**BEFORE**
**THE PUBLIC UTILITIES COMMISSION OF OHIO**

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| In the Matter of the Procurement of Standard Service Offer Generation for Customers of Ohio Power Company | ) ) ) ) | Case No. 17-2391-EL-UNC |
| In the Matter of the Procurement of Standard Service Offer Generation for Customers of the Dayton Power and Light Company | ) ) ) ) ) | Case No. 17-0957-EL-UNC |
| In the Matter of the Procurement of Standard Service Offer Generation for Customers of Duke Energy Ohio, Inc. | ) ) ) ) | Case No. 18-6000-EL-UNC |
| In the Matter of the Procurement of Standard Service Offer Generation as Part of the Fourth Electric Security Plan for Customers of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company | ) ) ) ) ) ) ) | Case No. 16-0776-EL-UNC |

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# STAFF PROPOSAL AND RECOMMENDATION

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By entry dated February 13, 2020, the Public Utilities Commission of Ohio ("Commission" or "PUCO") directed Staff to file a proposal for a modified product which contains capacity flow-through provisions for electric utility default service auctions. This was in response to continued delays and uncertainty regarding PJM Interconnection's ("PJM") capacity construct, known as the Reliability Pricing Model ("RPM"). Staff submits the following proposal for the Commission's consideration.

## BACKGROUND

In June 2018, the Federal Energy Regulatory Commission ("FERC") issued an order in Dockets Nos. EL16-49-000 and EL18-178-000 finding that PJM's capacity market design was unjust, unreasonable and unduly discriminatory due to the purported price suppressive effects of out-of-market payments received by certain generators. Due to this finding, PJM was unable to run its capacity auction for the 2022/2023 delivery year as normally scheduled in May 2019. In December of 2019, FERC issued an order directing PJM to modify the existing capacity construct by instituting an expanded Minimum Offer Price Rule ("MOPR").

PJM's compliance filing implementing these changes is due to be filed by March 18th of this year. However, in advance of the compliance filing, PJM has already filed with FERC a request for rehearing and clarification, as have the PUCO and many other intervening parties, so the timing of future capacity auctions is still very much in doubt. PJM has indicated to interested stakeholders through its Markets Implementation Committee that it will need a minimum of six months after FERC approves the compliance filing to hold an auction, which means the earliest an auction could take place for the 2022/2023 delivery year is December 2020. A date for the 2023/2024 capacity auction, which certainly will not take place in May 2020 as it would have been normally scheduled, is also unknown at this time.

## EFFECT OF DELAY ON PROCUREMENTS FOR DEFAULT SERVICE

Ohio's regulated electric utilities all administer a competitive bid auction process to establish Standard Service Offer ("SSO") rates, a process that has proven to be an efficient mechanism to allow competitive forces and wholesale market conditions to set default retail generation rates. However, in the absence of a FERC approved wholesale rate for capacity, it is nearly impossible for bidders to offer a full requirements product into such auctions without absorbing an unacceptable amount of risk.  In response, the Commission has already modified the SSO auction schedules for both Duke Energy Ohio and Dayton Power & Light to delay the procurement of generation service for delivery years in which the capacity price is not yet known.  AEP Ohio and the FirstEnergy Companies both also have auctions scheduled in fall 2020 that include delivery years for which wholesale capacity rates have not yet been established.

Many retail jurisdictions in PJM have similar processes in place where competitive procurements establish default service rates for non-shopping customers.  PUCO Staff is an active member of the Organization of PJM States, Inc. ("OPSI") and has had a number of discussions with our colleagues in other states, as well as with the independent auction administrators and with the Commission's consultant, Bates White, on how best to proceed.

After FERC ordered PJM to delay the 2022/2023 capacity auction, the Public Service Commission of the District of Columbia ("D.C. Commission") convened a Standard Offer Service ("SOS") working group to discuss changes to their auction process.  The following options were considered.

(1) Option 1: Maintain the status quo.

(2) Option 2: Change the residential and small commercial three (3)-year term to a two (2)-year term.  Hold an auction for the remaining year in the 2019-2020 procurement cycle contingency tranche or at another, later time during the current procurement cycle.

(3) Option 3: Change the residential and small commercial three (3)-year term to a two (2)-year term. Hold an auction for the remaining year during the 2020-2021 procurement cycle or subsequent cycle; or

(4) Option 4: Suppliers incorporate a capacity price of $0/MW-day into their bids for the delivery year, June 1, 2022, through May 31, 2023. The utility will reimburse SOS suppliers for the final zonal capacity price for that delivery year times the daily unforced capacity ("UCAP") obligation.

