The PJM Industrial Customer Coalition ("PJMICC") appreciates the opportunity to submit these Comments, and trusts that PJM will thoughtfully consider stakeholder input as PJM continues to deliberate whether to move forward with its Capacity Performance ("CP") Proposal and, if so, when and how it will move forward.

PJMICC is comprised of 27 large consumers of electricity, with facilities throughout the PJM footprint. PJMICC members consist of manufacturers across many industry segments, and large institutional consumers such as medical complexes and universities. A few PJMICC members own and operate on-site generation. Many PJMICC members engage in operations that enable customer-initiated interruptions of load.

As a threshold matter, PJMICC has raised on multiple occasions its strong concerns about the poor generator performance that was evident during January 2014. This poor performance caused PJMICC members to incur extraordinary energy and ancillary service costs that were unbudgeted and that had disastrous impacts on PJMICC members' operations. PJMICC requested on March 25, 2014, and in follow-up correspondence, detailed answers and information relative to the events that occurred in January 2014 and in subsequent months. PJMICC also has outstanding requests for additional information relative to generator outages that occurred during September 2013, which caused both severe pricing and reliability impacts on retail customers. The ability of PJMICC, and ostensibly other stakeholders, to meaningfully and fully evaluate the CP Proposal remains hampered by the unavailability of this information.

PJMICC's Comments here are based on the information that is available to PJMICC at this time. In the absence of the requested information, and pending further analysis, PJMICC cannot determine whether the CP Proposal is a proportionate response to the issues that surfaced in September 2013 and January 2014 and to PJM's longer-term reliability concerns. To be clear, PJMICC and its members have fundamental questions whether the PJM Problem Statement on PJM Capacity Performance Definition ("PJM Problem Statement") accurately captures the reliability concerns. Even assuming that it does, however, PJMICC has serious concerns that the CP Proposal is not a proportionate response and, in fact, may not effectively target the gas-electric coordination issues that appear to be the root of the reliability problem. If that is in fact the case, the CP initiative may have devastating impacts on energy-intensive businesses in the PJM footprint. To that end, PJMICC may supplement these Comments, or re-evaluate the positions advocated in these Comments, if and when additional information about the September 2013 and Winter 2014 generator performance issues becomes available.
1. **Strong Market Power Protections Must Be a Key Component of Any CP Proposal.**

As PJM refines its CP Proposal, it is of paramount importance that PJM add more rigorous safeguards against the potential for market power exercise. With the structural concentration of generation ownership and vertical ownership of transmission and generation, strong market power protections are necessary for assuring that RPM produces capacity prices that are just and reasonable.

Market power concerns are inherent in capacity markets, including PJM's Reliability Pricing Model ("RPM"). When PJM filed its initial RPM proposal in 2006, PJM included explicit rules to address the exercise of market power by existing capacity resources that may physically or economically withhold capacity to increase market clearing prices in the RPM auctions. Namely, all existing Generation Capacity Resources have a must-offer requirement into the Base Residual Auction ("BRA") with an annual commitment. Moreover, all existing Generation Capacity Resources that fail the Three Pivotal Supplier ("TPS") test have defined offer caps applied.

The potential for market power exercise remains a real issue under RPM, and the problem may be exacerbated by the CP Proposal. Based on the evaluation of the PJM Independent Market Monitor ("IMM"), the aggregate market structure was found to be not competitive for each and every BRA that has been held since RPM went into effect. Similarly, the local market structure was evaluated and determined not to be competitive. For the various RPM auctions, the IMM found that participant behavior and market performance were consistent with competitive outcomes, but only because of the application of market power mitigation rules.

The same market power rules that were approved for RPM, however, are insufficient if the new CP initiative is implemented. Market power is implicated under the CP initiative when fleet owners with a diversified portfolio may have a range of flexibility in their market participation. By creating two classes of annual capacity products, the potential to exercise market power increases because generation owners, particularly those with portfolio of assets, may withhold CP-eligible resources from bidding in an effort to inflate prices. Moreover, as discussed below, the eligibility criteria for Demand Resources to qualify as CP will be extremely limiting, from a practical and legal perspective. As such, it is not reasonable to expect vibrant supply-demand interaction in the BRAs. Simply put, unless PJM includes strong market power mitigation rules as part of the CP Proposal, it will be difficult for customers to trust, and PJM and the IMM to ensure, that RPM will produce just and reasonable rates.

