

Black Start Issues: Revised

Operating Committee
September 3, 2020
Revised 09.09.20

IMM



Monitoring Analytics

Revisions to Black Start Presentation

- **IMM proposed CRF rates include an interest rate of 7.0 percent.**
- **Presentation of 09.03.2020 included CRF rates including a current market interest rate of 3.5 percent.**
- **Rates and excess recovery totals recalculated.**
- **Descriptions clarified.**
- **IMM proposed CRF rates for future RFPs include a current market interest rate.**

Black Start Issues

- **CRF: capital recovery factor**
 - **A rate, multiplied by the investment, which provides for a return on and of capital over a defined time period**
 - **CRFs are calculated using a standard financial model that accounts for the weighted average cost of capital and its components, including depreciation and taxes.**
 - **For example, a five year CRF will allow the recovery of 100 percent of the investment plus a return over five years.**

CRF History

- **The CRF table was created in 2007 as part of the new RPM capacity market design**
 - **The CRF table provided for the accelerated return of incremental investment in capacity resources based on concerns about the fact that some old units would be making substantial investments related to pollution control.**
 - **The same CRF table was used in the black start rules.**

CRF Issues

- **The CRF table includes assumptions that are no longer correct. The CRF values are significantly too high.**
 - **Tax depreciation rules reduce taxes**
 - **Corporate tax rate lower**
- **Need two CRF tables:**
 - **CRF for full application of 2017 tax law including changes in depreciation and corporate tax rate for units going into service after 2017**
 - **CRF for application of corporate tax rate under 2017 tax law for units in service prior to new tax law**

Original CRF Table

Original CRF table created in 2007

Age of Black Start Unit	Term of Black Start Commitment	Levelized CRF
1 to 5	20	0.125
6 to 10	15	0.146
11 to 15	10	0.198
16+	5	0.363

Revised CRF Table 1

Original CRF table with CRF values based on 2017 tax code including depreciation and tax rate changes: post 2017 units.

Age of Black Start Unit	Term of Black Start Unit Commitment	Levelized CRF
1 to 5	20	0.096
6 to 10	15	0.111
11 to 15	10	0.144
16+	5	0.246

Revised CRF Table 2

Original CRF table with CRF values based on 2017 tax code including tax rate change: pre 2017 units.

Age of Black Start Unit	Term of Black Start Unit Commitment	Levelized CRF
1 to 5	20	0.119
6 to 10	15	0.136
11 to 15	10	0.179
16+	5	0.313

CRF Issues

- **CRF table column header: “Term of black start commitment”**
 - **This is misleading and incorrect**
 - **The column is simply the cost recovery period**

Term of Black Start Commitment

- **No need for current short recovery periods for black start investments. Based on RPM.**
- **Accelerated recovery reduces risk to black start units and should not be the basis for a shorter commitment.**
- **Two periods, based on unit age, are more than adequate. The two periods still reflect accelerated recovery.**
- **Full payment of all costs of black start investment should require commitment for life of unit.**
- **Without such commitment, customers pay full price multiple times for the same service.**

IMM Proposed CRF Table 1

**CRF values based on 2017 tax code including depreciation and tax rate changes: post 2017 units.
Two age categories rather than four.**

Age of Black Start Unit	Black Start Cost Recovery Period	Levelized CRF
1 to 10	20	0.096
11 Plus	10	0.144

IMM Proposed CRF Table 2

Original CRF table with CRF values based on 2017 tax code including tax rate change: pre 2017 units.

Age of Black Start Unit	Term of Black Start Unit Commitment	Levelized CRF
1 to 5	20	0.119
6 to 10	15	0.136
11 to 15	10	0.179
16+	5	0.313

IMM Proposed CRF Table 3

CRF values based on 2017 tax code including depreciation and tax rate changes, and current interest rate (3.5 percent): new RFP units.

Age of Black Start Unit	Black Start Cost Recovery Period	Levelized CRF
1 to 10	20	0.085
11 Plus	10	0.134

Note: Actual interest rate may change based on market conditions.

