

**UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION**

Centralized Capacity Markets	:	
in Regional Transmission	:	Docket No. AD13-7-000
Organizations and Independent	:	
System Operators	:	

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**COMMENTS OF THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

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**I. INTRODUCTION**

The Pennsylvania Public Utility Commission (PA PUC) submits the following Comments in response to the Federal Energy Regulatory Commission's (FERC) Notice Allowing Post-Technical Conference Comments issued October 25, 2013 at this docket number. The foregoing Notice was issued following FERC's September 25, 2013 Technical Conference convened to consider how current centralized capacity market rules and structures in the regions served by ISO New England, Inc. (ISO-NE), New York Independent System Operator, Inc. (ISO-NY) and PJM Interconnection LLC (PJM) are supporting the procurement and retention of resources necessary to meet future reliability and operational needs.

**II. BACKGROUND**

The PA PUC is the regulatory agency of the Commonwealth of Pennsylvania with the responsibility to ensure the provision of safe, adequate and reliable electric

distribution service at fair and reasonable rates to all Pennsylvania ratepayers. A significant part of that obligation includes the assurance that electric distribution companies (EDCs) subject to its jurisdiction have procured or otherwise possess sufficient generation supply to meet their service obligations.

The PA PUC was an early and active proponent of the regulatory shift to wholesale and retail competition. The Electricity Generation Customer Choice and Competition Act (Electric Competition Act) laid the groundwork for electric retail competition in Pennsylvania.<sup>1</sup> Shortly thereafter, FERC issued its landmark decision establishing the regional transmission organization (RTO) as the entity responsible for administering the centralized capacity market.<sup>2</sup> The PA PUC was an active participant in those proceedings in which the earliest phases of PJM centralized capacity markets were proposed and implemented.<sup>3</sup> PJM's current centralized capacity market dates to FERC's initial approval of the Reliability Pricing Model (RPM) in 2006.

The first PJM RPM Base Residual Auction (BRA) was held in 2007. Since 2007, there have been eight BRAs utilizing the RPM as the economic model for procuring capacity. During those years, the PA PUC has actively participated in proceedings at FERC wherein PJM's centralized capacity market model, RPM, has evolved to its current form. Most recently, the PA PUC filed comments in support of PJM's proposed revisions to its tariff provisions governing the Minimum Offer Pricing Rule (MOPR).<sup>4</sup>

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<sup>1</sup> Act of Dec. 3, 1997, P. L. 802, No. 138, § 4, effective Jan. 1, 1997 (codified at 66 Pa. C. S. §§ 2801-2812).

<sup>2</sup> *Regional Transmission Organizations*, Order No. 2000 (Dec. 20, 2000), 89 FERC ¶ 61, 285 (2000).

<sup>3</sup> *PJM Interconnection, LLC*, 117 FERC ¶61,331 (2006).

<sup>4</sup> *PJM Interconnection, LLC*, Order issued May 2, 2013 at Docket No. ER13-535-000.

Pennsylvania is centrally located within the PJM footprint with significant amounts of generation located within its borders. Pennsylvania is also a significant consumer of electricity for its industrial, commercial and residential load. The state is “ground zero” for the production of natural gas from the Marcellus Shale formation. This fuel source has greatly accelerated the shift away from coal-fired generation that has resulted in the increased rate of retirements of these base-load facilities in the PJM region coupled with a marked increase in construction of gas-fired generation facilities. Pennsylvania is also a major route for backbone transmission facilities for movement of electricity within PJM and to neighboring planning authorities such as the Midcontinent Independent System Operator (MISO) and the NYISO. Consequently, Pennsylvania has an ongoing interest in the successful functioning of centralized capacity markets.

The PA PUC appreciates FERC allowing it to provide comments in this important proceeding and looks forward to working with FERC in future stages of this docket.<sup>5</sup>

### **III. SUMMARY OF COMMENTS**

In its Notice, the FERC requested post-technical comments on five general topics:

1. Role of capacity markets and definition of capacity product;
2. Accommodating state policies and self-supply by load serving entities;
3. Market design elements;
4. Regulatory certainty; and
5. Next steps.

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<sup>5</sup> The PA PUC intervened in this proceeding on November 13, 2013.

