

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Illinois Commerce Commission)
On Its Own Motion)
) 06-0800
Investigation of Rider CPP of Commonwealth)
Edison Company, and Rider MV of Central)
Illinois Light Company d/b/a AmerenCILCO,)
of Central Illinois Public Service Company d/b/a)
AmerenCIPS, and of Illinois Power Company)
d/b/a AmerenIP, pursuant to Commission Orders)
regarding the Illinois Auction)

INITIAL BRIEF OF THE CITIZENS UTILITY BOARD

CITIZENS UTILITY BOARD

Julie Soderna
Anne McKibbin
208 S. LaSalle, Suite 1760
Chicago, Illinois 60604
312-263-4282
312-263-4329 fax
jsoderna@citizensutilityboard.org
amckibbin@citizensutilityboard.org

TABLE OF CONTENTS

I.	INTRODUCTION.....	1
II.	ARGUMENT ON CONTESTED ISSUES.....	3
	A. Use of an Auction.....	3
	1. For the Fixed Price Section, should the auction be modified as follows.....	3
	b. Use of demand side bidding.....	3
	2. Alternatives to the auction whereby the utility, or some other procurement manager, separately procures baseload, intermediate, and peaking load resources to meet expected load requirements.....	11
	a. CUB’s proposal to bid base, intermediate, and peak loads separately is properly within the scope of this docket.....	11
	F. Customer Supply Group Definitions.....	13
	2. Separate Auction product for residential and/or small business customers.....	13
III.	CONCLUSION.....	14

I. INTRODUCTION

On December 20, 2006, the Commission initiated this proceeding to review the Illinois Auction process. Initiating Order at 1. This proceeding fulfills the Commission's intent, stated in the Procurement Docket Orders, to hold a periodic docketed review of the auction process. ICC Docket No. 05-0159, Order at 154; ICC Docket Nos. 05-0160, 05-0161, and 05-0162 (cons), Order at 157-58.

The Commission initiated this proceeding to determine whether the Illinois Auction tariffs, Rider CPP of ComEd and Rider MV of each of the Ameren Companies, "are unjust, unreasonable, discriminatory or preferential, or in any way in violation of any provisions of law." Initiating Order at 5. The Commission stated, "the reviews, recommendations, and suggestions" presented in the public reports of the Auction Manager and Staff are "appropriate examples of the types of issues to be considered in this docket." *Id.* Consequently, the Commission made the public reports of the Staff and Auction Manager a part of the record. *Id.* at 6. In addition, the Commission emphasized that this docket should address issues "directly related to matters that have come to the attention of the parties as a result of the conduct of the auction process itself, or that relate to proposed changes to the auction process to address facts or circumstances that are new or different from those considered in the Procurement Dockets." *Id.* at 5-6.

The Illinois Procurement Auction (hereafter "the auction"), held in September 2006, produced significant increases in customer rates. When coupled with increases in delivery service rates, average customer bills have increased by 22% to more than 55%. Some groups of customers have experienced much higher increases. CUB Ex. 1.0 (Second Corrected) at 2. These prices, and the accompanying public outrage, are a result of the conduct of the auction

process and were not known during the Procurement Dockets. Staff's Report suggests that these prices include a risk premium of between 7% and 25%. ICC Staff Report at 16. CUB's proposed auction modifications will reduce auction prices directly by allowing all resources to participate, and indirectly by reducing the risk premium. CUB Ex. 1.0 (Second Corrected) at 3-4, 17. In addition, Staff's report specifically recommends a reexamination of the Customer Supply Group Definitions. ICC Staff Report at 47. While CUB's proposal for redefining Customer Supply Groups differs from the proposal in Staff's report, they share a purpose – to reduce the risk premium. CUB Ex. 1.0 (Second Corrected) at 17; ICC Staff Ex. 1.0 at 20-21 (ultimately finding that Staff does not believe its proposal would reduce switching risk).

ComEd suggests that CUB's proposals are outside the scope of this proceeding, and its witness Ms. Tierney suggests that CUB's proposals go too far. ComEd Ex. 4.0 at 17-19. CUB's proposals are significant. But so are the rate increases that now face Illinois electricity customers, but were unknown during the Procurement Dockets. CUB Ex. 1.0 (Second Corrected) at 2. Because CUB's proposals directly address these facts, that were not known during the Procurement Dockets, and a recommendation made in Staff's Report, they are within the scope of this docket as described by the Commission in its Initiating Order. Initiating Order at 5-6.

