COMMENTS ON THE 2010 PROCUREMENT PROCESS PURSUANT TO SECTION 16-111.5(o) OF THE PUBLIC UTILITIES ACT

PRESENTED TO

THE ILLINOIS COMMERCE COMMISSION

by

BOSTON PACIFIC COMPANY, INC.

Craig R. Roach, Ph.D.
Miguel Campo
Andrew Gisselquist
Boston Pacific Company, Inc.
1100 New York Avenue, NW, Suite 490 East
Washington, DC 20005
Telephone: (202) 296-5520

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I. INTRODUCTION

Boston Pacific Company, Inc. ("Boston Pacific") appreciates the opportunity to submit these comments in response to the Illinois Commerce Commission's (the "Commission's") request for comments concerning the Spring 2010 Electric Procurement Events.[1]

Boston Pacific served as the procurement monitor for all five of the requests for proposals (RFPs) issued so far by both ComEd and Ameren in 2010. In compliance with the Illinois Power Agency Act's (Public Act 095-0481, hereafter the "Act") requirement, after each Bid Day we provided confidential reports to the Commission that presented the procurement results and assessed bidder behavior and compliance with the procurement processes and rules. In all five cases we recommended that the Commission accept the RFP results.

The bases for our recommendations were as follows. First, each RFP achieved its stated procurement targets. Second, in the context of the Act's requirement to assess bidder behavior, we found no evidence of collusive or otherwise anticompetitive behavior. Third, in the context of the Act's requirement to assess whether the RFPs were run in compliance with the rules, Boston Pacific concluded that these RFPs were run by the procurement administrators in compliance with all Commission-approved rules. We structure our feedback and recommendations around these three areas. We also comment on RFP design and provide a few suggested recommendations in this area.

II. COMMENTS ON RFP RESULTS

The RFPs were successful in that they competitively procured all of the required target quantities. The total value of contracts for the five RFPs was about $830 million, out of which 97% was represented by the Ameren energy and ComEd energy ("Standard Products") RFPs.

The weighted average prices for ComEd's energy RFP for the two service years 2010-2012 were $43.04 for peak and $25.60 for off-peak products. These prices are 4% and 2% higher than those observed in last year's RFPs (2009), respectively. The weighted average prices for Ameren's energy swaps for the same time period were $40.18 for peak and $24.50 for off-peak. These prices are 5% and 7% lower than last year (2009), respectively.

When compared to the results from two year ago (2008), the resulting prices from both energy RFPs are significantly lower. As a reminder, the 2008 RFPs only procured for a single

[1] *Public Notice of Informal Hearing (Request for Comments) Concerning the Spring 2010 Electric Procurement Events Which Were Held On Behalf of Commonwealth Edison Company and the Ameren Illinois Utilities (Ameren-CILCO, Ameren-CIPS, and Ameren-IP),* Issued 5/28/2010.

year and resulted in average weighted prices of $82.48 peak and $45.78 off-peak for ComEd. Similarly, higher prices were seen in the 2008 Ameren's RFP for energy swaps.[2]

Ameren's Capacity RFP resulted in significantly lower prices than in the previous two years. Over the three-year period covered by the RFP the weighted average winning price was $246/MW-month – this reflects an 80% decrease from last year. If we only include the upcoming 12-month service year, average price was $66.18 per MW-month of capacity. This was 93% below the comparable average 2009 price and 95% below the average 2008 price. While the prices fell sharply compared to those from last year's procurement, it is difficult to determine a specific cause for the drop. However, it is generally believed that the recession has cut demand and, thereby, created a surplus of capacity. In addition, expectations about government programs promoting demand response, energy efficiency, and new power plant technologies can influence bidders' views on pricing. There is no simple equation that would allow us to explain this welcome, but somewhat unexpected drop in capacity prices.

Significantly lower prices were also observed for Renewable Energy Credits (RECs) when compared to previous years. The average winning REC price was $4.05 for Ameren and $4.88 for ComEd. This compares to average winning prices last year of $15.86 for Ameren and $19.27 for ComEd. Equally important is the fact that all winning RECs were from Illinois, as they were last year. Furthermore, the great majority of winning RECs were Illinois Wind RECs (91% for Ameren and 80% for ComEd).

Recommendation 1: Ameren and ComEd should report the full cost of providing service

The products procured in these five RFPs, while very important, do not provide the entirety of the full electricity service Illinois ratepayers' need. To fill in the rest of that service, both ComEd and Ameren purchase from other markets products such as dispatchable energy and ancillary services. In order to compare the full cost of providing service from year to year we suggest that at the end of each June through May service year, each utility make easily available via public reports to the Commission the cost of providing this full requirements service. Full disclosure would allow a fair comparison of both electric procurement costs year to year and of potential procurement methods such as block procurement versus full requirements procurement.

Also, the utilities should report how the results of these RFPs impact rates in a manner that is isolated from other rate impact sources. For example, we understand that ComEd asked

[2] Average prices are computed using publicly available information. Due to rounding the actual average prices may be slightly different.

for a significant rate increase this year, but only a small portion of the increase is attributable to the winning contracts from this year's RFPs.