Each of the general topics are divided into various sub-topics which request additional input on many technical aspects of the centralized capacity market. The PA PUC takes this opportunity to provide state regulator input on how the centralized capacity market in PJM has performed and to provide suggestions on how this market can be improved in the future. The Comments of the PA PUC may be summarized as follows:

1. Centralized capacity markets in PJM have been largely successful in promoting resource adequacy, price stability and reliable service.
2. Centralized capacity markets should function as a mandatory market for procuring capacity.
3. Certain capacity products specifically demand response and imported capacity should be subject to performance requirements in the delivery year to ensure resource adequacy.
4. FERC should continue to be aware of the need to preserve a competitive environment as it fashions solutions to self-supply issues and state sponsored generation resources.
5. FERC should, in the context of examining changes to market design elements that comprise RPM, be cognizant of the consequences of market participant decisions to close generation facilities. FERC should require market participants to provide reasonable assurance that there has been a full examination of alternatives to retirement before a decision to close a plant is made. This examination should encompass full evaluation of reliability and market impacts to allow for more effective generation and transmission solutions to be developed.
6. Any changes that FERC implements at this docket should consider the impacts of these changes on competition in retail choice states.
7. FERC should continue its examination of the centralized capacity market on an open, transparent and incremental basis.

## **IV. COMMENTS**

### **A. Role of Capacity Markets and Definition of Capacity Product.**

#### **1. The PJM's Centralized Capacity Market Construct Has Been Largely Successful.**

The PA PUC has been an active participant in the regulatory proceedings that have shaped the current RPM capacity mechanism. In PJM's earliest filing seeking approval of the RPM mechanism, PJM characterized its initial goals in establishing the key design elements of RPM as "a three-legged stool" as follows:

1. A liquid energy market providing competitive supply and demand options for customers to meet their short-term needs and price transparency to support their long term bilateral arrangements;
2. An independent regional transmission process that produces transmission solutions that support economically efficient and competitive wholesale energy and capacity markets; and
3. A forward capacity market to ensure the availability of necessary resources that can be called upon to ensure the reliability of the grid.<sup>6</sup>

Since approval of the RPM, PJM has conducted eight BRAs. During that time, PJM and its stakeholders have consistently worked to refine the RPM mechanism. Although some deficiencies exist, the PA PUC submits that the RPM mechanism has generally functioned well in accomplishing the aforementioned objectives first proposed by PJM in 2006.

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<sup>6</sup> Statements of Audrey Zibelman and Andrew Ott at Docket No. ER05-1410-000 at 4.

Some of the more significant results of the RPM mechanism were highlighted by the Brattle Group in its most recent assessment report in 2011<sup>7</sup>:

- Since RPM was implemented, the market has achieved its design objective of procuring sufficient capacity to meet reliability requirements. A total of 28,400 MW of gross additions of installed capacity (ICAP) from new resources were committed on an RTO-wide basis. These additions consisted of 11,800 MW of demand response (DR) resources, 6,900 MW of increased imports and decreased exports, 4,800 MW of new generation, 4,100 MW of plant uprates, and 800 MW of plant reactivations. These resource additions were partially offset by 15,300 of gross capacity reductions consisting of 5,000 MW of retirements; 2,700 MW of plant de-rates; 6,800 MW of capacity initially offered but withdrawn and 700 MW of generation excused from the auction. On balance, the amount of committed capacity has increased by 13,100 MW, more than enough to meet reliability requirements.<sup>8</sup>
- RPM has attracted and retained sufficient capacity to maintain resource adequacy in the RTO and all Load Deliverability Areas (LDAs), in spite of environmental and other challenges faced by suppliers. All regions have demonstrated capacity supplies in excess of their reliability requirements in all delivery years for which procurement was undertaken on a full three year forward basis.<sup>9</sup>
- On both an RTO and LDA-specific basis, sufficient capacity was procured under RPM to meet or exceed the reliability targets, with no significant capacity deficits. Procurement below the reliability targets in the eastern LDAs during the early years of RPM were due to overall tight supply conditions existing prior to RPM.<sup>10</sup>
- RPM has performed well despite proposed federal environmental regulations scheduled to take effect in the 2014/2015 delivery year. Despite announced retirements, capacity procurement through 2014/2015 (and in later years) exceeded the target procurement on an RTO-wide level.<sup>11</sup>
- Clearing prices in the base auctions have been consistent with market fundamentals clearing at levels below Net Cost of New Entry (Net CONE) during times and locations of capacity excess and above Net CONE at times and locations of relative scarcity. Large quantities of low-cost capacity additions from DR,

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<sup>7</sup> This report analyzed the results of the first eight auctions.

<sup>8</sup> The Brattle Group, *Second Performance Assessment of PJM's Reliability Pricing Model* at 49.

