**Before**

**The Public Utilities Commission of Ohio**

In the Matter of the Commission’s Review of the )

Participation of The Cleveland Electric Illuminating )

Company, the Ohio Edison Company, and The ) Case No. 12-814-EL-UNC

Toledo Edison Company in the May 2012 )

PJM Reliability Pricing Model Auction. )

**Comments of the Industrial Energy Users-Ohio**

Following a January 26, 2012 announcement by FirstEnergy Corporation that its generation subsidiaries would be retiring some power plants located in northern Ohio, the Public Utilities Commission of Ohio (“Commission”) issued, on February 29, 2012, an Entry in this proceeding. The February 29, 2012 Entry directed The Cleveland Electric Illuminating Company (“CEI”), the Ohio Edison Company (“OE”), and The Toledo Edison Company (“TE” and collectively the “Companies”) to file a report and invited comments from interested parties.[[1]](#footnote-1)

**Background**

In the present context, identifying options to address reliability challenges and mitigate abrupt and excessive increases in wholesale market capacity prices, requires an understanding of, among other things, how PJM Interconnection LLC’s (“PJM”) Reliability Pricing Model (“RPM”) is structured and how the Base Residual Auction (“BRA”) is conducted.

The function of the BRA is to clear sufficient capacity resources (supply and demand-side resources eligible for capacity resource status under PJM’s rules) to reliably meet the expected coincident peak demand within the PJM footprint or region. RPM utilizes a demand curve in establishing auction clearing prices. The general shape of the RPM demand curve used by PJM in the BRA and capacity pricing process is shown in Figure 1 below:

At the real time price (“RTP”) level, PJM establishes a capacity objective from probabilistic studies to identify the quantity of capacity resources necessary to meet a one day in 10 year loss of load equivalent to frame the contingency-considered reliability target. That level of capacity would typically fall slightly to the left of Point B on the demand curve shown in Figure 1. The capacity objective in the BRA is reduced by a 2.5% set-aside to reflect capacity to be obtained in subsequent incremental auctions held after the BRA and closer to the delivery year. Points A, B and C on the demand curve shown in Figure 1 are “administratively derived” from values in PJM’s tariff approved by the Federal Energy Regulatory Commission (“FERC”).

Under RPM rules, the BRA or auction clearing price is established by the intersection of supply and demand offers with the demand curve. The theory behind the downward sloping demand curve used in the auction is that capacity in excess of the reliability-driven capacity target will be cleared in the auction if doing so will lower the total amount of capacity compensation that PJM funds through its capacity pricing conventions and then pays out to providers of accepted capacity resources. Conversely, capacity clearing prices in the BRA process will rise if offered capacity falls below the reliability-driven capacity target. Also, if the offered capacity that clears in the auction falls below the level associated with Point A, prices are administratively set at levels equivalent to 1.5 times the estimated cost of new entry (“CONE”) for a theoretical new combustion turbine generating unit. In the case of American Transmission Systems, Inc. (“ATSI’), this CONE-based price is $537.33 per megawatt-day (“MW-Day”) for the 2015-2016 delivery year.

Although the BRA is conducted as a single auction, prices may separate between Locational Deliverability Areas (“LDA”). This occurs due to transmission constraints, capacity resource limitations or a combination of both. For the upcoming BRA, ATSI will be modeled as a separate delivery zone. PJM made this determination after concluding the capacity emergency transfer objective (“CETO”) was less than 115% of the capacity emergency transfer limit (“CETL”) which is based on a one day in 25 year loss of load equivalent.

In layman’s terms, this means that import capacity into the region is constrained and the in-region resources may not be sufficient to meet the expected peak load. PJM has set the ATSI CETL at 5417.8 MW of unforced capacity (“UCAP”). UCAP reflects the nameplate output of a capacity resource, discounted to reflect historical forced outage rates.

For the upcoming BRA, the preliminary demand curve for the ATSI LDA is shown below in Figure 2.

**$/MW-Day**

**MW UCAP**

There are presently approximately 11,494 MWs of UCAP generating resources in the ATSI zone. In the last BRA, the CETL was in excess of 4,221 MWs and there were approximately 1,385 MW of demand response resources offered into the 2013-2014 Integration Auction (not all demand response offers cleared).

The generation retirements announced by FirstEnergy Solutions (“FES”), **if** approved by PJM, would work to reduce generating capacity in the ATSI zone to approximately 9,954 MW (UCAP).[[2]](#footnote-2) At the current CETL set by PJM of 5417.8 MW, if all of these remaining generation resources cleared in the auction and if external resources equal to the CETL existed, the ATSI zone would still require 85 MW of demand response resources to clear in the upcoming auction just to reach Point A (15,457 MW) on the demand curve. But, FES’s proposed generation plant retirements must be evaluated based on a much bigger picture. For example, GenOn Energy Inc.’s (“GenOn”) recent announcement[[3]](#footnote-3) of plans to retire an additional 1,269 MW of capacity in the zone suggests that the level of demand response resources required to clear in the auction to reach Point A on the demand curve could be as much as 1,354 MW **if** PJM approves the retirement requests.[[4]](#footnote-4) And, on March 8, 2012, FirstEnergy Generation Corp. announced it had filed an application with PJM to conduct a feasibility study to interconnect new combustion turbine peaking units totaling 800 MW at the site of the existing Eastlake Plant in Northern Ohio.[[5]](#footnote-5) **If** these new combustion turbines are bid into the auction (as a “planned resource[[6]](#footnote-6)”) it may reduce, but not eliminate, the need for demand response resources to clear in the auction to hit the reliability target. And, new combustion turbine units in a constrained LDA are required to bid subject to PJM’s minimum offer price rule, which may affect the BRA capacity clearing price as discussed below.

