



AMP is a member of the American Public Power Association (“APPA”) and is also one of the public power Load Serving Entities (“LSEs”) and Joint Action Agencies (“JAAs”) described by APPA in its Post-Technical Conference Comments. AMP concurs with APPA’s observation in those comments that centralized capacity mechanisms administered by regional transmission organizations (“RTOs”) have not been able to attain a mature, or even stable, state.<sup>1</sup> The constant RTO “rules churn” does not just result in an overwhelmingly complex administrative capacity construct and resource exhaustion, but points to the fact that the basic capacity procurement construct is flawed. Accordingly, AMP supports APPA’s recommendation to reform the current RTO mandatory capacity market constructs to allow them to serve as voluntary, residual capacity procurement mechanisms.

As an alternative, and a minimum step to reform the capacity construct, the Commission should restore the unfettered ability of public power systems in the three Eastern RTOs to self-supply their own loads with their own resources.<sup>2</sup> This recommendation, however, should not be construed as support for an option like the Fixed Resource Requirement (“FRR”) approach included in the PJM Interconnection, LLC (“PJM”) capacity construct. In fact, while AMP fully supports and adopts the facts and arguments presented by APPA in its Post-Technical Conference Comments in this proceeding, the purpose of these comments is to provide facts and evidence in addition to those in APPA’s Post-Technical Conference Comments to support the conclusion that the FRR option is neither an adequate substitute nor an appropriate

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<sup>1</sup> See “Written Statement of Susan N. Kelly on Behalf of the American Public Power Association,” Accession No. 20130909-5278, Docket No. AD13-7-000 at 2 (submitted Sept. 9, 2013)(“APPA Statement”).

<sup>2</sup> *Id.* at 5-11.

accommodation for self-supply through the long standing business models of public power LSEs like AMP.

## **II. AMP'S INTEREST**

AMP's primary purpose is to assist its Member communities in meeting their electric and energy needs in a reliable and economic fashion. This purpose is served in a number of ways, including through the ownership of electric generating facilities, scheduling and dispatch of Member-owned generation, and through power supply and transmission arrangements that AMP makes with third-parties at the request of and on behalf of its Members. AMP has load and generation resources in both PJM and MidContinent ISO ("MISO") and must operate within and across the RTOs to effectively serve its Members and optimize its resources.

As market participants and Load Serving Entities ("LSEs") within PJM, AMP will be affected directly by any changes made to the capacity procurement mechanisms in PJM as a result of this proceeding. Moreover, as AMP has experienced, changes made to one RTO often migrate to others. Thus, changes made to the capacity procurement mechanisms in any of the eastern RTOs [ISO New England Inc. ("ISO NE"), the New York Independent System Operator, Inc. ("NY ISO") and PJM, together, "Eastern RTOs"] are of interest to AMP. AMP respectfully submits these comments for the Commission's review.

## **III. ANSWER TO THE FRR QUESTIONS POSED IN THE OCTOBER 25 NOTICE**

In its October 25 Notice, the Commission posed a series of questions for commenters to respond to in comments but noted that "[c]ommenters need not address every question." AMP provides the following response to the second series of questions

regarding (i) whether an alternative to mandatory centralized capacity markets like PJM's FRR option should be offered in other Eastern RTOs and, (ii) given that the FRR option was originally developed to address a narrow set of circumstances facing the PJM region and its market participants, whether modifications to the FRR option would be appropriate.

While the FRR approach may be a viable alternative for a small number of LSEs - those that are net long on capacity resources and are capable of supplying all capacity obligations plus reserve requirements for the entire FRR Service Area for a five-year period – the reality is that most LSEs and public power entities,<sup>3</sup> like AMP, operate under legal and practical constraints that limit their options for capacity self-supply. Because of those constraints, public power LSE's would face substantial risks and disincentives if they were forced to comply with eligibility requirements similar to those that govern FRR use. Simply put, the constraints inherent in the public power business model - a long-standing business model the Commission has recognized - preclude use of the FRR approach as a viable alternative to capacity markets.

The constraints inherent in the municipal portion of the public power business model flow from their status as components of municipal governments. Specifically, the municipal LSE business model is premised on securing a reliable supply of power for each utility's citizen-owners at a reasonable and stable cost. Often, municipal utilities (i) do not have fixed service areas, and (ii) utilize a diverse mix of resources including market purchases in order to diversify their power supply and lessen risk. Both items can present issues under the FRR option.