CRF Implementation Issues

- **CRF values have overcompensated all black start units following changes to the tax code in 2017.**
 - **Depreciation rules allow more accelerated depreciation.**
 - **Reduced corporate tax rate to 21 percent.**
- **Black start units going into service currently are being overcompensated**
 - **The new CRF rates should apply to all units going into service following the changes in tax law in December 2017 and to which the changes apply.**
 - **There are eight plants with 20 black start units.**

CRF Implementation Issues

- **Black start units in service prior to the tax law changes are also being overcompensated**
 - **The new CRF rates that include the change in the corporate tax rate should apply to all units with a CRF.**
 - **Units did not invest with the expectation of this windfall.**
 - **There are 21 plants with 29 black start units.**

CRF Implementation Issues

- **Overcompensation amounts vary with the project investment and the CRF recovery period.**
- **For a post 2017 black start unit with an investment of \$21M to which the full tax law applied, the overcompensation for a 20 year recovery period is:**
 - **\$609,000 per year**
 - **\$12,180,000 over the recovery period**
- **For a post 2017 black start unit with an investment of \$21M to which the lower tax rate applies, the overcompensation for a 5 year recovery period is:**
 - **\$2,457,000 per year**
 - **\$12,285,000 over the recovery period**

Annual Difference: Full Tax Law

Example	Old CRF Rate	New CRF Rate	Project Investment	Old Annual Revenue Requirement	New Annual Revenue Requirement	Annual Difference
1	0.125	0.096	\$9,000,000	\$1,125,000	\$864,000	\$261,000
2	0.125	0.096	\$15,000,000	\$1,875,000	\$1,440,000	\$435,000
3	0.125	0.096	\$21,000,000	\$2,625,000	\$2,016,000	\$609,000
1	0.146	0.111	\$9,000,000	\$1,314,000	\$999,000	\$315,000
2	0.146	0.111	\$15,000,000	\$2,190,000	\$1,665,000	\$525,000
3	0.146	0.111	\$21,000,000	\$3,066,000	\$2,331,000	\$735,000
1	0.198	0.144	\$9,000,000	\$1,782,000	\$1,296,000	\$486,000
2	0.198	0.144	\$15,000,000	\$2,970,000	\$2,160,000	\$810,000
3	0.198	0.144	\$21,000,000	\$4,158,000	\$3,024,000	\$1,134,000
1	0.363	0.246	\$9,000,000	\$3,267,000	\$2,214,000	\$1,053,000
2	0.363	0.246	\$15,000,000	\$5,445,000	\$3,690,000	\$1,755,000
3	0.363	0.246	\$21,000,000	\$7,623,000	\$5,166,000	\$2,457,000

Lifetime Difference: Full Tax Law

Example	Old CRF Rate	New CRF Rate	Project Investment	Old CRF Lifetime Recovery	New CRF Lifetime Recovery	Lifetime Difference
1	0.125	0.096	\$9,000,000	\$22,500,000	\$17,280,000	\$5,220,000
2	0.125	0.096	\$15,000,000	\$37,500,000	\$28,800,000	\$8,700,000
3	0.125	0.096	\$21,000,000	\$52,500,000	\$40,320,000	\$12,180,000
1	0.146	0.111	\$9,000,000	\$19,710,000	\$14,985,000	\$4,725,000
2	0.146	0.111	\$15,000,000	\$32,850,000	\$24,975,000	\$7,875,000
3	0.146	0.111	\$21,000,000	\$45,990,000	\$34,965,000	\$11,025,000
1	0.198	0.144	\$9,000,000	\$17,820,000	\$12,960,000	\$4,860,000
2	0.198	0.144	\$15,000,000	\$29,700,000	\$21,600,000	\$8,100,000
3	0.198	0.144	\$21,000,000	\$41,580,000	\$30,240,000	\$11,340,000
1	0.363	0.246	\$9,000,000	\$16,335,000	\$11,070,000	\$5,265,000
2	0.363	0.246	\$15,000,000	\$27,225,000	\$18,450,000	\$8,775,000
3	0.363	0.246	\$21,000,000	\$38,115,000	\$25,830,000	\$12,285,000

Excess Recovery for Pre 2017 Units

Old Annual Revenue Requirement	New Annual Revenue Requirement	Annual Difference	Total Difference
\$53,281,144	\$47,528,292	\$5,752,852	\$30,764,964

Based on IMM proposed CRF rates for pre 2017 units.

Excess Recovery for Post 2017 Units

Old Annual Revenue Requirement	New Annual Revenue Requirement	Annual Difference	Total Difference
\$28,479,043	\$19,840,359	\$8,638,684	\$64,020,531

Based on IMM proposed CRF rates for post 2017 units.

Total Excess Recovery

Existing Annual Revenue Requirement Total	New Annual Revenue Requirement Total	Total Annual Difference	Total Difference
\$81,760,187	\$67,368,651	\$14,391,536	\$94,785,495

CRF Substitution Issues

- **Substitution of a black start unit should be permitted only under very specific circumstances and with defined conditions**
- **A second unit at the same location, connected to the same bus.**
- **Review of costs of old and new units to ensure no overpayment**
 - **Cost reductions possible**

Monitoring Analytics, LLC

2621 Van Buren Avenue

Suite 160

Eagleview, PA

19403

(610) 271-8050

MA@monitoringanalytics.com

www.MonitoringAnalytics.com

