Northern Virginia Electric Cooperative (NOVEC) proposal – CCPPSTF

Preface

We have heard a lot of theories about how the capacity markets work, how companies make bidding decisions, and what factors go into that decision-making. The belief that these are all soundly considered, economically rational decisions with clear go/no-go points ignore realities that we all know and have experienced. There is a momentum behind business decisions that will tend to drive existing facilities forward despite what the theorists tell us. Subsidized resources are not the only resources that are making capacity market offers that reflect something other than their theoretical going forward or avoidable costs. We recognize that subsidized resources doing so means they're not taking on the entire risk of the consequences of that bid, but there are other considerations, and treating those decisions differently in the capacity market will create more problems than it will solve.

The consequence of most of the CCPPSTF proposals is to push capacity market prices up – which may be worthy of consideration if the proposals were grounded by any market fundamentals. Instead, the repricing proposals take one type of resource – state subsidized resources – and assigns them a price based on perfect theoretical economic calculation. All other market participants continue to bid through a combination of economics, game theory and guesswork. Presumably, the behavior that is trying to be corrected in subsidized resources is perfectly acceptable in all other existing resources. And therefore we are going to remove reliance on market fundamentals for one subset of resources and correspondingly accept artificially higher RPM prices as the outcome. And that doesn't make sense.

We are concerned that all of the repricing proposals push toward dichotomous results: the "race to the bottom" – resources ignoring their market fundamentals in order to ensure they clear – and pressure toward clearing at Net CONE * B. At the bottom end, lower clearing prices would result in more resources seeking subsidies to make up their true costs. At the top end, knowing that if sufficient numbers of resources receiving subsidies will push the price up toward Net CONE * B actually provides additional incentive for resources to seek subsidies and non-subsidized resources to potentially bid higher than they might have otherwise, particularly within smaller LDAs.

We believe that it is better to let the market do what the market does best – respond to good information. Let PJM and its market participants assure that the market information to be provided meets the needs of the market to elicit the best market results. Therefore, we propose a solution to the potential issue of subsidized resources that simply requires that the appropriate information about those resources be published along with the planning parameters for each auction, such that other market participants can set their bids in accord with their expectations of the bidding of those resources. The subsidies would then be added to the resources' competitive offers, and the resource stack would clear as usual.

The Proposal

The proposal provides solutions for only three of the design components identified by the CCPPSTF; the rest remain status quo.

Actionable and non-actionable subsidies:

A resource with a subsidy amount greater than 1% of actual or anticipated market revenues would trigger reporting in the planning parameters for each auction and action in the auction clearing. Units subject to the existing MOPR exemption, a subsidy under a Federal program, a subsidy that does not focus on supply side participation, or a subsidy that affects less than 1,000 MW of unforced capacity for each resource class in PJM would not trigger any action.

Competitive Offer Price

Subsidized resources will have their subsidies, as confirmed by PJM and the IMM, added to their competitive offers.

Price Discovery

Status quo PLUS known subsidy information will be published with the planning parameters.

Task Force Questions

How do you define the problem that you are trying to solve with your proposal?

The problem we're trying to solve is the one pre-defined by PJM. To the extent that anyone thinks that subsidized market entry is having a price suppressive effect on the capacity market, we believe that market participants put many factors into consideration in forming their capacity offers, and the behavior of other resources in the auction is a significant factor. However, it is NOT only subsidized resources that are failing to hew to the model of making economically rational offers at precisely their costs – like any auction sellers, resources are setting their offers in order to assure they are given the best chance to clear. Even with relatively low capacity prices in most areas, as capacity has become a bigger part of the overall revenues, just clearing has become more important. So if subsidized resources are able to make offers below their true costs because they are receiving out-of-market revenues, it has to be acknowledged that other resources are likely doing the same and hoping to make that up in the long run.

Does your proposal accommodate resources with state government preferences on a non-discriminatory basis? How?

Yes. This proposal identifies them and provides that information to the market, and adds the subsidy to the resource's offer so it can continue to offer competitively

Will your proposal encourage or frustrate state policy objectives or other subsidies?

Ideally, it should do neither.

What is your definition of an actionable subsidy (you may include specific factors such as MW or economic thresholds, timing of payment, rate and reasons for the subsidy, etc.)?

We would adopt the same language proposed by NRG:

Actionable Subsidies include any payments, concessions, rebates, or incentives other than Market Revenue where Market Revenue is defined as revenue that is received under a tariff administered by PJM or other RTO or ISO and regulated by the Commission. Actionable Subsidies shall not include (i) payments (including payments in lieu of taxes), concessions, rebates, subsidies, or incentives designed to incent, or participation in a program, contract or other arrangement that utilizes criteria designed to incent or promote, general industrial development in an area; (ii) payments, concessions, rebates, subsidies or incentives designed to incent, or participation in a program, contract or other arrangements from a county or other local governmental authority using eligibility or selection criteria designed to incent, siting facilities in that county or locality rather than another county or locality; or (iii) federal government production tax credits, investment tax credits, and similar tax advantages or incentives that are available to generators without regard to the geographic location of the generation. Additionally, Actionable Subsidies shall not include revenue or costs that are supported through any contracts obtained in any state-sponsored or state-mandated procurement processes that are deemed to be Competitive and Non-Discriminatory as described in under the requirements for a procurement process to be deemed "Competitive and Non-Discriminatory" as specified in Attachment DD, Section 5.14 h) (7) ii).)

What impact does your proposal have on energy markets?

This proposal retains the status quo.

Will your proposal result in or mitigate long term price suppression in the capacity market and/or the energy market?

We believe that the proposal will maintain the status quo and, by providing additional market information on the state subsidized resource as part of the annual planning parameter, this proposal will not impact the long term price. The markets will develop in the same manner as today; those units receiving a subsidy can price their respective impacted units in the same manner going forward understanding that the value of the subsidy will be recognized as part of the market solutions. If the bidding behavior of the subsidized unit is cost based, then there should be no difference to the energy market.

How do you think your proposal will impact bidding behavior?

Bidding will continue per the status quo, based on some additional, official information on subsidies. With information on levels of subsidized resources supported in the market, bidders will be able to make the same estimates they've been making about where those resources will bid in order to clear, and will set their expectations accordingly.

Please address the effects of your proposal on potential market manipulation.

Unlike some of the proposals, this offers no new mechanisms for market manipulation.

Please address the potential for "leakage" (the effects of one jurisdiction's actions on other jurisdictions).

We believe that the leakage effects of subsidies are simply absorbed by the market in this proposal.

What is the preferred implementation timing?

Next BRA and associated IAs; no retroactive changes to committed DYs.

For repricing proposals, please explain your treatment for "in between" resources and why you believe it is the right approach ("in between" resources are those that did not clear in one stage of a repricing proposal but offered at a level less than the final clearing price determined in a second stage).

This proposal does not result in in-between resources.

How does your proposal address RGGI, RPS programs, RECs, and ZECs.

To the extent that those programs constitute subsidies as defined above, those subsidies would be reported in the planning parameters. RGGI as currently constituted does not provide revenues to the units it relies upon, so there should be no impact. This proposal envisions that the resource owner has considered their operating parameters for RPS, REC and ZEC programs in today's market as well as the future markets. If the bidding behavior is cost based, then there should be no difference under this proposal.

How does your proposal address DR?

We do not believe there is any impact to unless the DR supplier receives any payments, concessions, rebates, or incentives other than Market Revenue where Market Revenue is defined as revenue that is received under a tariff administered by PJM or other RTO or ISO and regulated by the Commission. The receipt of any such revenues would be considered a subsidy.