Throughout this proceeding, CUB has made constructive, substantive proposals, including (1) modifying the Fixed Price Section of the auction to allow demand side bidding, (2) modifying the auction to create separate auction products for base, intermediate, and peak loads, and (3) changing the customer supply group definitions to create separate auction products for smaller customers. CUB proposes these changes because they will reduce the prices that result from the auction. Consequently, CUB's proposals are within the scope of this proceeding.

Initiating Order at 5-6. In addition, the Commission has full authority to adopt CUB's proposals stemming both from its general authority to ensure just and reasonable rates and from the same source as its ability to adopt any modifications to the current auction. 220 ILCS §5/9-101. The Commission should adopt the following proposals because they will result in lower prices for customers. Discussion of the proposals below is organized according to the Joint Brief Outline filed in this docket.

II. ARGUMENT ON CONTESTED ISSUES

A. Use of an Auction

1. For the Fixed Price Section, should the auction be modified as follows:

b. Use of demand side bidding.

CUB proposes to modify the Fixed Price Section of the auction to allow the use of demand side bidding. Because the current auction only allows generation resources to participate, and excludes other demand side resources such as energy efficiency and demand response, it cannot produce the lowest possible prices. CUB Ex. 1.0 (Second Corrected) at 3. To eliminate these barriers, CUB proposes to redesign the auction to create separate, consecutively bid auction products for energy efficiency, demand response, and generation. CUB Ex. 2.0 at 13-14. CUB refers to this as the three-tier bidding approach. *Id.* at 13.

The three-tier bidding approach splits the auction into three consecutive sections, as described by CUB witness Mr. Crandall's testimony. First, the utilities would hold an auction to purchase a block of energy efficiency. The utilities would purchase all energy efficiency resources they perceive to be cost effective. CUB Ex. 2.0 at 13. Utilities would then determine the shape and amount of the remaining load that they did not procure in the energy efficiency tier. *Id.* Second, the utilities would hold an auction to purchase all of the dispatchable, peak-

reducing demand response resources that they perceive to be cost effective. *Id.* Then, the utilities would again determine their remaining needs. The resulting load curve would become the basis for the third tier auction for generation supply. *Id.* at 14.

To ensure the success of the three-tier approach, the Commission should make certain that the utilities clearly define the conditions under which they will call demand response resources for economic or reliability reasons. CUB Ex. 2.0 at 14. In addition, to reduce supply risk, the auction must allow sufficient time for the utilities to compile accurate forecasts of their needs after the first and second tiers. *Id.*

The three-tier approach explicitly incorporates energy efficiency and demand response resources into the auction. Illinois needs such an approach because energy efficiency and demand response resources offer a number of benefits for customers. Existing energy efficiency and demand response programs are not fully capturing those benefits, and the current auction creates barriers to their full participation in the Illinois electricity markets. CUB Ex. 2.0 at 6-10.

Energy efficiency resources meet customers' energy needs for a lower cost than generation procured under the current Illinois auction. CUB Ex. 2.0 at 5. For example, the American Council for an Energy Efficient Economy's April 2004 analysis shows that energy efficiency programs in 18 states have reported a cost of between \$0.023 and \$0.044 per kilowatt-hour saved. *Id.* This is significantly lower than the auction-clearing price of approximately \$0.064 per kWh. *Id.* The amount of energy efficiency that utilities could procure is potentially significant as well. For example, a recent study indicates that conservative energy efficiency programs could reduce Michigan's peak electric demand by 660 MW and annual energy use by 4,952 gigawatt-hours. *Id.* at 6 (*citing* CUB Exhibit 2.05 at 6, 32). Based on the experience of

surrounding states, it is reasonable to believe that significant amounts of energy efficiency are untapped in Illinois, as well. CUB Ex. 2.0 at 6.

