

**Senate Committee on Business & Commerce  
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Chairman, Public Utility Commission of Texas**

**Resource Adequacy**

CSAPR

I would like to begin by providing an update regarding EPA's Cross-State Air Pollution Rule, or CSAPR. You may have already heard this news, but the federal appellate court in D.C. granted our motion for a temporary stay of the rule. It was set to go into effect on January 1<sup>st</sup> and would have caused two large generating units in ERCOT to cease operations. It would also have significantly increased electricity prices in the state. Given the potential for drought and high temperatures again this summer, the fact that these two generating units will be able to operate is very good news. The court plans to hear argument on the final merits of our legal challenge in April, with a decision to follow sometime after that.

## Generation Signals

The PUC has devoted significant time over the last nine months to make sure that our market rules incent developers to build new generation when needed. The PUC has already asked ERCOT to make a number of changes to market rules that I believe will improve the signals being sent to generators. These changes are technical but the general idea is that our market rules should minimize the distortionary effect of administrative tools that ERCOT uses to ensure reliability. We have seen some of those tools cause short term wholesale prices to fall during periods of scarcity. As you know, the wholesale market in ERCOT is an “energy only” market and not a “capacity market.” In an energy only market, generation companies get paid when they generate electricity. In a capacity market, generators get paid to install capacity and to generate electricity. Scarcity pricing is more critical in an energy only market, in order to allow companies to earn the money necessary to build additional generation plants. From an economic standpoint, during times of scarce supply, prices should rise to incent generators to bring their units online and to encourage electricity users to reduce their consumption. Again, the changes we are making to the market rules are technical but they are important. I don’t see any one of these changes as being a silver

bullet. Rather, we are looking at a number of things that, when taken together, should improve the market signals.

We also have rulemaking projects open to explore ways to remove barriers to storage technologies, including large scale compressed air energy storage and smaller scale storage like batteries and flywheels. While these technologies do not themselves generate electricity, they do allow us to store electricity generated when demand is low so that it can be consumed when demand is higher. They allow us to better use the variable resources like wind that tends to blow best at night.

### Demand Response

In addition to the steps we are taking to incent generation and storage, we are also looking at ways to expand demand response. Demand response is when users of electricity reduce their usage during times of scarcity. Some demand response happens passively, when users reduce their consumption simply because they see high prices. Other demand response happens through specific programs administered by ERCOT and the utilities.

For example, the PUC has a rule establishing a demand response program called Emergency Interruptible Load Service (EILS). This program is administered by ERCOT, and under the program, participants agree to reduce their electric usage during times of scarcity in exchange for a payment.

In December, the Commission proposed a new rule that would replace EILS with a new service known as Emergency Response Service (ERS). The purpose of the proposed new service is to increase the amount of demand response available to ERCOT over that provided by the current EILS service. The proposal seeks to achieve this by making several changes to the current service. The first proposed change would open the program to certain distributed generators. The current program is only open to electric loads providing demand response. Allowing small generators to participate should increase the total number of megawatts available to ERCOT. The second proposed change would give ERCOT greater flexibility in designing the program. For example, the current rule specifies that contracts with emergency response providers must be four months in duration. The proposed rule would allow ERCOT to determine the length of the contracts so that ERCOT can match the needs of program participants with the needs of ERCOT. In addition to these changes to EILS, I think we should also consider

whether changes to ERCOT's Load Acting As a Resource program need to be made to increase participation in that program.

ERCOT is also working with two utilities, CenterPoint and Oncor, on a pilot project that would use advanced meters and aggregate the electric load of participating customers. In times of electric scarcity, we would be able to reduce those customers' usage to help maintain grid reliability.

Also, on a related point, I am pleased to note that CenterPoint and Oncor announced the winners of their biggest energy saver contest in December. The contest was designed to encourage residential customers to leverage the power of their advanced meters to reduce electricity consumption. The grand prize winners of the contest, Rodrigo Reyna of Pflugerville and Mike Butler of Houston, achieved reductions of 39% and 36%, respectively. The top 10% of participants cut their usage by 26%. Encouraging smarter electricity consumption habits is one of the many ways that Texas will meet its energy needs in the future. Mr. Reyna and Mr. Butler attended a PUC open meeting in December and shared with us some of the ways that they reduced their usage. The things they did—from

simple things that all of us can do to more aggressive conservation steps—were truly remarkable. I would encourage you to visit with these individuals.

At the PUC's open meeting this week, I will propose that we get a group of people together to help craft our conservation message. We did a lot to promote conservation this past summer, but I think we need to start early this year to consider the best ways to engage customers while avoiding message fatigue.

One final point about demand response is that I expect to see more participation from industrial customers this summer. Electricity is the second biggest cost for many industrials, and I have been told that electric bills last summer were eye-opening. Many industrials discovered that it would make more financial sense for them not to operate during periods of very high electric prices even if that meant deviating from their production schedules. So I think we will see greater participation from industrials in demand response programs this year.

### **Rulemaking Activity**

In addition to the rulemakings I mentioned regarding storage and EILS, we have been working on several telecom rulemakings.

## Universal Service

SB 980 requires the PUC to initiate one or more proceedings to review and evaluate whether the Texas universal service fund accomplishes the fund's purposes and whether any changes are needed. The universal service fund was originally designed to help keep telephone rates in rural areas low and to help persons with low incomes and disabilities get phone service. It is funded by a surcharge that appears on telephone bills. We have established a number of projects to implement the universal service fund legislation. PUC staff held a workshop on the rulemaking for the large company fund last week, and we expect to publish a rule addressing that fund later this month. A contested case proceeding to implement the new rule will take place after the rule's adoption. We also expect to publish rules on the small company fund and on transparency and accountability issues toward the end of the spring. Our report to the Legislature describing all of these activities will be provided to you by November 2012.

## **Drought Conditions**

The PUC is working with ERCOT to assess the impact of current and anticipated drought conditions on electric generating capacity. ERCOT is researching and identifying those regions of Texas that will be most affected by drought. We are also working closely with the Texas Division of Emergency Management and the Texas Commission on Environmental Quality to ensure that all parties are preparing together. Trip Doggett will discuss ERCOT's drought response efforts in more detail. I would just note at this point that we only have predictions about the length of the drought and will continue to monitor the situation and act as necessary.

On the specific issue of incenting generators to build plants that use less water, I believe that market signals should encourage generators to address water issues. A generator that cannot operate because it runs out of water will lose money, so existing generators will be looking for ways to meet their water needs. And new generators that see water as an issue going forward will be looking to build new plants that use less or no water.



Finally, in response to SB 1133, the PUC hired Quanta Technology to prepare a report on Extreme Weather Preparedness Best Practices. The report will address a number of weather-related issues, including drought. Quanta Technology will make recommendations identifying the programs that will provide the maximum benefit per cost expended on both a state-wide and regional basis. We expect to provide their report to the Legislature by the end of September 2012.