Although the SOS working group did not come to a consensus on a preferred option, Option 4 was preferred by 4 of the 8 suppliers responding to a poll, while Option 3 was preferred by 3 suppliers and Option 1 was preferred by 1 supplier. The D.C. Commission ultimately adopted Option 4.[1]

Our colleagues at the New Jersey Board of Public Utilities ("NJBPU") also have adopted an approach that merits consideration. New Jersey's Base Generation Service ("BGS") auctions were modified such that the supplier's bid for the three-year Residential and Small Commercial product includes capacity priced at a "proxy rate" for the June 2022 to May 2023 time period that is based on the average of previous delivery years' capacity prices and is trued up once the actual rate is established.[2] In this case, the true up may be either a debit or a credit to the supplier, based on whether the actual capacity rate ends up being higher or lower than the predetermined proxy rate.

[1] Public Service Commission of the District of Columbia, Formal Case No. 1017, In the Matter of the Development and Designation of Standard Offer Service in the District of Columbia, Order No. 20227

[2] New Jersey Board of Public Utilities, Docket No. ER19040428

Bates White, who serves as the Commission's consultant for competitive procurements in the District of Columbia and New Jersey, as well as Ohio, has informed Staff that both the D.C. and New Jersey auctions were successful in attracting competitive offers.

## STAFF RECOMMENDATION

PUCO Staff recommends that the Commission direct the utilities and their auction administrators, in consultation with the Commission's consultant, to modify the SSO auction products such that the capacity obligation is priced at $0/MW-day and suppliers are made whole for all RPM capacity costs incurred through a "pass-through" charge. This charge shall be recovered within each utility's existing auction cost recovery mechanism, for delivery year 2022/2023 through the end of each utility's current electric security plan ("ESP"). All Ohio utilities' ESPs are set to expire by the end of the 2023/2024 delivery year, at which time we are cautiously optimistic a FERC approved capacity construct will be in effect.

Staff recommends that each utility be required to submit a modified auction timeline that clearly identifies which products include capacity as a "pass-through" and catches up on tranches not procured in previous auctions that had been modified by the Commission to exclude the 2022/2023 delivery year. Revised Master Supply Agreements and associated documents should also be submitted that reflect the modified auction product. To be clear, suppliers would still be responsible for supplying capacity as part of their provision of full requirements service. Sufficient time must be given to auction administrators to implement the pass-through clause and to allow suppliers to understand and gain comfort with their rights and obligations under this proposal.

Given that allowing a true up for the capacity portion of the product will result in an artificially lower auction price in years where capacity is not known, Staff recommends that procurements going forward separate products where the capacity price is known from products where the capacity cost will be trued up. This recommendation is necessary to avoid unnecessary confusion although it will admittedly, at least temporarily, eliminate the rate certainty benefits associated with blending procurements of multiple durations.

The pass-through option appears to Staff to be the simplest and lowest risk option available to address the continued delays and uncertainty surrounding PJM's capacity construct. While it certainly is an option to wait for the issues surrounding PJM's capacity market to resolve at the federal and regional level, this approach would unduly deprive Ohio ratepayers the opportunity to lock in the historically low electricity prices that are currently available in the marketplace. The "proxy rate" concept espoused by NJBPU makes sense as a mechanism to preserve three-year solicitations in the absence of a FERC-approved capacity price for year three. However, since all the Ohio utilities are nearing the end of their ESPs, this concern is of less relevance here. Using a proxy rate other than zero adds administrative complexity that may outweigh its incremental value. Estimating the appropriate proxy rate is also inherently difficult due to the high levels of volatility in annual capacity prices.

Staff is confident that the independent auction administrators, Charles River Associates ("CRA") and National Economic Research Associates ("NERA") possess the requisite skills to implement the recommended auction structure without undue harm on bidder interest or participation. As one may recall, NERA conducted a series of energy-only auctions on behalf of AEP Ohio in 2014 when AEP was still providing capacity on behalf of all wires-connected customers.[3] These auctions successfully attracted bidder interest and produced prices that were consistent with then-prevailing market conditions.

One concern that Staff must bring to the Commission's attention is the effect that this proposal may have on the Percentage of Income Payment Plan ("PIPP") procurement process. Today, the PIPP benchmark price is calculated as a tranche-weighted average price for all procurements for a given delivery year. This sets the "price to beat" for potential PIPP suppliers. If the price to beat does not include capacity, it may be the case that the PIPP product may also need to be modified to include a capacity pass-through clause, so it can be compared on an apples-to-apples basis with the benchmark price.

## CONCLUSION

Staff proposes that all procurements for the 2022/2023 delivery year and beyond, for the duration of each utility's ESP, be modified to include a pass-through clause for RPM capacity costs incurred by winning suppliers. The Commission should direct the utilities to take all actions necessary to implement this change as soon as is practicable so Ohio utility ratepayers can enjoy the benefits of historically low electricity prices currently available in the wholesale market.

[3] See 14-0300-EL-UNC