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

plant up-rates and increased net imports have resulted in prices below Net CONE in most locations.<sup>12</sup>

- Clearing prices in the incremental auctions have been persistently below BRA prices, in part reflecting low incremental demand for capacity due to declines in load forecast and increased transmission capabilities.<sup>13</sup>
- Contributions from DR particularly limited, extended summer and annual DR continues to increase contributing to product diversity but raising stakeholder concerns over the dependability of DR resources. In the 2014/15 BRA, demand side resources (DR and energy efficiency) accounted for 14, 900 MW of capacity or 9.4% of total resources committed.<sup>14</sup>

The Brattle Group Report, which is the most comprehensive review of the performance of PJM's RPM, was published in August 2011. Additionally, the performance of the capacity market is reviewed annually by the PJM Independent Market Monitor (IMM) in its State of the Market Report (SOM Report). The IMM analyzed market structure, participant conduct and market performance in the PJM capacity market for the first nine months of 2013 including supply, demand, concentration ratios, pivotal suppliers, volumes prices, outage rates and reliability. These reports have also highlighted the successes and some persistent shortcomings of the present capacity market model.

In its 2013 Report,<sup>15</sup> the IMM highlighted the mostly positive aspects of the PJM capacity market:

- (i) Participant behavior was evaluated as competitive. Market power mitigation measures were applied when the capacity market seller failed the

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<sup>12</sup> *Id.*

<sup>13</sup> *Id.* at 50.

<sup>14</sup> *Id.* at 71.

<sup>15</sup> *State of the Market Report for PJM (2013)*, Monitoring Analytics LLC (November 14, 2013).

market power test for the auction, the submitted sell offer exceeded the defined offer cap and the submitted sell offer, absent mitigation, would increase the market clearing price. Market power mitigation rules were also applied when the capacity market seller submitted a sell offer for a new resource or uprate that was below the Minimum Offer Price Rule (MOPR) threshold.

- (ii) Market performance was evaluated as competitive. Although structural market power exists in the capacity market, a competitive outcome resulted from application of market power mitigation rules.
- (iii) Market design was evaluated as mixed. The IMM found many positive features to the RPM design but identified two features which threaten competitive outcomes. These features are the 2.5% reduction in demand in the BRA and the definition of DR which permits inferior products to substitute for capacity.
- (iv) The aggregate and local market structures were evaluated to be not competitive due to the failure of LDAs to pass the Three Pivotal Supplier Test (TPST).<sup>16</sup>

The IMM 2013 Report is a rigorous and thorough empirical analysis of all aspects of the PJM capacity market. At the conclusion of that Report, the IMM makes a number of recommendations to PJM which may be discussed and acted upon by PJM through its internal committee structure. The 2013 Report found the most critical elements of the PJM capacity market, specifically participant behavior and market performance, to be competitive. One component, market design, is operating well but modifications are recommended. Market structure, both local and aggregate, were found to be non-competitive. The PA PUC asserts that the PJM capacity market is not a perfect model but is largely performing the function for which it was designed.

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<sup>16</sup> *Id.* at 137. The TPST is an empirical mathematical test employed by economists to measure three factors: market structure, participant behavior and market impact. This test has been modified by the IMM for purposes of evaluating the PJM capacity market.



On balance, the PA PUC submits that the overall performance of RPM over the past seven years is indicative of a centralized capacity market that is functioning as intended but continues to need monitoring and oversight. Currently, PJM and its stakeholders have been addressing a number of issues of concern relating to the capacity market including modifications to how DR is treated as a capacity product, operational constraints on DR, limits on the importation of capacity from adjoining planning authorities, treatment of replacement capacity and other topics.<sup>17</sup> The PA PUC asserts that the PJM committee process provides an avenue for a robust and informed discussion of these critical issues and has been an effective mechanism for examination of the many features of RPM. The PJM committee process is reasonably transparent in allowing monitoring of ongoing developments and the process allows state commissions to monitor ongoing developments.

## **2. Responses to Specific Questions Posed in Topic 1.**

The PA PUC responds to selected questions identified in Topic 1 as follows:

- a. What is the role(s) of centralized capacity markets? Should the centralized capacity markets function as a mandatory market for procuring capacity or a residual market that entities only need to use to meet their resource adequacy obligations that they cannot otherwise meet through self-supply?

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<sup>17</sup> All of these topics are or were recently the subject of discussion at PJM's Capacity Senior Task Force. On November 29, 2013, PJM filed proposed tariff changes to the treatment of DR as a capacity resource at Docket No. ER14-504-000. On the same date, PJM filed its proposal to establish limits on capacity imports at Docket No. ER14-503-000. On December 24, 2013, PJM filed proposed tariff changes that would create additional operational requirements on DR at Docket No. ER14-822-000.