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<sup>3</sup> For purposes of these comments, we define the term "public power entities" to include (i) municipal utilities, (ii) public power-supply entities composed of either cooperatives, municipal utilities, or both, and (iii) joint action agencies.

For the reasons set forth below, the FRR approach simply is not a workable avenue for public power LSEs like AMP to avoid the costs and risks of participation in RTO-administered capacity markets.<sup>4</sup> In this regard, the Commission should not be misled by those who continue to insist that FRR is an adequate substitute for self-supply LSEs. Because the FRR approach is not viable for public power entities, the Commission should not confine this class of LSEs to using the ill-suited FRR option.

1. **Variability of Capacity Obligations**: The FRR approach is designed for LSEs that are net long on capacity resources because it requires the LSE to supply all of its capacity obligations plus its reserve requirements for its entire FRR Service Area<sup>5</sup> for a five year period. Specifically, the FRR rules prohibit LSEs from purchasing capacity in the RPM auctions. See PJM Reliability Assurance Agreement (“RAA”), Schedule 8.1(B). This basic FRR design element makes it fundamentally incompatible with the FERC recognized business model long used by AMP, its Members, and other public power utilities.

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<sup>4</sup> AMP uses the term “markets” solely as a shorthand way of referring to the administrative constructs through which PJM and the other eastern RTOs acquire capacity to meet resource adequacy targets in their respective footprints. These constructs bear little resemblance to true markets, and AMP’s use of the term as a shorthand reference should not be read to suggest otherwise.

<sup>5</sup> PJM defines the FRR Service Area as, “(a) the service territory of an IOU as recognized by state law, rule or order; (b) the service area of a Public Power Entity or Electric Cooperative as recognized by franchise or other state law, rule, or order; or (c) a separately identifiable geographic area that is: (i) bounded by wholesale metering, or similar appropriate multi-site aggregate metering, that is visible to, and regularly reported to, the Office of the Interconnection, or that is visible to, and regularly reported to an Electric Distributor and such Electric Distributor agrees to aggregate the load data from such meters for such FRR Service Area and regularly report such aggregated information, by FRR Service Area, to the Office of the Interconnection; and (ii) for which the FRR Entity has or assumes the obligation to provide capacity for all load (including load growth) within such area. In the event that the service obligations of an Electric Cooperative or Public Power Entity are not defined by geographic boundaries but by physical connections to a defined set of customers, the FRR Service Area in such circumstances shall be defined as all customers physically connected to transmission or distribution facilities of such Electric Cooperative or Public Power Entity within an area bounded by appropriate wholesale aggregate metering as described above.” PJM Reliability Assurance Agreement (“RAA”), Article 1, Section 1.31.

A key factor in the AMP business model relates to the variety of arrangements in effect between AMP and its Members. Under AMP's and its Members' long standing business model:

- There is a wide variety of ways in which Members use (or choose not to use) AMP as their power supplier. AMP supplies, at each Member's option, full or partial requirements wholesale power service to most of its Members. Supply arrangements are for terms that can range from less than one year to very long term. Members, however, also are free to take *no* power supply from AMP. AMP, in turn, undertakes to meet the array of its Members' needs in a number of ways, including through the ownership of electric generation, the scheduling and dispatch of Member-owned generation, and the entry into power supply and transmission arrangements with third parties at the request and on behalf of Members.
- There also is variation in whether Members participate in AMP-developed power supply projects. Members are free to participate (or not participate) in AMP-developed projects, and to participate at whatever level a Member believes fits best with its own portfolio. Alternatively, Members are free to contract for power supplies on their own, for some or all of their needs, as dictated by each system's individual needs and goals.
- There also is a wide variety of ways in which Members use (or choose not to use) AMP as their PJM LSE. Some Members designate AMP to act as the LSE for their loads and to interact on their behalf with PJM. Other AMP Members have their own PJM accounts; such members settle and schedule directly with PJM. In fact, some AMP Members participate in AMP projects and/or power supply contracts but use other entities as their PJM LSE. These entities are free to, and have changed PJM LSEs, switching from AMP to others as their PJM LSE over time.
- AMP also accommodates the addition of new Members and expects to continue to do so. Additionally, most AMP Member municipal utilities do not have certified or clearly defined service territories and AMP Member municipalities sometimes annex customers and may serve a limited amount of load outside of their corporate limits.<sup>6</sup>

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<sup>6</sup> See, for example, Sections 4933.81-4933.87, Ohio Revised Code.

For these reasons, there is great variability in (i) how AMP Members use AMP as their PJM LSE, (ii) how they participate in AMP projects or other power supply, (iii) how they acquire load and, (iv) how they provide capacity and energy for that load.