Similarly, based on discussions at the September 11 CP stakeholder meeting, concern exists that PJM and the Market Monitor may have inadequate tools to assess whether investments undertaken by resources seeking to become eligible as CP resources go beyond levels that could be considered just and reasonable. Marginal resources (i.e., those that are most likely to affect clearing prices) may make investments that are purportedly necessary to become CP-eligible and inflate their offer caps by seeking recovery either through the Avoidable Cost Rate ("ACR") or Avoidable Project Investment Rate ("APIR"). Protections must exist that such investments were, in fact, reasonably made based on decisions consistent with Good Utility Practice.
To that end, PJMICC urges that any CP proposal be enhanced with more robust market power mitigation protections, including, but not limited to:

- At a minimum, all Generation Capacity Resources that could be eligible, based on objective design criteria, to provide the Capacity Performance product must have a Must-Offer Obligation for that product.

- Those Generation Capacity Resources that would only be eligible for CP products with a pre-defined, relatively modest investment, must have a Must-Offer Obligation for that product. Such resources, however, would have the option of also submitting a coupled bid for the Base Capacity product.

- PJM, in consultation with the IMM, must include additional tools to enable PJM, as the independent market administrator, and Monitoring Analytics, as the independent market monitor, to review and approve the legitimacy of any investments that are purportedly undertaken to enable generators to become CP-eligible.

2. **Any Increase in the Net Avoidable Cost Rate-Based Offer Cap Must Reflect Actual Costs, Not an Arbitrary Amount Associated with Undefined Risk Premiums.**

A fundamental question that must be asked in determining whether PJM's proposal would result in "just and reasonable rates" as required by the Federal Power Act is the manner in which Generation Capacity Resources serving as CP may reflect in their offers any additional costs associated with the risk of non-performance. A similar question must be asked for Generation Capacity Resources serving as Base Capacity, but to a lesser degree, given the limited volume associated with Base Capacity under PJM's proposal. Under the existing rules, PJM's rules allow for a 10% adder as a proxy to account for hard-to-quantify costs, but the offer cap itself is a function of a unit's actual costs or a reasonable proxy of actual costs. PJM's CP Proposal includes a formulaic approach to potential increases to the offer cap. The formula is a function of the pool-wide EFORD, average historic number of hours of Hot and Cold Weather Alerts, and the average Real-Time LMP at the specific generation bus during those Hot and Cold Weather Alert hours.

While PJMICC appreciates PJM's efforts to move away from an apparently arbitrary 10% adder, more information is necessary to understand whether PJM's proposed formula approach more accurately captures a generator's reasonably expected actual costs for complying with the additional obligations imposed on CP resources. Questions on the application of the proposed formula remain outstanding, and without more concrete support, PJMICC is not in a position at this point to opine on the reasonableness of PJM's proposal or suggest any alternative. We point to this aspect of PJM's proposal, however, as being one of core fundamental importance to the appropriate pricing of the CP product.
PJMICC is concerned by the lack of information provided on this key point and urges PJM to provide much more detail on this component of CP in the final PJM proposal.

3. **PJMICC Questions Whether Demand Resources ("DR") Can Perform As CP As Currently Proposed.**

PJMICC questions whether industrial customers providing demand response capability can satisfy the onerous eligibility and performance requirements for DR Resources to serve as CP under PJM's draft proposal. By way of background, many industrial customers provide DR on their own basis, not aggregated with other customers. Such industrial customers participate as DR as a way to hedge or partially mitigate their capacity costs; such participation is not undertaken as a profitable venture.

Preliminary indications are that industrial customers cannot realistically commit to perform at the levels that would be required for CP status, with its increased eligibility and flexibility requirements. It must be remembered that such obligations would need to be undertaken three years in advance of a Delivery Year, which is already a challenge for industrial customers with unknown business cycles and given that they do not know their Peak Load Contribution ("PLC") tickets until the prior Delivery Year. The increased eligibility and flexibility requirements for the proposed CP product may be a barrier impossible for an industrial customer to overcome.

