Dynegy Comments on Capacity Portability for the MISO-PJM JCM Stakeholder Process
July 30, 2012

Dynegy Midwest Generation, LLC and Dynegy Power Marketing, LLC (collectively, "Dynegy") appreciate the efforts undertaken by MISO, PJM and all interested stakeholders in addressing capacity portability and other issues related to the June 11, 2012 Order on Resource Adequacy Proposal.[1] The Commission ordered FERC Staff to initiate an administrative docket (AD12-16-000) to gather comments on capacity portability, due August 10, 2012.[2] Dynegy, an owner and operator of capacity resources in both the MISO and PJM markets, submits the following comments for MISO's consideration.

At the core of this issue are the extreme capacity market design differences between MISO's capacity construct, which was recently approved by FERC, and PJM's Reliability Pricing Model ("RPM"). Dynegy shares the concerns voiced by Dayton Power and Light ("DPL") at the recent July 16, 2012 Joint & Common Market ("JCM") meeting. Generation and load customers on both sides of the MISO/PJM seam are likely to be impacted by the substantial differences in the capacity market rules on each side of the seam.

A well designed capacity market should include design elements that help guard against potential negative impacts. In the recent RA Order, FERC directed MISO on compliance to remove the proposed provisions from its tariff that would have protected capacity suppliers from the potential exercise of buyer market power. In order to even begin discussing capacity portability between MISO and PJM, the differing treatment of potential buyer market power is a significant issue that must be reconciled. Without minimum offer price rules ("MOPR") for MISO capacity buyers, the potential for price suppression will likely irreparably harm capacity providers on both sides of the MISO/PJM seam.

A joint and common market will require a commonality of energy market scheduling and transacting rules in both regions. There must be compatible operational, planning and scheduling processes for market participants providing energy, capacity and ancillary services at the seam.

<u>Dynegy's Major Concerns with Capacity Portability as Currently Proposed</u>

MISO's capacity market rules and overall market design must be fundamentally revised to create price convergence, where, for example, MISO-sourced capacity seeks to satisfy the capacity requirements for load located within PJM West. Price convergence is necessary because the overall differences in capacity market design are likely to result in significant differences in the price of capacity traded at the MISO/PJM seam.

---

[1] *Midwest Indep. Transmission Sys. Operator, Inc.,* 139 FERC ¶ 61,199 (2012) ("RA Order").

[2] *Id.* at P 330.

This will allow for reciprocal sales from PJM to MISO. MISO's capacity products and the related market rules must be aligned with PJM's RPM if price convergence is ever going to be achieved. Today energy is traded in both directions across the seam because price convergence occurs at the seam. This is not an accident – the market rules and the administration of the Joint Operating Agreement by MISO and PJM promote price convergence for energy. This is simply not yet the case for capacity.

If MISO market participants want to sell capacity into the PJM capacity market, the MISO capacity construct must include market rules and requirements like those that currently exist for PJM capacity market participants. Further, any capacity sales to PJM must have firm transmission and meet must offer and non-recall requirements. A requirement for firm transmission service is a set of well-defined physical property rights and not simply one of the "institutional barriers" to capacity portability. All interested parties on both sides of the seam need to have an understanding of how the Capacity Benefit Margin is determined and taken into account by both RTOs. Additionally, MISO-sourced capacity delivered to the MISO/PJM interface is not necessarily deliverable throughout the PJM footprint. The limited nature of the existing transmission system must continue to be taken into consideration in the discussion of capacity portability. Due to transmission and deliverability limitations, MISO's proposal that capacity portability can be achieved via an inter-RTO form of network service may not be feasible as currently proposed.

The MISO stakeholder process is the proper venue to work toward the further evolution of MISO's capacity construct that is necessary to achieve price convergence with PJM. While the parameters for MISO's capacity construct for the 2013-14 planning year have been set, MISO stakeholders must diligently use the stakeholder process at the SAWG to pursue these necessary market design changes if price convergence is going to have any realistic chance of occurring for the 2014-15 planning year.