The above-described variation in arrangements and circumstances is a natural outgrowth of the long-standing public power business model FERC has recognized. Because of this variation, however, the unforced capacity obligations AMP and its Members must meet can fluctuate materially over time.<sup>7</sup> At the same time, though, the FRR requires an LSE to lock into a five-year commitment with no ability to use the RPM capacity market to resolve single-year excesses or shortfalls. By failing to address the possibility of material variations in an LSE's unforced capacity obligations during the commitment period, the FRR approach simply does not accommodate public power's longstanding and FERC-recognized business model.

**2. Prohibition of Residual RPM Purchases:** The FRR rules' prohibition on the purchase of capacity in the RPM BRAs or the incremental auctions serves as another basic FRR design element that makes it fundamentally incompatible with the FERC recognized business model long used by AMP, its Members, and other public power utilities. See RAA Schedule 8.1(B).

AMP has limited capacity resource options for self-supply, either because of the unavailability of economically priced capacity from existing generation, as discussed herein, or because of internal resource limitations for financing self-build options. Specifically, AMP's, its Members' and other public power entities' longstanding business models include not only safeguards against the kinds of market manipulation that

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<sup>7</sup> Notwithstanding the possibility of such fluctuation, AMP and the vast majority of its Members are net short and will remain so for the foreseeable future.

minimum offer price rules were designed to mitigate but tax and other prohibitions that effectively prohibit public power entities from using tax advantaged financing for anything other than governmental purposes.

For example, AMP has only developed and financed new generation projects if 100% of AMP's associated capacity and energy entitlements from such project is contracted for on a take or pay basis by its Members for at least the life of the bonds issued to finance the project, typically 30 years, and who retain rights to the project thereafter.

Additionally, in order to secure long-term capacity supply arrangements in the form of asset ownership or long-term capacity contracts at the lowest possible cost, municipal LSEs utilize tax exempt and tax advantaged financing. However, in order to maintain the critically important tax exempt and tax advantaged status, municipal LSEs must meet and maintain several mandatory conditions, including (but not limited to) a prohibition against the municipal LSE and any participants in a project financed with tax-advantaged obligations using the project for anything other than the governmental purposes of such municipal LSE or project participant or for any "private use."

The tax requirements and other obligations that are critical to the long-standing business models of public power and other self-supply LSEs serve as effective barriers against such entities building generation as merchant generation, market manipulation, or anything other than legitimate self-supply.<sup>8</sup> The restrictions also serve to limit the

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<sup>8</sup> The Commission's findings demonstrate that it concurs that the tax requirements and other obligations that are critical to the long-standing business models of public power and other self-supply LSEs, (coupled with net-short, net-long thresholds) serve as effective barriers against such entities building generation as merchant generation, market manipulation, or anything other than legitimate self-supply. See, *PJM Interconnection, LLC*, Docket Nos. ER13-535-000, ER13-535-001, Order Conditionally Accepting in Part, and Rejecting in Part, Proposed Tariff Provisions, Subject to Conditions at P 108 (May 2, 2013).

availability of resources available to AMP and other public power utilities. Thus, the prohibition of residual purchases from the RPM auction under the FRR rules imposes significant risks on AMP and smaller LSEs who are likely net buyers of capacity.

**3. Unavailability of Bilateral Options:** At the Technical Conference, Susan Tierney, Ph.D., Managing Principal, Analysis Group, stated that it was her understanding that either long- or short-term bilateral contracts could be included in the FRR supply plan to cover any shortfall that would otherwise be purchased through RPM. See page 272 of the Transcript of the September 25, 2013 Technical Conference (“Tr.”). However, it is difficult if not impossible to find existing generators in PJM today willing to sell capacity in bilateral arrangements at competitive prices that reflect the long-run cost of investment. Thus, the requirement to obtain enough capacity through bilateral arrangements to self-supply even the balance of its capacity obligations poses significant risks for LSEs like AMP.