Demand response also provides significant benefits to consumers, as it “discipline[s] wholesale market prices, reduce[s] opportunities for generators to exercise market power, and ensure[s] an efficient allocation of resources.” CUB Ex. 1.0 (Second Corrected) at 9-10. A U.S. Department of Energy report lists three types of benefits to demand response programs: (1) direct participant benefits; (2) collateral benefits, which accrue to all electricity consumers, and (3) other benefits, which are more difficult to quantify. *Id.* at 10 (*citing* U.S. Department of Energy – Benefits of Demand Response in Electricity Markets and Recommendations for Achieving Them: A Report to the United States Congress Pursuant to Section 1252 of the Energy Policy Act of 2005 (hereinafter “DOE Report”), February 2006, at 26-29). Participant benefits consist of increased reliability and financial benefits, including cost savings from using less energy and shifting usage to lower-priced hours and payments for curtailing usage in a demand response program. CUB Ex. 1.0 (Second Corrected) at 10. Collateral benefits, which accrue to all customers, regardless of participation, result from “a more efficient use of the electricity system” and include “bill savings to consumers from avoided energy and, in some cases, capacity costs.” *Id.* at 11, *citing* DOE Report. Collateral benefits also include additional reliability benefits and long-term market impacts such as avoided capacity investments. *Id.* (*citing* DOE Report). Other benefits identified by the DOE Report include more robust retail markets, improved choice, market performance benefits, and possible environmental benefits. *Id.* (*citing* DOE Report).

In addition, demand response repairs a market flaw that leads to inefficient prices. *See* CUB Ex. 1.0 (Second Corrected) at 14-15. The DOE Report states that “[s]tates should consider aggressive implementation of price-based demand response for retail customers ... Flat, average-

cost retail rates that do not reflect the actual costs to supply power lead to inefficient capital investment in new generation, transmission and distribution infrastructure and higher electric bills for customers.” *Id.* at 15 (*citing* DOE Report, at V). The DOE Report also stated:

As a result, electricity costs may be higher than they would otherwise be because high-cost generators must sometimes run to meet the non-price responsive demands of consumers. The lack of price-responsive demand also gives generators the opportunity to raise prices above competitive levels and exercise “market power” in certain situations. In the long term, the impact of insufficient demand response may be even greater as non-price-responsive peak demand can result in long-term investments in expensive generation capacity. An important benefit of demand response is therefore avoidance of capacity investments in peaking generation units to serve heightened demand that occurs in just a few hours per year.

Id. at 16 (*citing* DOE Report at 7-8). Aggressive demand response and energy efficiency can both protect customers, and can begin to provide discipline lacking in the wholesale markets. *Id.* at 16.

Existing energy efficiency and demand response programs are insufficient to capture the full benefits of these resources. CUB Ex. 1.0 (Second Corrected) at 6-9. Existing energy efficiency programs are often seasonal and rely on irregular funding by utilities. *Id.* at 6-7. While CUB supports these programs, they do not represent a comprehensive set of energy efficiency resources. *Id.* at 7. For example, Illinois does not enjoy the wide range of energy efficiency programs, including rebates, special rate options, and other incentives that are offered in other Midwestern states. CUB Ex. 2.0 at 6-7 (*citing* CUB Exhibit 2.02, 2.03). In addition, we should not rely solely on market price signals to provide incentives for energy efficiency. CUB Ex. 1.0 (Second Corrected) at 7. Market barriers such as high up-front costs for energy efficient equipment and a lack of consumer knowledge prevent the market from fully serving the interests of Illinois customers. *Id.*

ComEd and Ameren also currently offer some demand response programs to customers and ComEd offers demand response resources into the PJM market. CUB Ex. 1.0 (Second Corrected) at 11-12. However, significant opportunities for demand response expansion remain. For example, ComEd has only used its Rider CLR7 and VLR7 demand response programs for commercial and industrial customers two times in the past 12 months. CUB Cross Ex. 1 (VLR7); CUB Cross Ex. 2 (CLR7). *See also* ComEd Ex. 6.0 at 3-5 (description of Rider CLR7 and VLR7 programs). These programs could be altered or supplemented to provide more aggressive demand response at times of high peak prices, thereby lowering average prices for all customers. *See* CUB Ex. 1.0 (Second Corrected) at 11-12.