Given the preliminary reliability-related implications of the generating plant closures on the ATSI zone and beyond, it is reasonable to suspect that PJM will order actions such as transmission upgrades and the use of reliability must-run agreements to keep generating units in service such that the probability of the BRA clearing at the maximum price of $537 per MW-Day is reduced. This expectation is supported by PJM's indication that its preliminary deactivation analysis has identified reliability concerns that are expected to be resolved by 2016 and that further refinements to the analysis, required upgrades and generation deactivation schedule continues.

Because PJM is presently treating ATSI as a separate LDA, PJM’s independent market monitor (“IMM”) has determined that the three existing generation owners in the ATSI zone (FES, GenOn and American Municipal Power or “AMP”) are “pivotal suppliers”. Therefore, the sell-offers from their generation resources shall be “mitigated” under PJM’s rules. The offers are mitigated to the owner’s net avoidable cost rate as determined by the IMM. The net avoidable cost rate reflects unavoidable going forward costs offset by net profits from PJM’s energy and ancillary services markets. In recent years, the net avoidable cost rate for coal-fired generating facilities has been close to zero. Presuming generating units within the ATSI zone are mitigated based upon their net avoidable cost rate, the generation resources will be close to zero, making it likely the marginal offer to set the BRA clearing price will be based on an external resource.

There are some exceptions to the net avoidable cost rate that exist for mitigated generation supply offers. First, if a generating unit is subject to a reliability must-run agreement, it is required to bid into the capacity auction as a price taker (offer at a price of zero). The second exception occurs if a significant capital investment is required to keep a capacity resource in service. Under this exception, the IMM may allow the generation resource owner to reflect a significant portion of the capital investment in its offer price. The other exception is for new gas-fired generating capacity located in a constrained LDA which is subject to PJM’s minimum offer price rule. Units subject to the minimum offer price rule are required to bid no less than 90% of net CONE. These later two scenarios seem to be the only ones in which a generation resource internal to the ATSI zone may be likely to set the BRA capacity clearing price.

In summary, PJM is factoring the announced retirements of generating plants into its controlling determinations on the ability of the remaining capacity resources to satisfy the probabilistically-determined reliability target. PJM’s reliability related determinations affect the structure, inputs and outputs of PJM’s wholesale capacity pricing model. As things presently stand, it is reasonable to proactively develop and implement plans that are based on a scenario (among others) that assumes that PJM’s reliability and capacity pricing determinations will significantly elevate wholesale capacity prices in the ATSI zone and elsewhere.

**The February 29, 2012 Entry**

IEU-Ohio commends the Commission for helping to shine some light on the potential future implications of the announced generation plant retirements on reliability and prices. This subject is very complicated and, all too often, poorly appreciated as a critically important subject. Under PJM’s system, owners of generation resources obtain higher capacity prices when PJM finds resource scarcity. Thus, owners of generation resources have very weak incentives “to do the right thing” and strong incentives to let scarcity happen. While the Commission’s Entry importantly shines useful light on this important subject and suggests the Commission is prepared to do more, there is little time left before the BRA in which to affect the outcome of the BRA in a way that meets the reliability objective and produces reasonable wholesale capacity prices.

The February 29, 2012 Entry suggests, implicitly and incorrectly, that the reliability implications of the announced plant closings can somehow be remedied by the Companies obsessive obedience to Ohio’s portfolio mandates in Section 4928.66, Revised Code. At page 2 of the Entry, the Commission states:

*By definition cost-effective energy efficiency and peak demand reduction programs will reduce total costs to consumers.*

At page 3 of the Entry, the Commission states:

*…the Commission is initiating this review to ensure that the EDUs inputs to and participation in the May 2012 RPM auction for 2015/2016 PJM capacity requirements are reasonable and to the extent practicable mitigate potential increases in RPM prices.*

The tone and content of the Commission’s Entry suggests that it has assumed that the Commission can somehow pull ***purposeful*** reliability improvement and capacity price mitigation strategies through the Companies (the “middleman”). By appearing to focus on the role of the regulator as it relates to the Companies, the Commission may ignore the more obvious and more effective problem-solving approaches which engage consumers directly and require proactive coordination with PJM.