**4. Non-Compliance Penalty:** Another deterrent to AMP’s, or its Members’, ability to use the current FRR option to self-supply its capacity obligations is the disproportionately higher penalty for non-compliance under the FRR rules as compared with the penalty for non-compliance with RPM auction rules. An LSE using the FRR approach that fails to submit its annual qualified plan demonstrating that it can satisfy 100% of its reliability requirements in any year is subject to a penalty of 2 times the gross Cost of New Entry (“CONE”) for each MW of deficient capacity. See, PJM RAA, Schedule 8.1 (D)(7). The LSE also may be subject to an FRR Capacity Deficiency Charge for failure to satisfy its Daily Unforced Capacity Obligation of 1.2 times the weighted average RPM clearing price for all RPM auctions for the zones covered by the

FRR plan. PJM RAA, Schedule 8.1(F)(2). These penalties likely will influence the price of a bilateral purchase, assuming capacity is available for a bilateral transaction. In contrast, the penalty for falling short of capacity commitments under RPM is the RPM auction clearing price plus the greater of 0.2 times that price or \$20/MW-Day times the amount of the capacity deficiency, a lower charge than either of the deficiency charges imposed under an FRR plan. PJM Open Access Transmission Tariff (“OATT”), Attachment DD, Section 8.2, referencing the Daily Deficiency Rate in Section 7.1(b) of Attachment DD. In other words, given the fact that the penalty for FRR non-compliance is significantly higher than the penalty for failing to secure enough capacity under RPM, if public power entities who wish to maintain their long-standing, self-supply business models are effectively required to do so under the FRR approach, they are subject to a disproportionate penalty for non-compliance.

5. **Restrictions on the Sale of Excess Capacity**: Finally, the lumpy nature of investment in generation results in a risk to the LSE using the FRR approach that the capacity in the early life of the resource that likely will be in excess of the LSE’s needs will be economically stranded given the significant restrictions under the FRR rules on an LSE’s ability to sell that excess capacity into RPM auctions. See PJM RAA, Schedule 8.1. Specifically, while an FRR entity is permitted to sell excess capacity into the RPM auctions, the sales are limited by both a minimum and a cap. An FRR entity may only offer to sell its capacity that is in excess of the “threshold quantity,” which essentially is the unforced capacity (“UCAP”) equivalent of the installed reserve margin multiplied by the forecast peak load plus the lesser of 3% of the UCAP or 450 MWs. RAA 1.82 Threshold Quantity; RAA Schedule 8.1 E. 2. However, the FRR entity may

not offer to sell excess capacity that exceeds an amount equal to the lesser of: (1) 25% times the UCAP equivalent of the installed reserve margin for the delivery year times the forecast peak load; or (2) 1300 MWs. RAA Schedule 8.1 E. 2. Thus, the threshold quantity creates a nominal amount of capacity above the required peak load forecast plus reserve margin that the FRR entity is not allowed to sell. And, even if the FRR entity has capacity above and beyond that extra reserve margin, it is restricted to selling only the excess capacity up to that limit. For most public power LSEs under the FRR option, these limitations would effectively strand capacity in excess of the LSE's needs. This would be an uneconomic and suboptimal use of capacity resources.

**6. LDA Boundaries:** The potential for changing LDA boundaries with differing internal minimum resource requirements, in combination with the five year length of the existing FRR rule, make use of the FRR approach a riskier option for LSEs in constrained LDAs (like AMP in American Transmission Systems, Inc.'s ("ATSI") transmission system). LDA boundaries can be modeled and potentially altered under the existing RPM rules for a variety of reasons, including PJM discretion. PJM Tariff, Attachment DD, Section 5.10(a)(ii). A change in such boundaries during a five year FRR plan may well result in a requirement to obtain a greater percentage of resources to satisfy capacity obligations from resources within the new LDA boundaries than existed at the time the LSE developed its five year FRR plan. Such a change would impose on the LSE a potentially significant risk that excess capacity from internal resources in the newly defined LDA may not be available for a bilateral transaction or that the owners of those resources may not be willing to sell that excess capacity in a bilateral transaction at reasonable and economic prices.

7. **RTO Migration**: The five year FRR plan requirement also adds risk resulting from transmission owner migration between RTOs to AMP's ability to export power from resources in one RTO for the beneficial use of AMP's Members located in another RTO or non-RTO areas. This is not a hypothetical or speculative risk for AMP.

AMP Members served from the ATSI transmission system or the Duke Energy Ohio ("Duke") transmission system were forced to transition from MISO to PJM because of decisions made by ATSI and Duke although AMP itself continues to have a substantial portfolio of existing and planned generating resources located within the MISO footprint, including several planned hydroelectric generating plants located along the Ohio River in Kentucky and AMP's 23 percent ownership interest in the 1,600 MW Prairie State Energy Center located in Southern Illinois. Importantly, in spite of the resulting separation of municipal generation resources from load, these generating resources continue to be dedicated to serving the needs of AMP's Members, including those Members that were effectively pulled from MISO into PJM by the RTO-change decisions of ATSI and Duke.