The PA PUC supports the concept of a mandatory market for procuring capacity. Mandatory participation in a capacity market can increase the number of participants, both suppliers and consumers. A mandatory centralized capacity market overseen by a competent planning authority that establishes, through tariff and contractual agreement, a workable economic model for setting capacity price, empirical parameters for participation, meaningful penalties for failure to perform and economic incentives for performance. This model is preferable to a capacity market that is residual in nature designed solely to meet resource obligations that cannot be met by other options such as bilateral contracts and self-supply.<sup>18</sup>

Mandatory participation is more effective at minimizing anti-competitive activity since the entire market is subject to continuous review by the planning authority, individual participants and the market monitor. Instances of improper market activity can be detected more quickly in a forum where all participants (except the improper actors) “play by the rules” and have a vested financial interest in the correct functioning of the market. Under this model, market manipulation and other types of anti-competitive activity can be more readily identified and remedied through investigations, enforcement actions and appropriate fines and penalties.

Power supply reliability requires that mandated levels of generating capacity be procured by load serving entities (LSEs) and that procured capacity be delivered to each LSE. A mandatory capacity market facilitates this process by requiring LSEs to bid for

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<sup>18</sup> Bilateral contracts and self-supply are viable options as long as no out-of-market compensation is received.

capacity that the planning authority has determined is deliverable to the LSE's transmission zone. Under this paradigm, the planning authority, operating pursuant to a centralized market model, can monitor and verify the procurement of needed capacity to the appropriate zones and detect physical or other barriers that impede the delivery of the capacity.

Another benefit of a mandatory centralized capacity market has been the ability of developing technologies to compete on an equal footing with traditional generation. A mandatory centralized capacity market requires that all capacity be procured through a single marketplace. The market sets the rules and parameters for the kinds of capacity product that are best suited to meet the varied demands of the market participants. The transparency and "level playing field" presented by a centralized market has facilitated the introduction, evolution and acceptance of new technologies and market approaches. The best example of this phenomenon has been the rapid growth of DR as an acceptable alternative to more traditional forms of capacity. The market for DR has been so favorable that DR has now evolved from a single product (Limited DR) to other forms such as Extended and Annual DR with each product having its own unique set of characteristics. Energy efficiency has also developed, albeit to a more limited degree, as a capacity product largely made possible by a neutralized capacity market.

On balance the PA PUC contends that a mandatory capacity market in PJM has proven to be more effective at establishing a vibrant capacity market that serves the needs of the region. This has been largely true since establishment of the RPM mechanism in

2006. The PA PUC encourages FERC to continue to promote a regulatory environment that favors mandatory centralized markets.

- b. When procuring a single capacity product, as under current market designs, are there certain fundamental performance standards that capacity resources should be required to meet in the delivery year to ensure resource adequacy? Should any such requirement change depending on the type of resource (traditional generation, new resources vs. existing resources, demand response, energy efficiency, distributed generation, etc.)?

As a state regulator, the PA PUC is not in a position to opine on specific performance standards applicable to individual capacity resources. However, the PA PUC can offer its views on generalized performance issues associated with certain capacity resources in light of the PA PUC's responsibility to ensure reliability and resource adequacy to Pennsylvania ratepayers. In this regard, the PA PUC offers comments on two capacity resources: demand response and capacity imports.

### **Demand Response.**

PJM has experienced tremendous growth in the megawatt quantity of demand resources offered and cleared in BRAs. For example, 12,408 MW of demand resources was offered and cleared in the most recent 2016/2017 BRA.<sup>19</sup> This growth has occurred

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<sup>19</sup> This compares to 14,832 MW in the 2015/2016 BRA; 14, 118 MW in the 2014/2015 BRA; 9,282 MW in the 2013/2014 BRA.

in all three categories of demand resources: Limited DR, Extended Summer DR and Annual DR.<sup>20</sup>

The PA PUC has long been a supporter of demand response initiatives as a key component of the developing centralized capacity market and has recognized demand response as a valuable component of its own energy efficiency and conservation programs. However, the PA PUC is also concerned over the rapid growth of demand resources and the availability of these resources when called upon. As DR becomes a greater component of PJM's capacity portfolio, the PA PUC contends that demand resource providers should be subject to additional requirements that ensure these resources will be available when called upon, can be operationally flexible and can assume a role in the capacity auction that is commensurate with their functional ability to serve PJM's operational needs during the delivery year.