As the Commission knows, customer-sited capabilities can qualify as “capacity resource” in the RPM process and aggregation can function to harvest reliability and price mitigation benefits from PJM’s market-based approach to improve reliability and mitigate “market power” as well as escalations in capacity prices. And, with a PJM BRA quickly approaching in May 2012, a Commission announcement that it expects the Companies to “do the right thing” is, realistically speaking, unlikely to produce meaningful or timely results.

More pointedly, feverish and excessive adherence to Ohio’s portfolio requirements[[7]](#footnote-7) will drive up electric bills and only coincidently do something useful to address the potential reliability and capacity price implications of closing power plants in northeast Ohio. The middleman orientation and the lack of alignment and coordination between the Ohio portfolio requirements, the Commission’s rules related to such portfolio requirements and PJM’s reliability-related measurement practices and protocols as well as the RPM capacity pricing process stand in the way of thoughtful and cost-effective solutions to reliability challenges and “just and reasonable” wholesale capacity prices.

**Conclusion**

 For the reasons briefly expressed above, IEU-Ohio urges the Commission to continue to shine light on this important subject and not assume that tossing more consumers’ money at the Companies’ energy efficiency and peak demand response activities will necessarily do anything to address reliability challenges or mitigate increases in capacity prices. The final reliability challenges, if any, must be identified and addressed through solutions that are recognized by PJM as solutions.

IEU-Ohio also urges the Commission to proactively work with PJM to identify options that will avoid the need to treat the ATSI zone as a “breakout” LDA. Given the nearness of the next BRA, IEU-Ohio believes that the Commission can and should make a direct and strong appeal to all consumers with a customer-sited capability that may qualify as a capacity resource in the BRA process, as well as Curtailment Service Providers presently registered with PJM, to help address potential reliability problems and mitigate the potential of an abrupt and excessive increase in wholesale capacity prices. Such an appeal will only be successful if accompanied by a significant educational effort undertaken jointly by the Commission and PJM. Lastly, IEU-Ohio urges the Commission to send a clear message that it encourages and is prepared to facilitate (through rider exemptions, accelerated approvals of mercantile-customer “reasonable arrangements” and otherwise) direct customer engagement in the PJM upcoming BRA to address reliability-related challenges and produce “just and reasonable” wholesale capacity prices through the BRA process.

Respectfully submitted,

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**Certificate of Service**

I hereby certify that a copy of the foregoing *Comments of the Industrial Energy Users-Ohio* was served upon the following parties of record this 10th day of April 2012, *via* hand-delivery, electronic transmission, or first class mail, U.S. postage prepaid.

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1. The Commission’s request for comments in this proceeding comes at a time when the Industrial Energy Users-Ohio (“IEU-Ohio”) and other consumer representatives are besieged by unreasonable and unlawful proposals of Ohio Power Company (“OP”). OP’s proposals are currently swirling around in multiple Commission cases as though the Commission is obligated to indulge this utility’s effort to apply the throw-hope-it-sticks method of searching for ways to raise rates and block shopping and otherwise violate Ohio’s law and policy. The resource burn caused by OP’s persistent disregard for the public interest and the multiple venues in which the Commission is allowing OP to prosecute OP’s unconscionable claims leave little time or resources to devote to the important subject identified in the Commission’s February 29, 2012 Entry. [↑](#footnote-ref-1)
2. PJM’s March 13, 2012 Retirement Study Update, Analysis of January 2012 FirstEnergy Deactivation Notifications, is attached as Appendix A. As indicated herein, the reliability implications of the announced deactivations extend beyond the ATSI zone. [↑](#footnote-ref-2)
3. GenOn’s announcement is available via the Internet at http://www.genon.com/news.aspx (last checked April 9, 2012). [↑](#footnote-ref-3)
4. PJM is in the process of evaluating the GenOn deactivation requests to determine reliability impacts. [↑](#footnote-ref-4)
5. A copy of FirstEnergy Generation Corp.’s news release regarding the interconnection request is posted at https://www.firstenergycorp.com/newsroom/news\_releases/firstenergy\_generationcorpfilesinterconnectionstudyrequestwithpj.html (last checked April 10, 2012). [↑](#footnote-ref-5)
6. BRA participation by “planned resources” is described by PJM at http://www.pjm.com/markets-and-operations/rpm/~/media/markets-ops/rpm/rpm-auction-info/communication-regarding-2015-2016-bra-deadlines-for-planned-resources.ashx (last checked April 10, 2012). Demand response can qualify as a “planned resource”. Planned resources may be subject to credit and collateral requirements. [↑](#footnote-ref-6)
7. Despite the clear language in Sections 4928.64 and 4928.66, Revised Code, that requires the Commission to encourage mercantile customers to commit their customer-sited capabilities to serve the public interest in reliability and reasonable prices, the Commission’s behavior since 2008 has displayed a strong bias in favor of wind and solar projects that do nothing or little to boost capacity or reliability. And despite repeated reports to the Commission by consumers and Curtailment Service Providers about the efforts of utilities like American Electric Power to block end-use customer participation in the BRA process, the Commission has stood by passively or said that it would consider the subject in the future. [↑](#footnote-ref-7)