CUB proposes to modify the current auction process because it creates barriers to the use of cost-effective energy efficiency and demand response resources. CUB Ex. 2.0 at 8-9. The current auction process makes no provisions for demand response and energy efficiency options whatsoever. *Id.* In addition, the load-following vertical tranche prevents both energy efficiency and demand response resources from competing with supply in the auction. *Id.* at 7-9.

Each vertical tranche is a slice of load measuring 50 MWs at peak and perhaps 30 MW on average. CUB Ex. 2.0 at 8; ICC Staff Report at 36. To supply a tranche, bidders must supply a mix of base load, intermediate, and peaking resources. CUB Ex. 2.0 at 8. Bidders cannot use energy efficiency to supply part of a tranche under existing procedures. *Id.* at 10. This is because the current auction does not allocate energy efficiency to a specific bidder. *Id.* Thus, energy efficiency provided by one supplier reduces total load - the megawatts that all bidders must supply to fulfill their tranches – and the energy efficiency supplier cannot bid their efficiency into the auction. *See Id.*

In addition, demand response resources only reduce peak demand. CUB Ex. 2.0 at 9. Thus, the load-following nature of the auction product prevents bidders who specialize in demand response resources from bidding in the auction. *Id.* at 9-10. In practice, it is difficult for demand side resource bidders to assemble resources to serve base, intermediate, and peak load to supply a full tranche. *Id.* at 9. As Mr. Crandall’s testimony states, “[i]t is very difficult to develop a demand side infrastructure for only a 5-10 MW slice.” *Id.* at 8. Specifically:

Because demand side resources are location-specific, bidders/resource planners cannot develop a system-wide demand side resource to sell elsewhere if they do not win the bid for the tranche. This represents a barrier to participation that does not exist for generation. While a generator can sell its generation into the market elsewhere, a bidder would not control load in northern Illinois to provide resources to fulfill a bid in Ohio, because demand side resources are location-dependent in nature. A demand side supplier that has invested in demand response infrastructure in a specific location has no option to transport that resource to another location if they fail to win the bid for a tranche in Illinois.

Id. at 8-9. Mr. Crandall concluded that the three-tier auction process is needed to allow demand side resources to fully participate in the Illinois electricity market. *See Id.* at 13.

PJM and MISO, the underlying wholesale electricity markets in Illinois, balance the amount of electricity demanded with the amount supplied. CUB Ex. 1.0 (Second Corrected) at 13. However, the PJM and MISO markets cannot, by themselves, remove these barriers to demand side resources. *Id.* at 12-13. In addition, neither PJM nor MISO require load-serving entities, such as utilities, to bid either energy efficiency or demand response into the PJM and MISO wholesale markets. *Id.* at 13. In addition, the PJM and MISO markets are designed to meet the collective needs of an entire region, not just Illinois. Thus, while demand response and energy efficiency benefit customers, “we cannot expect that the wholesale markets will send signals of sufficient strength to make it happen.” *Id.* at 13.

The three-tier bidding process explicitly integrates demand response and energy efficiency into the auction. In doing so, it will result in lower prices for consumers and opportunities for companies that specialize in demand response and energy efficiency. *See* CUB Ex. 2.0 at 7, 9, 13-14. Consequently, the Commission should adopt it. If, however, the Commission does not feel that it can adopt this proposal in time to adjust the 2008 auction, CUB suggests that the Commission open a new proceeding to consider the proposal for a later auction. *Id.* at 4.

The Commission has full authority to adopt this proposal. Indeed, the Commission's authority to adopt CUB's proposals comes from both its general authority to ensure just and reasonable rates and from the same source as its ability to adopt any modifications to the current auction. 220 ILCS §5/9-101. Staff witnesses Dr. Kennedy and Mr. Zuraski opine on the Commission's authority to oversee utility-funded demand-side management programs. ICC Staff Ex. 4.0 at 7-8. Dr. Kennedy and Mr. Zuraski first cite the Commission's recent termination of several rulemaking dockets regarding energy efficiency and demand response issues. *Id.* at 7. However, the Commission may decide to terminate a rulemaking docket for any reason, or no reason at all. Thus, the termination of these dockets does not, in itself, speak to the Commission's authority regarding energy efficiency and demand response issues.