Recently, PJM proposed a number of modifications on how DR will participate as a capacity product in future capacity auctions. On August 2, 2013, PJM proposed tariff revisions that would increase the identification, registration and resource verification requirements currently imposed on DR providers that parallel those requirements imposed on traditional generation resources.<sup>21</sup> These revisions are designed to clarify the information required prior to submission of a demand resource offer into PJM's forward

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<sup>20</sup> Limited Demand Response is defined as a demand resource available for use from June through September and may only be called between 12 p. m. and 8 p. m. EST for at least ten service interruptions a year of no more than six hours duration. Extended Summer Demand Response is defined as a demand resource available May through October between 10 a. m. and 10 p. m. EST for an unlimited number of interruptions of no more than ten hours. Annual demands response is available throughout the year for periods of no more than ten hours

<sup>21</sup> *PJM Interconnection, LLC*, Docket No. ER13-2108-000.

capacity auctions to ensure that the resource will be able to provide the offered demand reduction capability and that the same resource is not offered by more than one Conservation Service Provider.

On November 29, 2013, PJM filed tariff revisions designed to correct prior changes to the RPM that PJM explained inadvertently resulted in increased amounts of lower quality Limited DR and Extended Summer DR being cleared in the BRA. In its filing, PJM expressed concern that increased amounts of Limited and Extended Summer DR product clearing the BRA may lead to inaccurate price signals being sent to existing and potential capacity resources that could precipitate additional retirements of base-load facilities coupled with investor reluctance to develop new generation resources. On December 20, 2013, the PA PUC has filed comments in support of this proposal.

On December 24, 2013, PJM filed proposed tariff revisions designed to add operational flexibility to its utilization of demand resources. PJM proposes to create a new category of demand resource known as Pre-Emergency Load Response designed to more precisely match the demand resource with the needs of the system. Other modifications limit DR response time, reduce minimum event duration, tie offer prices to notification time and improve PJM's measurement and verification procedures.

The PA PUC highlights these filings and supports the proposed revisions to emphasize that additional requirements need to be imposed on demand resources commensurate with the increasing role these products play in the capacity markets. It is not unreasonable to impose on DR providers requirements to ensure the availability of the committed demand resource similar to those imposed on generation resources. As the

DR market matures and the financial opportunities for DR increase, so must the various requirements that apply to demand resources such as registration, identification, notification and response time, source granularity and measurement and verification.

The PA PUC recognizes that each of the foregoing filings will be reviewed by FERC on their individual merits. However, the PA PUC highlights these filings in this proceeding to apprise FERC of the larger role that demand resources play in the PJM capacity market and to recommend that appropriate measures be taken to accommodate these important resources and to maximize their benefit to the PJM capacity market as a whole.

### **Capacity Imports.**

Capacity imports from adjoining regions have been and continue to be an important component of PJM's capacity resource portfolio. Capacity imports are especially critical during emergency conditions. PJM has experienced significant increases in capacity imports over the last few BRAs. For example, 7,482 MW of capacity imports cleared in the 2016/2017 BRA representing an increase of 90% over imports for the 2015/2016 BRA.<sup>22</sup> However, PJM determined that only 4,788 MW of the 7,842 MW offered and cleared held firm transmission service at the time of the BRA.

The BRA process represents capacity commitments three years into the future. Capacity resources offered by external generators may commit to deliver but be physically unable to do so due to lack of firm transmission rights to deliver that capacity

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<sup>22</sup> See PJM, 2016/2017 RPM Base Residual Auction Results.

into PJM. Additionally, the occurrence of emergency conditions within the external region may result in curtailment events being declared by the adjacent planning authority that results in the failure to deliver the external capacity into PJM.

The PA PUC recognizes the importance of external capacity resources to the effective functioning of the capacity market and system reliability. Capacity imports serve an important role in the current market environment where both plant closures in the PJM region and hot weather events have increased. Under current conditions, the PA PUC does not believe that the existing RPM process properly recognizes the increased level of capacity imports and increased the risks of non-delivery.

The current RPM process does not include capacity import limits in its RPM auction process. Further, the current RPM process does not consider the limits on the ability of the transmission system to support firm transmission into the PJM region. Additionally, the current RPM process does not factor into the BRA clearing price the risk that an external resource may be curtailed by the external planning authority. Finally, the current RPM does not distinguish between the various geographic zones where capacity imports may originate.<sup>23</sup> The PA PUC contends that the increased contribution of capacity imports has not yet been properly factored into the RPM auction process.

To remedy these deficiencies, PJM has submitted a proposal to implement capacity import limits into its reliability rules governing its RPM forward capacity

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<sup>23</sup> PJM currently has the ability to import capacity from a number of adjoining regions. However, the vast majority of capacity imports originate from MISO.



market.<sup>24</sup> In its tariff filing, PJM proposes to establish import limits for the next BRA for the 2017/2018 Delivery Year. The key elements of PJM's capacity import proposal are as follows: (i) establish an overall capacity import limit from all external areas; (ii) divide external areas into source zones; and (iii) allocate capacity imports as well as the Capacity Benefit Margin factor across the source zones.<sup>25</sup> Additionally, the PJM proposal creates exceptions for those resources that are physically outside of PJM but are electrically equivalent to resources inside PJM and do not present reliability risks.

