REPLY COMMENTS ON THE 2008 PROCUREMENT PROCESS PURSUANT TO SECTION 16-111.5(o) OF THE PUBLIC UTILITIES ACT

PRESENTED TO

THE ILLINOIS COMMERCE COMMISSION

by

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I. INTRODUCTION

Boston Pacific Company, Inc. served as the independent monitor for both the recent 2008 Illinois RFPs and the 2006 Illinois Auction. On May 15, 2008 we filed Initial Comments in this proceeding.[1] Today we are filing Reply Comments.

The 2008 RFPs and the 2006 Auction solicited different products and used different procurement designs. In our Initial Comments we noted that "these back-to-back procurements in Illinois provide an ideal opportunity to assess procurement design for the long run."[2] We all want to find the best possible product definition and procurement design so we get the best possible deal for Illinois ratepayers given market and regulatory conditions. To that end, it is essential that the results of the 2008 RFPs and 2006 Auction be compared accurately.

The Attorney General's (AG's) Initial Comments focused almost exclusively on a comparison of the prices in these two solicitations.[3] Such a comparison is complex and, based on the limited information in the filing, the calculations in the AG's comments appear to contain some errors. We would be happy to meet with the AG to better understand these calculations and to explain our concerns. To that end, the remainder of our Reply Comments address these possible calculation errors.[4]

II. RESPONSE TO THE ATTORNEY GENERAL'S INITIAL COMMENTS

At the outset, let us say that there is no disagreement on one point: Boston Pacific agrees with the AG that the winning prices in the 2008 RFPs are higher than the winning prices in the 2006 Auction when the prices are put on an apples-to-apples basis. The only open question is by how much.

In the AG's Comments at page 6, a bar chart shows this increase in price. Using information in the text, we understand that the AG shows the winning prices in the ComEd 2008 RFP to be $68.82/MWh. This is the sum, from page 4, of the block energy price of $63.66/MWh, plus $0.85/MWh for ancillary services, plus $4.31/MWh for capacity.

Also in the AG's chart on page 6 is the comparable price for the 2006 Auction, $63.96/MWh;[5] this 2006 price already includes full requirements service (block energy,

[1] *Comments on the 2008 Procurement Process Pursuant to Section 16-111.5(o) of the Public Utilities Act*, Boston Pacific Company, Inc., (BP Initial Comments), Published May 16, 2008, www.icc.illinois.gov/downloads/public/en/BostonPacificInitialCommentsMay15.pdf

[2] Ibid., p. 3

[3] *Comments and Recommendations By the People of the State of Illinois on the 2008 Electricity Procurement Process*, Illinois Attorney General, (AG Initial Comments), Published May 16, 2008, www.icc.illinois.gov/downloads/public/en/051508final.doc

[4] Note that our Reply Comments deal exclusively with the AG's Initial Comments and the final prices in the 2006 and 2008 ComEd procurements. We are not here commenting on other provisions of the Act such as the ComEd or Ameren swaps, on other topics breached in the initial comments process, or on the Ameren procurement.

[5] On page 7 of the AG's Initial Comments, the price given for the winning auction price ComEd in 2006 is $64.00. This is the price for the 29-month product that year. We believe that the 17-month product from 2006 is a better

dispatchable energy, ancillary services, and capacity). This means that by the AG's reckoning, the winning prices from the 2008 RFPs are about 7.6% higher than the winning price from the 2006 Auction. [$68.82/MWh divided by $63.96/MWh]

However, we see some possible errors in the AG's calculations that lead us to find that the prices from the 2008 RFP are at least 22% higher than the comparable prices from the 2006 Auction. To see this, let us look at each component of the AG's calculation.

- First, using the correct and public information on the load weightings, the average winning price for block energy in the ComEd RFP is $67.49/MWh, not $63.66/MWh as calculated by the AG. We do not know the source or methodology of the AG's calculation.

- Second, the AG estimates that the capacity price will be $4.31/MWh while we estimate it to be more than double that amount. There should be little disagreement here since the capacity price is dictated by a PJM RPM Auction that already has concluded. The winning price from the PJM RPM Auction is reported on the PJM web site as $113.22/MW-day.[6] For a full year, then, the price is $41,325/MW. [$113.22 multiplied by 365 days] To convert this to dollars per MWh, we have to estimate how many MWh are sold for each MW of capacity; the load factor tells us this, and a rough estimate of the load factor is 50%. Given that, the PJM RPM capacity price translates to $9.44/MWh as compared to the $4.31/MWh calculated by the AG. [$41,325/MW-year divided by 50% of the hours in a year, or 4,380] We would expect that the AG's error here can be traced to a failure to make the adjustment for load factor.