MISO's capacity construct has several major fundamental flaws, as summarized below, which must be addressed in order to be better aligned with PJM's more mature RPM. These issues were the focal points of the Capacity Suppliers[3] September 15, 2011 protest of MISO's resource adequacy proposal and the July 11, 2012 rehearing request of the RA Order. The "regional differences"[4] frequently cited by MISO must be reconciled as a prerequisite to enhancing opportunities for capacity portability between MISO and PJM.

[3] Capacity Suppliers are Ameren Energy Marketing, Calpine Corporation, Dynegy Power Marketing, LLC, Dynegy Midwest Generation, LLC, Electric Power Supply Association, Exelon Corp., FirstEnergy Solutions Corp. and NextEra Energy Resources, LLC. The Capacity Suppliers are an *ad hoc* coalition of power providers and load serving entities in MISO advocating in support of a properly designed and well-functioning capacity market in MISO. The Capacity Suppliers represent approximately 13,300 MW of generation and 3,100 MW of load in the region.

[4] MISO has repeatedly cited the 90% traditional cost of service regulation operating in non-retail choice states as a basis for not proposing an "eastern style" mandatory forward capacity market.

- Forward Term – MISO's forward commitment time horizon is only two months prior to the start of the planning year versus PJM's three year forward time horizon. A two month forward commitment is not sufficient to create the long-term price signal in MISO that is necessary for investment in new capacity resources.

- The Fixed Resource Adequacy Plan ("FRAP") component of MISO's capacity construct allows loads to toggle in and out of the voluntary capacity auction year-to-year, for either all or part of their annual requirements. As designed, FRAP invites gaming, especially when contrasted to PJM's Fixed Resource Requirement ("FRR") which prohibits loads electing FRR from participation in PJM's auctions for the five years following an FRR election.

- Shape of the demand curve – MISO continues to rely on a vertical demand curve in its capacity construct versus a downward sloping demand curve to recognize the true value of an incremental MW of capacity beyond the reserve margin. This inherent shortcoming in the MISO construct should be addressed in the near term within the MISO stakeholder process.

- As previously noted, adequate protection against buyer market power through inclusion of sufficient MOPR provisions in MISO's tariff must be addressed.

- MISO's capacity construct is inequitable by design, with a "voluntary" annual auction design where generators must participate, subject to a 50 MW physical withholding threshold, while the participation of load is entirely voluntary.

As currently proposed, MISO's capacity construct will remain a bilateral market for the 2013-14 planning year with no real potential for promoting a long-term price signal for the construction of new capacity resources within the MISO region. Industry electric and IPP analysts at UBS Investment Research reached the same conclusion after the June 29 conference call with MISO Vice President of Market Operations, Richard Doying. UBS Investment Research stated:

> **Market not designed to provide new build signals…**
> Interestingly, while filed under the guise of "resource adequacy", the MISO capacity market construct would not be geared towards incentivizing new capacity. Rather, MISO believes the auction could work to bring modest incremental demand response resources at best. Much of the emphasis in the new capacity auction design would rely on vertically integrated utilities to *opt-out* of participation through the filing of fixed resource adequacy plans (FRAPs). We would hence look for overall market liquidity to prove limited, with a real chance for *extremely limited* clearing capacity across much of MISO.

While Dynegy is realistic and understands that the evolution of MISO's capacity construct via the SAWG will take time, the following operational, scheduling and planning processes can be addressed and improved upon in the near-term through the JCM initiative between MISO and PJM as follows:

- Transmission Operations Coordination
- Day-Ahead coordination
- Interchange Scheduling Business Rule Alignment
- Interchange Optimization
- Fine-tuning Market to Market Process
- Cross Border Projects to Address Market Efficiency
- Request for Incremental Auction Revenue Rights
- Market Participant Funded Upgrades

These are separate change processes (JCM and SAWG) that can be discussed in parallel where the capacity market evolution efforts should be undertaken by MISO market participants starting immediately in the SAWG. If MISO participants want to increase sales into PJM capacity market and enhance overall regional reliability by allowing the reciprocal provision of capacity from PJM to MISO, then MISO, including the state regulatory commissions and all other interested MISO stakeholders, must make a concerted and committed effort in the SAWG to bridge these vast capacity market disparities.