The PA PUC filed joint comments in support of this PJM capacity import limit proposal on December 20, 2013. The PA PUC recognizes that this proposal will be examined and judged on its merits by FERC in due course. However, the PA PUC asserts that external capacity imports do present an increased threat to system reliability and urges FERC to consider appropriate limitations on external resources consistent with the concerns raised herein.

**B. Accommodating State Policies and Self-Supply By Load Serving Entities.**

The PA PUC asserts that centralized capacity markets in PJM should accommodate individual state policies and self-supply by LSEs, provided that there is no cost subsidization or mandatory purchasing obligation that adversely affects the viability of wholesale markets. In two recent examples, PJM member states (Maryland and New

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<sup>24</sup> *PJM Interconnection, LLC*, Docket No. ER14-503-000 (November 29, 2013)

<sup>25</sup> The Capacity Benefit Margin is defined under the PJM tariff as external capacity reserved for emergency purposes.

Jersey), acting in response to localized reliability concerns, proposed initiatives to attract new generation facilities.

In the first case, the Maryland Public Service Commission (MDPSC) initiated a proceeding soliciting a Request for Proposals for Generation Capacity Resources under Long Term Contract (Request or RFP) soliciting up to 1800 MW of capacity, energy and ancillary services. In exchange for building and operating the generation resource, the MDPSC offered the potential supplier a long term contract for differences with three Maryland electric utilities which would provide the supplier with a guaranteed revenue stream. The MDPSC would select the bid that produced the lowest cost solution for ratepayers.<sup>26</sup> After an extended comment period on the precise terms of the RFP, the MDPSC finally issued the RFP on December 8, 2011. In the RFP, the MDPSC solicited proposals for a facility with the following characteristics: (i) a new, natural gas-fired generation capacity resource; (ii) physically located inside the southwest MAAC zone serving eastern Maryland; (iii) capable of producing energy and capacity products not to exceed an installed capacity of 1,500 MW; and (iv) for an initial term of up to 20 years.<sup>27</sup> The project ultimately selected by the MDPSC was a gas-fired combustion turbine facility rated at 661 MW.<sup>28</sup>

In the second case, the New Jersey Board of Public Utilities (NJBPU), acting pursuant to a legislative mandate known as the New Jersey Long-Term Capacity

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<sup>26</sup> *In the Matter of Whether New Generating Facilities are Needed to Meet Long-Term Demand for Standard Offer Service*, Case No. 9214 (Order No. 82936 issued September 29, 2009).

<sup>27</sup> *In the Matter of Whether New Generating Facilities are Needed to Meet Long-Term Demand for Standard Offer Service*, Case No. 9214 (Order No. 83555 issued December 8, 2011).

<sup>28</sup> *In the Matter of Whether New Generating Facilities are Needed to Meet Long-Term Demand for Standard Offer Service*, Case No. 9214 (Order No. 84815 issued April 12, 2012).

Pilot Project (LCAPP),<sup>29</sup> initiated a “pilot program” to authorize issuance of “Standard Offer Capacity Agreements” (SOCAs) to selected generators through a competitive solicitation process. This process required winning bidders to enter into a SOCA of up to 15 years with the state’s four electric utilities. Under a contract for differences arrangement, electric utilities were required to pay any difference between the RPM prices and actual development costs with these costs ultimately passed on to ratepayers.<sup>30</sup>

Thereafter, PJM filed a number of revisions to its OATT to implement stakeholder-driven revisions to the MOPR provision of its Tariff reflecting proposed changes to its RPM. Among other changes, PJM addressed the issue of state-subsidized projects by proposing that a resource participating in PJM’s capacity market auction be permitted to qualify for an exemption from the MOPR requirements, as a competitive-entry project, subject to a showing that it satisfied certain criteria.<sup>31</sup>

Under PJM’s proposal, a resource would qualify for the MOPR exemption if it can demonstrate the following:

- (1) No costs are recovered from customers either directly or indirectly through a non-by-passable charge that is linked to the construction or clearing in any RPM auction of the resource;
- (2) No costs of the resource are supported through any contract with at least one year obtained in any state-sponsored or state-mandated procurement processes that are not competitive or non-discriminatory;
- (3) The market seller does not have any arrangement to seek or receive any material payments from any government entity connected with the construction

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<sup>29</sup> P.L. 2001, c. 9, approved Jan. 28, 2011 *codified at* N.J.S.A. §§ 48:3-51.

