responsive Reserve Service and Regulation Up used for capacity to minimize the impact of reliability-driven administrative interventions on the market. ERCOT implemented this change on January 5, 2012 (NPRR 427).
- Formalize the process used to enter into Reliability Must Run agreements with generators to meet capacity needs. ERCOT implemented the new process on March 1, 2012 (NPRR 432).
- Establish an offer floor for Reliability Unit Commitment (RUC) units deployed for capacity. ERCOT implemented this change on March 1, 2012 (NPRR 435).
- Increase by 500 MW the amount of Response Reserve Service procured by ERCOT and decrease by 500 MW the amount of Non-Spinning Reserve Service procured by ERCOT. ERCOT implemented this change on April 1, 2012 (ERCOT Methodologies for Determining Ancillary Service Requirements and NPRR 434).
- Hire the Brattle Group to study the resource adequacy issue and propose possible solutions. Brattle released its report on June 1, 2012.
- Adjust the compensation for RUC units brought online to provide local reliability and transmission relief and adjust the RUC claw-back. The ERCOT Board adopted this change on July 17, 2012 (NPRR 416).
- Increase the system-wide offer cap to \$4,500 per MWh. The PUC implemented this change on August 1, 2012 (Project No. 37897).

Attachment A - Resource Adequacy Actions

- Adjust the width, slope, and magnitude of the Power Balance Penalty Curve in light of the increase to the System Wide Offer Cap to \$4,500 per MWh. ERCOT implemented this change on August 1, 2012 (Setting the Shadow Price Caps and Power Balance Penalties in Security Constrained Economic Dispatch).
- Increase the system-wide offer cap to \$5,000 per MWh on June 1, 2013; \$7,000 per MWh on June 1, 2014; and \$9,000 per MWh on June 1, 2015. The Commission adopted these changes on October 25, 2012 (Project No. 40268).
- Adjust the Peaker Net Margin threshold and the Low System Wide Offer Cap. The Commission implemented this change on November 15, 2012 (Project No. 40268).
- Examine whether changes should be made to address price suppression resulting from the “0 to LSL problem” when a generation or load resource is deployed for reliability purposes. The ERCOT Protocol Revision Subcommittee is currently considering this issue (NPRR 444).

The Commission and ERCOT have also taken the following actions to remove barriers to storage technologies and to increase the amount of demand response that can be used when electricity supply threatens to exceed demand:

- Clarify rules regarding the regulatory treatment of energy purchased to charge a storage resource, including when such purchases may be considered wholesale transactions and when such purchases may be settled on a nodal basis. The Commission adopted these changes on March 7, 2012 (Project No. 39917).
- Adjust rules for the Emergency Response Service (ERS) program to allow participation by certain distributed generators and provide more flexibility to ERCOT to encourage greater participation in the program. The Commission adopted these changes on March 22, 2012 (Project No. 39948).
- Give ERCOT authority to conduct pilot projects for new technologies like battery storage and new services like 30-minute Emergency Response Service. The Commission adopted this change on May 18, 2012 (Project No. 40150).
- Explore distributed load demand response. ERCOT worked with CenterPoint and Oncor during the summer of 2012 to implement a demand response pilot program using aggregated electric load of participating customers.
- Expand the utility energy efficiency load management programs. The Commission directed utilities to expand their load management programs for the summer of 2012.
- Publish non-binding near real-time forward prices to allow electric loads to voluntarily reduce their usage in response to high prices. ERCOT implemented this change in June 2012 (NPRR 351).
- Develop a campaign to raise public awareness of energy conservation. Campaign elements include research, branding, messaging, television and radio public service announcements, a new website, media tours, video news releases, and public outreach. The Commission hired Sherry Matthews Advocacy Marketing to develop the campaign in April 2012. The micro website, powertosavetexas.com, launched on July 1, 2012, and the full website will launch by the spring of 2013.

Attachment B - Generation Interconnection Activity by Fuel

