

PJM's base residual auction kicks off amid market concerns

May 12, 2014

The PJM Interconnection's Base Residual Auction (BRA) for the 2017/2018 delivery year begins on May 12, 2014, amid concerns regarding the capacity market raised in a report for PJM Interconnection by an independent market monitor.

The BRA sets prices for wholesale generation capacity resources needed to serve the anticipated load during the delivery year. This cost is typically passed along to consumers in the generation portion of their overall electric bill. The objective of each BRA is to procure capacity reserve for electricity in a least-cost manner.

This reserve of generating capacity ensures that there are adequate resources to meet system electricity requirements and to prevent brownouts and blackouts. The results of the auction will be posted on May 19, 2014.

In the recent report, [State of the Market Report for PJM](#), done by the Independent Market Monitor (MMU) for PJM, concerns about various aspects of PJM's capacity market were raised. The capacity market is intended to function so that when energy market revenues are low, capacity market prices are higher, thereby incentivizing investment in generation. However, according to the MMU, market design deficiencies in PJM's capacity market may be leading to the premature retirement of generation resources:

It is more critical than ever to get capacity market prices correct. A number of capacity market design elements have resulted in the substantial suppression of capacity prices for multiple years. The impact in the 2016/2017 base auction was about \$4.6 billion. That price suppression has had and continues to have a negative impact on net revenues and thus on the incentive to operate existing units and to invest in new units. Price suppression is more acute in western zones than in eastern zones. Price suppression leads to premature and uneconomic retirements and the failure to make economic investments. Coal units and nuclear units are under stress in PJM markets.

In all, the MMU's report found that PJM's "aggregate market structure was evaluated as not competitive." To address the market design issues, the MMU made a series of recommendations, including:

- The enforcement of a consistent definition of capacity resource that is required to be a physical resource;
- That the definition of demand-side resources be modified in order to ensure that such resources be fully substitutable for other generation capacity resources;
- The clarification of protocols for recalling the energy output of capacity resources when PJM is in an emergency condition;
- That generation capacity resources be paid on the basis of whether they produce energy when called upon during any of the hours defined as critical; and

- That PJM eliminate the broad exception related to lack of gas during the winter period for single-fuel, natural gas fired units.

Capacity prices determine roughly 10 to 15 percent of customers' electric bills. The generation portion of the bill — about half of the total — includes capacity, as well as the energy prices for electricity when it is actually produced.

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