<sup>30</sup> *In the Matter of the Long Term Capacity Agreement Pilot Program*, Dkt. No. EO-11010026 (Order issued February 11, 2011).

<sup>31</sup> *Letter Filing of PJM, L.L.C.*, Docket No. ER13-535 at 17-24.

or clearing in any RPM auction of the resource or other material support through contracts with a term of at least one year obtained in any state-sponsored procurement processes connected to the construction or clearing of any RPM auction of the resource; and

- (4) The seller submits a sworn, notarized officer certification similar to the certification required for the self-supply exemption.<sup>32</sup>

PJM's proposal regarding the competitive entry exemption was adopted by the FERC in its Final Order.<sup>33</sup> The competitive entry exemption embodied in PJM's MOPR proposal provides a mechanism that properly balances a state's ability to develop its own generation as long as such generation meets the standard of "competitive and non-discriminatory." The FERC Order provides a roadmap for any state that is interested in the capacity procurement process to structure the process in a way that ensures that the operation of MOPR will not adversely affect the RPM wholesale procurement mechanism. The PA PUC supported PJM's MOPR revisions on the basis that state sponsored projects present a fundamental threat to the viability of wholesale markets.

The PA PUC submits that PJM and FERC fairly and correctly addressed the nascent problem of state-subsidized projects developing in capacity-constrained states by providing these states the opportunity to decide what type of generation to procure while insulating the wholesale market from the inappropriate price suppression effects to the wholesale competitive market through institution of the "competitive and non-discriminatory test." As a state strongly committed to the success of wholesale and retail competition, the PA PUC encourages FERC to continue to be mindful of the need to

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<sup>32</sup> *Id.* at 14-15.

<sup>33</sup> *PJM Interconnection L.L.C.*, ER13-535 at 53.

ensure preservation of the competitive environment as it fashions solutions to issues of self-supply especially with regard to state-sponsored generation resources.

### **C. Market Design Elements**

Topic 3 seeks input on the various components of market design such as slope of the demand curve, derivation of resource adequacy requirements, Net Cost of New Entry, length of forward periods and granularity of zones. The PA PUC understands that these complex economic concepts need to be periodically re-examined and modified to reflect market conditions but refrains from making specific recommendations insofar as other market participants will provide valuable input.

However, there is one market design element that the PA PUC contends should be examined – PJM’s current procedures regarding the notice provisions for retirement of coal-fired plants within the PJM region and the consequent economic impacts on local employment and local economies. States are often given inadequate notice of generation retirements and have little or no opportunity to minimize their impacts on local communities.

To illustrate, on July 9, 2013, PJM received notice of deactivation from First Energy (FE) of its planned deactivation of the Hatfield Ferry and Mitchell Generating Stations with a planned effective date of October 9, 2013. Shortly thereafter, the PA PUC became aware of these planned closures by way of a press release.<sup>34</sup> The Hatfield Ferry and Mitchell Generating Stations represented approximately 2,080 MW of

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<sup>34</sup> PJM Press Release dated July 10, 2013.

generation or approximately ten percent of FE's generation capacity. FE alleged that the decision to close these plants was driven by lower demand for power and lower electric prices associated with the economic recession, failure to clear the 2016-2017 BRA, historically low capacity and energy prices and anticipated increased costs of approximately \$270 million associated with environmental compliance.<sup>35</sup>

Under PJM's Open Access Transmission Tariff (OATT), generators are required to provide a 90-day notice of intent to retire a generation facility.<sup>36</sup> Pursuant to the OATT, PJM conducts an initial analysis within 30 days of the closure notice to identify any reliability issues that need to be addressed. A more in-depth analysis is then conducted to verify that reliability will not be compromised by the plant closure. If short-term reliability impacts are identified, PJM can offer the generator a Reliability Must Run contract that allows the facility to continue to operate for a defined period and receive payments reflecting that continued commitment to operate.<sup>37</sup> PJM, in both public statements and testimony before the Pennsylvania Legislature, indicated that all procedures required under the OATT were followed.

The PA PUC was extremely proactive regarding the impacts of these plant closures that resulted in the loss of 380 jobs and adverse impacts on surrounding communities in Southwestern Pennsylvania already hard hit by the economic downturn. These plant closures triggered both legislative hearings on the subject and investigation

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<sup>35</sup> Testimony of James H. Lash, President - FirstEnergy Generation before the PA Senate Consumer Protection and Professional Licensure Committee on September 12, 2013 at 2-3.

<sup>36</sup> *PJM Open Access Transmission Tariff* at § 113.1.