Moreover, with the continuing uncertainty surrounding the D.C. Circuit Decision on FERC Order 745 and the likelihood that certain interests will continue advocating for a legal invalidation of all DR participation, industrial customers are unlikely to be willing to assume the performance obligations of a CP resource. Furthermore, if the D.C. Circuit Decision were to be sustained, DR may not be permitted legally to comply with a day-ahead energy market must-offer obligation, even if DR participation as a capacity resource is not addressed or impacted by the D.C. Circuit Decision.

4. **The CP Proposal Will Stifle Existing DR Participation As Well As Future DR Growth.**

Since the beginning of RPM's implementation, PJM has touted the growth of DR as one of the largest accomplishments of RPM. Through the first eight BRAs, DR was responsible for more new capacity than all types of generation resources combined. At present, even with the recent entry of significant new Combined Cycle resources, DR represents about 25% of all incremental Capacity additions since RPM's beginning. Through the eleven BRAs that have been held to date, DR currently is the second largest resource class, trailing only the 40% share provided by Combined-Cycle generation. PJMICC's initial assessment is that DR may be collateral damage in the CP initiative.¹

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¹ As PJM is aware, DR participation has already dropped significantly in the two most recent BRAs (i.e., 45% since the 2015/2016 BRA).
Based on our initial review of PJM's proposal, the CP initiative would have a chilling, if not evaporating, effect on DR participation. Given the onerous eligibility and flexibility requirements (and associated penalties) for DR to serve as CP, few industrial customers will be in a position to make such a commitment to serve as CP. Given that the other DR options will necessarily have reduced revenue expectations, participation in those DR options is likely not economic as a tool to meaningfully hedge capacity costs. Thus, it is not realistic to expect that many industrial customers, who have real and demonstrable costs associated with their curtailments, will be willing to participate as DR in the more limited products. As a consequence, the CP initiative, as it currently is framed, will certainly stall DR growth in PJM, but will also likely result in a serious contraction of DR resources, particularly with respect to industrial customers.

The reliability concerns identified in the PJM Whitepaper are ones that could be addressed by active DR participation in an appropriate capacity mechanism design. DR generally, and industrial customers specifically, have historically delivered to PJM significant benefits in terms of resource adequacy and operational flexibility. When considering the "value proposition" of the CP Proposal and the potential impacts on reliability, PJM should assume that the CP Proposal as currently structured would likely degrade PJM's ability to call upon DR as a reliability and/or operational flexibility tool.

The fact that industrial customers and other customers providing DR may be collateral damage in the CP initiative is troubling when DR has been effective as a tool for PJM to ensure reliability during recent events when the system was stressed by generator, not DR, non-performance. To the extent that the CP initiative is a response to recent events where generators have not performed as expected, as suggested by PJM's Problem Statement and Proposal, PJMICC questions the need to raise the bar for DR participation so high as to effectively preclude participation. PJMICC respectfully requests that any solution prescribed to address generator non-performance be tailored to better reflect and retain the positive performance of DR.

5. **If CP Proposal Moves Forward in Largely the Same Form As When It Was First Released, PJM Should Consider Options for Allowing Customers To Purchase Only the Capacity They Need.**

To the extent that the CP initiative moves forward with the same fundamental structure as when it was first released, PJMICC respectfully requests that PJM consider including an option to allow customers to purchase only the capacity they need, rather than forcing customers into "must buy" capacity-purchasing decisions that are unnecessary for reliability and that are unduly costly for customers. Customers should be permitted to purchase only the capacity they need, by engaging in certain commitments as follows:

- a) A retail customer commits to a Firm Service Level ("FSL") prior to the Delivery Year, and the retail customer's load-serving entity ("LSE") communicates that FSL to PJM (as it now communicates the customer's Capacity Obligation to PJM);
b) The customer operates at or below that FSL during that Delivery Year whenever PJM requires all CP resources to perform during a Max Generation event;

c) PJM provides advance notice of any such event; and,

d) The customer pays penalties for any metered consumption above the FSL during the Max Generation event.