Dr. Kennedy and Mr. Zuraski also note that the Commission's "infrastructure for evaluating energy plans and conservation programs was eliminated" with the repeal of Sections 8-402 and 8-404 of the Illinois Public Utilities Act ("PUA"). ICC Staff Ex. 4.0 at 7. These sections of the PUA "required utilities to provide 20-year energy plans, and to include in those plans, ... 'a demonstration that the plan fully considers and utilizes all available, practical and economical conservation, renewable resources, cogeneration and improvements in energy

efficiency.’” *Id.* The repeal of these sections does not affect CUB’s current proposal. Due to the restricted scope of this proceeding, CUB is not proposing that the utilities provide a 20-year energy plan or that Staff evaluate energy plans or conservation programs, despite their merits. CUB’s proposals only call for the Commission to allow these resources to bid into the auction. Even if it is necessary to demonstrate that utilities fully considered conservation and demand response bids in the modified auction, the repeal of a section of the PUA involving 20-year energy plans does not logically preclude the Staff from evaluating such a demonstration.

The repeal of Section 8-404 of the PUA does not hinder CUB’s proposals either. Dr. Kennedy and Mr. Zuraski note that Section 8-404 stated, “the Commission is also authorized to require any public utility to implement energy conservation, demand control, or alternative supply programs ... whenever the Commission determines after hearing, that such programs are likely to be cost-effective.” ICC Staff Ex. 4.0 at 8 (*citing* PUA Section 8-404 (repealed)). Again, CUB is not asking the Commission to require that utilities implement any conservation programs themselves. Instead, CUB only proposes that the Commission allow energy efficiency and demand response providers to bid into the auction.

Dr. Kennedy and Mr. Zuraski “do not recommend that the Commission commence another general proceeding to consider demand response and energy efficiency programs given the open issues regarding the scope of the Commission’s authority.” ICC Staff Ex. 4.0 at 8, L. 177-180. Dr. Kennedy and Mr. Zuraski further note that “it would be prudent” to define the boundaries of Commission authority regarding “oversight of utility-funded demand-side management and energy efficiency programs” before opening any related dockets. *Id.* at 8, L. 180-185. CUB agrees and requests that the Commission make a definitive ruling on the matter to alleviate Staff’s concerns about the “open” nature of the Commission’s authority.

A. Use of an Auction

2. Alternatives to the auction whereby the utility, or some other procurement manager, separately procures baseload, intermediate, and peaking load resources to meet expected load requirements.

CUB also proposes an alternative to the three-tier bidding process. If the Commission does not choose to adopt the three-tier bidding process, then it should consider the following proposal to diminish the barriers to demand response created by the current auction, described above. CUB proposes modifying the current auction to create separate auction products for the base, intermediate, and peak loads. CUB Ex. 2.0 at 16. This modification would alleviate the barriers to demand response resources. *Id.* Demand response reduces peak load. However, as discussed in section A.1.b., above, it is practically difficult for specialized demand response providers to fulfill vertical tranches that require them to provide base, intermediate, and peak load. *Id.* at 9. This proposal eliminates the vertical tranche, and instead allows bidders specializing in dispatchable demand response, such as remotely operated air conditioner cycling, to bid specific resources for the peak auction product only. *Id.* at 16.

Unfortunately, this proposal would not incorporate low-cost energy efficiency products into the Illinois electricity resource mix. CUB Ex. 2.0 at 17. Energy efficiency reduces all base, intermediate, and peak load. *Id.* Thus, separately bidding for base, intermediate, and peak load would not give an additional incentive to provide energy efficiency. *Id.* Consequently, this proposal improves on the existing auction, but does not provide as many benefits as the three-tier approach.

a. CUB’s proposal to bid base, intermediate, and peak loads separately is properly within the scope of this docket.

