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STATE OF MARYLAND
PUBLIC SERVICE COMMISSION

In the Matter of Whether New Generating Facilities Are Needed to Meet Long-Term Demand for Standard Offer Service	)	Case No. 9214

COMMENTS OF THE INDEPENDENT MARKET MONITOR FOR PJM

Pursuant to the Notice of Approval of Request for Proposals for New Generation to Be Issued by Maryland Electric Distribution Companies issued by the Commission in the above referenced case on September 29, 2011, Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor for PJM[1] ("Market Monitor"), submits these comments on the Commission's proposal to conduct an RFP to select resources to supply capacity in the PJM capacity market, the Reliability Pricing Model ("RPM"), and to require electric distribution companies to enter into long term contracts for differences with selected resources.

The Market Monitor has reviewed the Request for Proposals for Generation Capacity Resources Under Long-Term Contract ("RFP"). With a few significant changes, we believe that the RFP could be modified in a manner consistent with the PJM Minimum Offer Price Rule ("MOPR"). The principal feature of the RFP that is incompatible with

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1 PJM Interconnection, L.L.C., which operates the bulk power grid and administers the organized wholesale electric markets in Maryland, and all or part of 12 other states and the District of Columbia. Capitalized terms used herein and not otherwise defined have the meaning specified in the PJM Open Access Transmission Tariff ("OATT").

competitive procurement is the requirement that "Generation Capacity Resources must be new, natural gas-fired units."[2]

It is the Market Monitor's view that any RFP should not discriminate among potential suppliers based on whether the unit is new or existing, or the fuel type of the unit. The proposed RFP approach is not consistent with the operation of a competitive capacity market. The proposed RFP approach would have the following undesirable results: the procurement of capacity that is not needed for reliability; the procurement of capacity through a process that is discriminatory because it excludes existing generation and non-gas fired units; and the requirement to offer the procured capacity so that it clears in the PJM capacity auctions. Offering capacity purchased through this RFP process into the PJM capacity market at prices less than cost would artificially depress prices in the PJM capacity market. This would negatively affect the incentives to build new generation and would likely result in a situation where only subsidized units would ever be built. The IMM report, previously submitted to the Maryland Public Service Commission, shows the detailed results that support the conclusion that such offers would depress capacity market prices below competitive levels.[3]

This does not mean that a modified RFP could not enhance resource adequacy objective in the affected zones. Some parties have complained to the FERC about the ability of Load Serving Entities to obtain capacity under long-term contracts from existing suppliers at reasonable terms. The Market Monitor believes that the RFP, modified to

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2 RFP § 2.1.

3 *See "Impact of Maryland PSC's Proposed RFP on the PJM Capacity Market,"* attached to Comments of the Independent Market Monitor for PJM, Case No. 9214 (January 28, 2011).

included participation by existing suppliers and any fuel type, would encourage the owners of existing supply to provide competitive offers for long term supply. The exclusion of existing supply is not necessary to achieve the legitimate and appropriate objectives of the RFP.

If Maryland wants to test the market for long term contracts, such contracts should be acquired through non-discriminatory, competitive auctions. The IMM has proposed that this alternative be included in a final MOPR rule.[4] This proposal has not yet been addressed by the FERC. However, this approach would meet the legitimate concerns raised by LSEs, by public power entities and by Maryland, and the Market Monitor continues to support developing such a rule. This approach offers a simple, clear, workable and consistent solution, that is also consistent with the MOPR's core standard that offers reflect "the competitive, cost-based, fixed, net cost of new entry were the resource to rely solely on revenues from PJM-administered markets."[5] It is essential that any approach to the PJM markets and the PJM capacity market incorporate a consistent view of how the preferred market design is expected to work to provide competitive results in a sustainable market design over the long run. A sustainable market design means a market design that results in appropriate incentives to retire units and to invest in new units over time such that reliability is ensured as a result of the functioning of the market. There are at least two broad paradigms that could result in such an outcome. The market paradigm includes a full

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4 *See* Motion for Leave to Answer and Answer of the Independent Market Monitor for PJM in Docket No. EL11-20 at 4–5 (March 21, 2011); *see also* Protest of the Independent Market Monitor for PJM in Docket No. EL11-20 (June 2, 2011).

5 OATT Attachment DD § 5.14(h)(5), revised as proposed by PJM in its compliance filing in Docket No. ER11-2875-003 (December 19, 2011).

set of markets, most importantly the energy market and capacity market, which together ensure that there are adequate revenues to incent new generation when it is needed and to incent retirement of units when appropriate. This approach will result in long term reliability at the lowest possible cost. The market paradigm also fits well with Maryland's competitive approach to the provision of retail service. The quasi-market paradigm includes an energy market based on LMP but addresses the need for investment incentives via the long-term contract model or the rate base/rate of return model. In the quasi-market paradigm, competition to build capacity is limited and does not include the entire PJM footprint. In the quasi-market paradigm, customers absorb the risks associated with new investment through guaranteed payments under either guaranteed long term contracts or the rate base/rate of return approach. In the quasi-market paradigm there is no market clearing pricing to incent investment in existing units.

Although the Market Monitor believes that the market paradigm is the preferred alternative, it is essential at a minimum that the current choices about incentives and regulatory approaches be made with an explicit understanding of the short run and long run implications of these choices for the design of wholesale power markets and the interaction between wholesale power markets and retail markets.

Although the modifications proposed by the Market Monitor are significant, they could be implemented with relatively modest revisions. The result would be a process that could achieve the Commission's objective consistent with the competitive wholesale market design. This approach could substantially strengthen PJM capacity markets in the affected zones rather than undermine them.

The Market Monitor respectfully requests that the Commission afford due consideration to these comments as the Commission resolves the issues raised in this proceeding.

Respectfully submitted,

Jeffrey W. Mayes

General Counsel
Monitoring Analytics, LLC
2621 Van Buren Avenue, Suite 160
Valley Forge Corporate Center
Eagleville, Pennsylvania 19403
(610) 271-8053
jeffrey.mayes@monitoringanalytics.com

Joseph E. Bowring
Independent Market Monitor for PJM
President
Monitoring Analytics, LLC
2621 Van Buren Avenue, Suite 160
Valley Forge Corporate Center
Eagleville, Pennsylvania 19403
(610) 271-8051
joseph.bowring@monitoringanalytics.com

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