- Third, we think the price of ancillary services is a bit low since it is typically estimated at 2% or 3% of energy costs. However, we can use the AG's $0.85/MWh because no one can know the true cost of ancillary services for the coming year until that year is over; ComEd will buy these ancillary services during the year from the PJM Markets.

- Fourth, the failure to add in the cost of dispatchable energy also makes the AG's estimate too low. But, again, we cannot know what the Illinois ratepayers will pay until the year is over. If the block of energy secured in the RFP is more than is needed, ComEd will be selling into the PJM spot market, while if it is less than what is needed, ComEd will be buying PJM' spot energy. On balance, it is reasonable to expect that Illinois ratepayers will pay something for this dispatchable energy.[7]

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comparison to the one-year product solicited in 2008, so our calculations are based off of the slightly different value for the 17-month product, $63.96.

[6] This is the Final Zonal Capacity Price for the COMED Zone in the 2008/2009 Base Residual Auction. See the PJM website at www.pjm.com or access the results directly at www.pjm.com/markets/rpm/downloads/2008-2009-base-residual-auction-results.xls [accessed May 21, 2008].

[7] It is reasonable to expect that, on balance, Illinois ratepayers will pay extra for this dispatchable energy. When buying in the spot market, demand is higher than forecast and this higher demand will likely push prices up, above the price ComEd paid for energy in the 2008 procurement. Demand is lower than forecasted when ComEd is

Making corrections only for the incorrect estimate of the weighted average winning price and the understated capacity price, an estimate of the winning prices in the 2008 RFP would be \$77.78/MWh, which is 22% above the winning price in the 2006 Auction.

With these corrections, much of the AG's additional discussion of relative competitiveness of the 2008 RFP and the 2006 Auction no longer stands. For example, at page 5 the AG claims that "One indication that the 2008 procurement produced a better outcome for consumers can be seen in a comparison of winning bid prices with contemporaneous wholesale market prices." Again we agree with AG's conceptual approach – give Illinois consumers comfort by comparing winning prices to comparable market prices – but we have concerns about the calculations used by the AG to make this comparison.

To see these concerns return to the chart on page 6 of the AG's Initial Comments. As to the 2008 RFP's, we would make the following two points:

- First, the AG uses NYMEX futures prices for block energy, so let us just compare the winning prices in the ComEd 2008 Energy RFP to NYMEX. The winning price was \$67.49/MWh, which is 3.5% higher than the average NYMEX futures price at the time of the RFP weighted to match the products that ComEd solicited. This comparison is legitimate since both the ComEd RFP and NYMEX are for just blocks of energy. (We would suggest adding a risk premium to NYMEX prices; this could justify the 3.5% difference.)

- Second, rather than compare prices for blocks of energy, let us compare something closer to full requirements service. Again, considering only the additional costs for ancillary services and capacity, the winning prices in 2008 were \$77.78/MWh, or about 3% higher than NYMEX prices adjusted in the same way. (Again, the 3% could be justified by a risk premium.)

Now let us turn to the comparison of the winning prices in the 2006 auction to the contemporaneous wholesale market prices. The AG claims that "the 2006 auction clearing-price was approximately 21 percent higher than contemporaneous NYMEX Northern Illinois hub prices on the day of the auction, even after adjustments for capacity and ancillary services."[8] While there is insufficient documentation to know what precisely went into the AG's calculation, it appears to reflect substantial errors. We say this based on the results of our comparison of 2006 auction prices to market prices that we did at the time of the 2006 auction. We have filed these at FERC and they show the winning prices in the 2006 auction for the 17-Month product were 4.2% <u>below</u> the market-based benchmark we calculated at the time.[9] Our benchmark was a detailed construct for a full requirements product; that is, it included, as it must, block energy, dispatchable energy, ancillary services, capacity, and a risk premium.

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selling, which will likely push prices down below the price ComEd paid for energy in the 2008 procurement. Thus it would be buying and selling the energy at a net loss.

[8] AG comments, p. 5-6.

[9] *Affadavit of Craig R. Roach, Ph.D. on behalf on Boston Pacific Company, Inc. as the Auction Monitor for the 2006 Illinois Auction*, June 6, 2007, Docket No. EL07-47-000. Redacted Public Version, p. 9.

We can end on a point of agreement. We do agree with the AG that the 22% increase (or higher) in price between the 2006 Auction and the 2008 RFPs is most likely to be the result of the general rise in energy market prices. Rising energy prices are something the average Illinois consumer has been made all too aware of each time she or he pays to fill up a gas tank or to heat a home.