<sup>37</sup> Testimony of Andrew Ott, Executive Vice president for Markets before the Senate Consumer Protection and Professional Licensure Committee on September 13, 2013 at 3-4.

by the PA PUC into the underlying bases for FE’s economic decision to close the Hatfield’s Ferry and Mitchell facilities. PA PUC Chairman Robert F. Powelson and Commissioner Pamela A. Witmer both expressed their frustration and concern over the timing and economic impact of the closures. Chairman Powelson voiced concern over FE’s recent prior statements regarding potential conversion of these facilities to gas-fired generation—a position clearly at odds with the decision to close the facilities.<sup>38</sup> In testimony, Commissioner Witmer voiced concern over the incongruity of closing a plant so soon after its prior owner, Allegheny Energy, invested \$715 million in environmental compliance equipment in 2009.<sup>39</sup> The PA PUC was also concerned that FE had not been as diligent as it might have been in looking at other options such as sale of the plants. Additionally, the PA PUC instituted its own investigation through the IMM to verify that the underlying cost bases for these FE facilities not clearing the BRA in the last few years were valid and supported by the data.

As a deregulated state, the PA PUC does not have jurisdiction to investigate or “second-guess” generator retirement decisions. As a consequence, Pennsylvania and other PJM states are largely powerless in addressing plant closures. The PA PUC believes that FERC should, in the context of examining changes to market design elements that comprise RPM, be cognizant of the underlying consequences of market participant decisions to close generation facilities and, in its future deliberations on the

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<sup>38</sup> Testimony of Chairman Robert F. Powelson before the Senate Consumer Protection and Professional Licensure Committee on September 13, 2013 at 1-3.

<sup>39</sup> Testimony of Commissioner Pamela A. Witmer before the House Consumer Affairs Committee on October 3, 2013 at 3-4.

subject, mandate that PJM and its generation stakeholders implement changes to the RPM that provide the maximum assurance that decisions regarding plant retirements also fully examine alternatives to outright closure especially. More lead time to evaluate reliability and market impacts may allow for more effective generation and transmission solutions to be developed. This is especially true where substantial environmental compliance investment has occurred.

**D. Regulatory Certainty.**

As a state regulatory body, the PA PUC agrees with those participants at the Technical Conference advocating for regulatory certainty in achieving capacity market stability. The PA PUC is responsible for balancing its obligations to Pennsylvania ratepayers of ensuring safe, adequate and reliable service at fair and reasonable rates with the responsibility of promoting a competitive retail electric market environment reflecting its statutory mandate under the Electric Competition Act. Further, the PA PUC has a parallel responsibility to monitor and provide input regarding the operation of the wholesale competitive market by the responsible RTO. Regulatory certainty from the PA PUC perspective should recognize that changes at the wholesale electric market level have real consequences to retail electric markets. From a state regulatory perspective, any changes or modifications to such factors as market design elements or the establishment of “best practices” across multiple RTOs/ISOs must consider the impacts these changes may have on the ability of state regulators in states with retail competition to effectively perform their regulatory functions. Such modifications must allow for a



sufficient transition period to permit the retail markets to fully adjust to the impact of these changes. The PA PUC asserts that FERC should consider the potential impacts on the state regulatory environment from future modifications to the centralized capacity markets within the PJM region.

**E. Next Steps.**

The PA PUC suggests that FERC continue its examination of these complex issues on an open, transparent and incremental basis and in a manner that facilitates the submission of input from all stakeholders, including state regulators, who have a continuing responsibility to their ratepayers to ensure a reliable supply of generation capacity. Procedurally, this may take the form of further technical conferences and opportunities for comment either on a multi-RTO or individual RTO basis as needs dictate. The PA PUC would caution FERC that imposing blanket requirements across all RTOs may not be practical considering the differences that exist between centralized capacity markets in PJM, the ISO-NE and the NY-ISO. FERC should continue to permit these three planning authorities to address future capacity-related issues on an individual RTO basis. At the conclusion of this process, FERC should consider issuance of a policy statement on the more significant issues in this proceeding which could serve as a basis for expressing its future intent while allowing sufficient flexibility for the individual planning authorities to manage centralized capacity market development prospectively.

## V. CONCLUSION

For the foregoing reasons, the PA PUC respectfully requests that FERC consider its Comments in this proceeding.

Respectfully submitted,

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## **CERTIFICATE OF SERVICE**

I hereby certify that the foregoing document has been served in accordance with 18 C.F.R. Sec. 385.2010 upon each person designated on the official service list compiled by the Secretary in this proceeding.

James P. Melia  
James P. Melia

Dated at Harrisburg, PA this 8<sup>th</sup> of January, 2014.