AMP's investments in operating generation in MISO (currently, AMP's share of Prairie State<sup>9</sup>) *already are being impaired* by the congestion charges MISO assesses whenever energy is delivered from AMP's MISO area resources across the PJM-MISO seam and into PJM. Those congestion charges today, plus charges for the required firm point to point transmission, represent a high portion of the delivered cost of energy from Prairie State to AMP's Prairie State Participants, approximately \$10/MWh for all

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<sup>9</sup> When Prairie State and the Smithland and Cannelton Hydroelectric Projects were planned and committed to by AMP, approximately 50% of AMP Members' load was in MISO, now less than 5% of AMP Members' load is in MISO due to the ATSI and DEOK "RTO Realignment".

MWhs delivered to the AMP Prairie State Participants during 2013.<sup>10</sup> The burden of these charges will only increase when the Smithland and Cannelton projects enter service and AMP moves energy from those resources across the seam to serve its PJM-area load. It bears repeating that AMP would not be suffering the full extent of these charges *but for the Commission's approval of the ATSI and DEOK "RTO realignments."* It is only because so many AMP Members were dragged by ATSI and DEOK from MISO into PJM — over the Members' protests and against their wishes — that AMP's Members are incurring these higher cross-border charges.<sup>11</sup>

**8. FERC Precedent:** While FRR may technically be an alternative to AMP or its Members, albeit one that does not work, the Commission has recognized that FRR should not be the *only* option for self-supply LSEs. The Commission has specifically recognized that RPM is also a choice for self-supply LSEs and the MOPR should not impede capacity investment under the long-standing business models. Specifically, the Commission held that whether to elect FRR or RPM is “an individual determination to be made by each state and distribution company.” 2011 MOPR Rehearing Order, 137 FERC ¶ 61,145 at P 100. The Commission also recognized that whether a self-supply LSE elects FRR or RPM will be “based upon their individual circumstances.” *Id.* At no time has the Commission indicated that in every instance, FRR is an appropriate way to accommodate LSEs operating under the identified long-

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<sup>10</sup> While AMP reserves firm transmission capacity for which it is not charged directly under PJM OATT, Schedule 7, AMP does get charged for associated ancillary services, under Ancillary Service Schedule 1 (Scheduling, System Control and Dispatch Services) and Ancillary Service Schedule 2 (Reactive Supply and Voltage Control from Generation Sources Service). These charges apply whether energy is scheduled or not.

<sup>11</sup> The November 29, 2013 filing by PJM to limit capacity imports from MISO into PJM could make it even more difficult for AMP to serve its Members in PJM with these generation resources. See, “Protest and Motion for Suspension and Other Relief by American Municipal Power, Inc.” filed on December 20, 2013, in *PJM Interconnection, L.L.C.*, Docket No. ER14-503-000.

standing business models that do not want to face market risk with respect to their capacity obligations.

#### **IV. CONCLUSION**

For the reasons set out above and as presented by the APPA, AMP requests that the Commission consider the foregoing comments, and to take affirmative steps as suggested by APPA and supported by AMP to revamp and improve RTO-administered mandatory capacity procurement mechanisms to better meet the needs of market participants and electric consumers. AMP further requests that the Commission find that the FRR option is neither an adequate substitute nor an appropriate accommodation for self-supply through the long standing business models of public power LSEs like AMP or its Members. The Commission should avoid limiting public power entities in PJM or other RTOs to the ill-suited FRR option and should not be misled by those who continue to insist that it is a workable option for LSEs that seek to avoid the risks and costs of participation in RTO-administered capacity markets.

Respectfully submitted,

/s/ John W. Bentine

American Municipal Power, Inc.  
John W. Bentine, Senior VP and General Counsel  
Lisa G. McAlister, Deputy General Counsel  
1111 Schrock Road, Suite 100  
Columbus, Ohio 43229  
Telephone: 614-540-6400  
Fax: 614-540-6397  
Email: [jbentine@amppartners.org](mailto:jbentine@amppartners.org)  
[lmcalister@amppartners.org](mailto:lmcalister@amppartners.org)

## CERTIFICATE OF SERVICE

I hereby certify that I have on this date caused a copy of the foregoing document to be served on each person included on the official service list maintained for this proceeding by the Commission's Secretary, by electronic mail or such other means as a party may have requested, in accordance with Rule 2010 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.2010.

Dated this the 8<sup>th</sup> day of January, 2014.

/s/ Lisa G. McAlister  
Lisa G. McAlister