September 17, 2014

Terry Boston
President and CEO
PJM Interconnection, LLC
2750 Monroe Boulevard
Audubon, PA 19403

Dear Terry,

The Public Utilities Commission of Ohio (Ohio Commission) appreciates PJM’s efforts to address resource adequacy and capacity market constructs to maintain reliability through both winter and summer peak operations in its proposed Performance Capacity product (Proposal).¹ As we previously expressed to the Federal Energy Regulatory Commission (FERC), the events of last winter highlight that the current Reliability Pricing Model (RPM) construct fails to provide sufficient incentives and penalties necessary to ensure generation resource performance. Specifically, the following items from the Proposal provide significant improvements to the current RPM capacity construct:

- Addresses the need for a winter and summer peaking product that appropriately values capacity resources that consistently perform during times of system stress.
- Notes the high level of forced outages in January and represents a proactive attempt to provide an appropriate balance of performance incentives and penalties.
- Acknowledges that “Out of Management Control” is not a legitimate or acceptable exemption from performance requirements, consistent with the

¹ The comments reflected in this letter are subject to further refinement and may change as PJM’s Proposal evolves through the Enhanced Liaison Committee. This letter should not be viewed as a comprehensive or final position.

180 East Broad Street
Columbus, Ohio 43215-3793
(614) 466-3016
www.PUCO.ohio.gov
An equal opportunity employer and service provider
previous recommendations of the Ohio Commission and the Independent Market Monitor (IMM).

- Allows generators to determine inputs needed to provide reliable service and allows those generators to include risk, cost, and investment in capacity market offers. This may include, pursuant to the generator’s discretion: firm fuel transportation costs, on-site fuel and storage, and maintenance upgrades.
- Further limits the amount of extended and limited summer demand response products in RPM, consistent with previous comments by the Ohio Commission.

While PJM’s Proposal recognizes that generation performance must improve during harsh weather conditions in order to ensure reliability, the Ohio Commission is concerned that, unless modified, the Proposal will lead to negative, unintended consequences.

Rather than revising requirements for the provisioning of the existing annual capacity product, PJM creates of a new tier of capacity in its Proposal that represents an extensive overhaul of the RPM construct. By rolling out a new capacity tier before the dust has even settled on recent demand response reforms, and before FERC has even seen filings from PJM’s VRR/Triennial Review, PJM casts a cloud of uncertainty over how these related proceedings, taken in a vacuum, will ultimately affect reliability and capacity prices. The Ohio Commission urges PJM to complete a sensitivity analysis, including a reliability and price impact of the Proposal, to determine the cumulative effect on RPM prices.

In addition, the Ohio Commission notes that the Proposal does not include the current capacity “must offer” requirement for the new product. Without such a requirement, PJM should explain how the appropriate quantity of Capacity Performance would be procured by PJM to meet its reliability needs.

Another concern relates to the potential of market power being exercised by suppliers, especially those with large portfolios, by withholding capacity from one class of product to drive prices higher for another product. Accordingly, “coupled offers” between the Capacity Performance and Base Capacity products
should be removed from the Proposal. To meet its reliability requirements, PJM could consider whether it should designate certain current units as Capacity Performance if that unit has already satisfied the performance standards.

The penalties in PJM’s Proposal appear to be less punitive than those found in the New England ISO’s new capacity market revisions. However, the Ohio Commission is concerned that the maximum penalties (2.5 X Annual Capacity Revenue) are significant and may prohibit investment in the Capacity Performance product due to risk exposure. One way to reasonably reduce that impact would be to establish a phase-in period and limited exceptions to incurring penalties when a supplier is unable to meet the performance requirements. We encourage PJM to consider a rebuttable presumption that would allow a generator to prove “force majeure” conditions as a cause for its non-performance. This rebuttable presumption could be reviewed by PJM and the IMM for reasonableness.

As the Ohio Commission has discussed in previous comments to FERC, uneconomic capacity prices do not lead to needed investment in new generation. Therefore, the Ohio Commission requests that PJM consider instituting, in its Proposal, a ceiling price for Base Capacity and a minimum offer price for Capacity Performance. This revision may discourage price takers while mitigating some of the risk and improving incentives and reliability. It may also keep prices in check if the higher priced Capacity Performance is offset by the Base Capacity product price. Further discussion in this area is warranted.

Finally, while the Ohio Commission supports PJM’s efforts to correct these issues in an expeditious manner prior to the next Incremental and Base Residual Auctions, upcoming generation retirements further highlight the importance of having an appropriate transition mechanism to ensure reliability for the winter of 2015/2016. The Ohio Commission implores PJM to gather additional information about generation unit capabilities through a detailed auditing process to identify performance capabilities. Again, PJM should consider phasing in its penalty structure through the transition process to allow generation units the opportunity to make any necessary investments to ensure performance.
The Ohio Commission appreciates the opportunity to comment on the Proposal, and we look forward to our future dialogue.

Sincerely,

[Signature]

Thomas W. Johnson
Chairman
Public Utilities Commission of Ohio