6. **PJMICC Supports Maintaining the Current Cost Allocation Structure.**

PJM's CP proposal offers two different options to allocate the costs associated with the CP initiative to LSEs: (1) extension of the existing method; and (2) winter peak allocation. PJMICC supports extension of the existing method.

As a threshold matter, extension of the existing method will minimize customer confusion and complexity. Moreover, while the CP initiative may incorporate requirements associated with ensuring reliability in the winter period, the summer peak season is still the primary driver associated with establishing PJM's resource adequacy needs.

7. **A More Surgical Transition Plan Should Be Considered.**

PJMICC is a signatory to the *Ex Parte* Letter to the PJM Board with comments specific to the CP Transition Plan. In the interest of efficiency, we will not reiterate those comments here. To supplement the concerns raised in those comments, however, PJMICC seeks to highlight for PJM the inability of industrial customers to adjust their operational strategy to avoid any increase in 2015/2016 capacity costs that may be associated with PJM's contemplated Transition Mechanism.

Industrial customers generally have two options to mitigate RPM capacity costs:

a) Participate as an RPM DR resource; or

b) Manage 5 CP loads, to minimize their capacity obligation.

At time of the BRA, a retail customer evaluates PJM market rules and requirements for each strategy and selects the strategy that will provide the largest cost offset. For the 2015/2016 Delivery Year, this results in many customers undertaking DR participation as the preferred strategy. Any 2015/2016 "transitional" auction for Capacity Performance changes the playing field and might result in a customer re-evaluating DR participation as the preferred means (either because of Capacity Performance eligibility requirements will not allow the DR to achieve maximum capacity market clearing price or because RPM Net Load Costs increase relative to existing, awarded RPM DR commitment clearing price).
So, if the DR strategy is now the inferior strategy with Capacity Performance, a customer might now want to try and manage its 5-CP demand and capacity obligation for the 2015/2016 Delivery-Year. The problem is that the PLC is determined by the 5 CP days that occurred during the 2014 summer, and the 2014 summer is already in the books. Consequently, there is no way a customer can change its strategy for the 2015/2016 Delivery Year. PJM’s proposed Transition Mechanism creates a timing issue for industrial customers trying to manage their capacity costs. PJM is making rule changes for periods when customers do not have an opportunity to adjust operations in time to effectively mitigate 2015/2016 cost increases.

For this reason and the reasons articulated in the above-referenced Ex Parte Letter on the CP Transition Mechanism, to the extent that reliability concerns exist for the 2015/2016 Delivery Year, PJMICC offers that PJM should consider a limited, focused, and interim approach to address any identified reliability concerns for the 2015/2016 Delivery Year. With the start of the 2015 Delivery Year less than a year away and with many industrial customers having already completed their energy budgeting for 2015, fundamental fairness requires that PJM pursue the least invasive approach to address any reliability concerns for the 2015/2016 Delivery Year.

8. **A Transparent Mechanism Should Be Developed To Return Penalties for Non-Performance To Load.**

As we understand PJM’s proposal, penalties for non-performance will be allocated to load. PJMICC supports this aspect of the CP proposal. Under the CP proposal, retail customers are paying Locational Reliability Charges that incorporate the costs associated with the CP eligibility and performance requirements as well as the risks for non-performance. As such, to the extent that penalties accrue for non-performance, it is not only fair but also just and reasonable for those penalties to be credited back to load if load does not receive the benefits for which they are paying.

In order for the actual retail customer to be in a position to receive the economic benefits of these penalties that would be remitted by PJM to LSEs, PJMICC requests that a transparent mechanism be developed to return the economic benefits of the penalties to LSEs. A transparent mechanism could include something as simple as a posting on a conspicuous section of the PJM website showing the details of any credits that are applied to LSEs. Transparent publication of these credits will help ensure that retail customers capture and receive these economic benefits in their retail contracts with LSEs.

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PJMICC appreciates the opportunity to provide input on the draft CP proposal. We look forward to working with PJM, its Members and stakeholders, as well as the opportunity to discuss with the PJM Board during this critical Enhanced Liaison Committee process.