The Commission’s Initiating Order stated, “the reviews, recommendations, and suggestions” presented in the public reports of the Auction Manager and Staff are “appropriate

examples of the types of issues to be considered in this docket” and made the public reports of the Staff and Auction Manager a part of the record. Initiating Order at 5-6. In addition, the Commission emphasized that this docket should address issues “directly related to matters that have come to the attention of the parties as a result of the conduct of the auction process itself, or that relate to proposed changes to the auction process to address facts or circumstances that are new or different from those considered in the Procurement Dockets.” *Id.*

Staff’s own Report considers the issue of the basic product definition – the tranche. ICC Staff Report at 36. Staff acknowledges that the current definition creates some risk for suppliers, but does not discuss the barriers that the use of the tranche creates for demand side resources. *Id.* The existence of these barriers falls directly within the issue of whether the auction should continue to use the tranche as its basic product. While Staff recommends that the auction continue to use the tranche, CUB believes that the Commission should examine this issue further in this docket, in light of the barriers to demand side resources presented by the current auction. *Id.*; CUB Ex. 2.0 at 16.

CUB’s proposal to modify the auction process to create separate auction products for base, intermediate, and peak load is intended to reduce the prices that result from the auction. *See* CUB Ex. 2.0 at 7, 17. The prices that resulted from the current auction, and the resulting public outrage, were not known during the Procurement Dockets. CUB’s proposed auction modification will reduce these auction prices and is, consequently, properly within the scope of this docket. Because CUB’s proposal directly addresses the issues raised in Staff’s Report and facts that were not known during the Procurement Dockets, it is within the scope of this docket as described by the Commission in its Initiating Order. Initiating Order at 5-6.

F. Customer Supply Group Definitions

2. Separate auction product for residential and/or small business customers.

CUB proposes changing the customer supply group definitions to create separate auction products for smaller customers. CUB Ex. 1.0 (Second Corrected) at 17-18. The auction price includes a risk premium that results, at least partly, from the ability of larger customers to switch suppliers. ICC Staff Report at 16. *See also* ICC Staff Ex. 1.0 at 22 (regarding switching). Separating smaller customers, many of whom cannot switch suppliers, would protect these customers from this risk premium and the associated increase in the auction price. CUB Ex. 1.0 (Second Corrected) at 17.

Practically speaking, a separate auction product should be constructed for (1) Ameren DS-1 and DS-2 customers and (2) ComEd's Residential and Small Load Customer Groups. CUB Ex. 3.0 at 2. Ameren's DS-1 and DS-2 customers demand up to 150 kw and ComEd's Residential and Small Load Customer Groups demand up to 100 kw. *Id.* Both Ameren and ComEd have indicated in testimony that they do not object to such a division of the current customer class definitions. Ameren Ex. 6.0, L. 272-276; ComEd Ex. 2.0, L. 495-513. In addition, Staff does not oppose such a division of the current customer class definitions. ICC Staff Ex. 1.0 at 21-22. Indeed, Staff agrees that such a division may lower prices for residential and small non-residential customers. *Id.*

Staff has expressed general concerns, however, that dividing the customer class definition raises certain measurement concerns. ICC Staff Ex. 1.0 at 22. These concerns were addressed by utility testimony during cross examination and that testimony should alleviate Staff's stated concerns. Specifically, to compute the hourly load served under the new customer class' auction contract, the utilities would need to take a representative sample of metering data from customers in the new customer class. *Id.* at 22. Alternatively, utilities would need to install hourly meters

for every member of the customer class. *Id.* At the evidentiary hearing, Ameren witness Mr. Blessing and ComEd witness Mr. McNeil both stated that their utilities are currently able to take the representative sample of metering data needed to implement the change in customer class definitions. April 25, 2007 Tr. at 332 (Blessing), 519 (McNeil). Thus, the Commission should adopt this proposal.

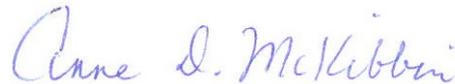
III. CONCLUSION

For the reasons discussed above, CUB respectfully requests that the Commission adopt our proposed modifications to the Illinois Auction.

May 30, 2007

Respectfully submitted,

CITIZENS UTILITY BOARD,



By: _____

Anne McKibbin

CITIZENS UTILITY BOARD

Julie Soderna
Anne McKibbin
Citizens Utility Board
208 S. LaSalle, Suite 1760
Chicago, IL 60604
(312) 263-4282
(312) 263-4329 fax
jsoderna@citizensutilityboard.org
amckibbin@citizensutilityboard.org