III. COMMENTS ON BIDDER BEHAVIOR

In the context of the Act's requirement to assess bidder behavior, we found no evidence of collusive or otherwise anticompetitive behavior. A fundamental sign of competition is that there were a good number of bidders and winners. The energy RFPs for both utilities had a greater number of winners than last year, with 12 winning parties for Ameren and 12 for ComEd (last year there were 8 and 10 winning parties, respectively). The Capacity RFP resulted in 12 winners, the same as last year. The REC RFPs resulted in 10 winners for ComEd and 6 winners for Ameren (last year there were 18 and 14 winners, respectively). These are fewer winners than observed last year; however, the low winning REC prices are evidence of the competitive nature of the REC RFPs.

Recommendation 2: Starting the RFPs earlier in the year can: a) enhance bidders' experience by providing enough time to meet deadlines for credit and other RFP requirements – this is particularly true for new participants, and b) provide necessary time for the procurement administrators, Staff, IPA and procurement monitors to fully vet and incorporate design enhancements to the RFPs.

For the past two years the Illinois RFPs have been held in an unnecessarily compressed schedule. We say unnecessarily because we see no reason why these procurements do not start shortly after the Commission's approval of the procurement plan. While this year the Commission's Final Order was issued in late December, the procurement administrators were not in place until early March, and the first RFP was issued on March 15. The Act's requirement to conduct RFPs so that contracts are in place by June 1 meant that this year there was only about two and a half months to design, issue and conduct the RFPs. Furthermore, the Act's requirement to conduct a make-up RFP by June 1st under certain circumstances further compressed the schedule to about two months by targeting all RFP completion by mid-May.

From a bidder's perspective this compressed schedule means that less time is given to review the RFPs and Standard Contracts, provide comments to these contracts, obtain necessary internal approvals to bid, and to obtain letters of credits and other necessary requirements to bid in these RFPs.

This year we were able to provide the necessary reviews of contracts, documents, and processes in a short timeframe given that we relied heavily on documents used in the previous two years. To the extent that such documents and processes may, at a future date, require significant changes due to changes in the marketplace or in the needs of Illinois utilities or ratepayers, procurement administers, procurement monitors, Commission Staff, and the Illinois Power Authority will need more time to complete the review and design process. As an example, the most significant process change this year originated from the Commission's requirement to hold a single combined REC event. We discuss later that there was a difference of interpretation by different parties as to what this meant. However, the lack of time due to the compressed schedule was one of the reasons given by the procurement administrators for not being able to implement a single combined REC event this year. We agree that the time was short. As procurement monitors we would have also had to devote a considerable amount of time to further develop the evaluation methodology and to fully vet an evaluation model. Additionally, all parties agreed that given the compressed schedule for procurements, the first priority should be placed on successfully conducting Ameren's RFPs for Capacity and Energy and ComEd's Standard Product RFP.

The delayed schedule this year left about a month, or less, to carry out the entirety of an eventual make-up RFPs by June 1. The Act calls for the procurement administrator, procurement monitor, and Commission Staff to meet no more than 10 days after an ICC decision to analyze potential causes of low supplier interest or causes for the Commission decision to reject the results of the procurement event. While make-up RFPs have not been needed in Illinois since the Act was passed, it is unclear whether the amount of time that was available this year would have been sufficient to be able to announce and hold another bid day before the new service year begins on June 1, if necessary.

Finally, we note that the Commission's Final Order approving this year's procurement plans recognized the importance of having the RFPs start earlier in the year by instructing the IPA to hire procurement administrators and begin conducting the procurement processes early in the year or in December of the previous year.

IV. COMMENTS ON COMPLIANCE WITH THE RULES

In the context of the Act's requirement to assess whether the RFPs were run in compliance with the rules, Boston Pacific concludes that these RFPs were run by the procurement administrators in compliance with all Commission-approved rules including: communication among the procurement administrators, bidders and the utilities; product types solicited; the use of standard contracts; the calculation and use of market-based benchmarks; and procedural requirements such as providing bidders an opportunity to comment on contracts and credit-related documents.

For the REC RFPs there was one area of the Order which was the subject of much discussion, and which according to one possible interpretation would mean that the RFPs were conducted in a manner that is different from what the Order intended. This area was the Order's instruction to conduct a "single short-term REC acquisition event."[3] According to one interpretation of the Order, a single RFP event should be conducted for both utilities in which RECs would be acquired for both utilities. A second interpretation was that the Order instructed the IPA to conduct two separate RFP events, but on a single day. Boston Pacific interpreted the Order as instructing the former, while the IPA and procurement administrators interpreted the Order as instructing the latter. Boston Pacific and ICC Staff ultimately agreed to adopt the IPA and the procurement administrators' recommendation to hold two separate REC RFPs on the same day. As indicated above, the compressed timeframe this year was one of the reasons for arriving at this decision.

Recommendation 3: The ICC should clarify whether next year a single, combined REC RFP should be conducted for both utilities.

The Commission should further define its requirements in next year's procurement plan Order to either a) conduct the REC procurements as two separate RFPs, as they were held this year, or b) conduct a single RFP in which bidders bid RECs that could be selected in either utility's winning pool. The benefits of holding a single combined REC RFP include: a) single registration process for REC bidders b) the need for a single pre-bid letter of credit to participate in the RFP (this year a separate letter of credit was required for each REC RFP), c) further harmonization on standard contracts, d) single procurement administrator, and e) bidders would not have to choose a single utility with which to place bids, the optimal allocation of bids would be automatically determined.

V. COMMENTS ON RFP DESIGN

In an effort to continue to improve the process, this year there were a number of credit related changes made to the Standard Contracts and RFPs with the goal of harmonizing as much as possible the credit requirements across all procurements and further defining certain credit aspects. First, a process description was added to determine collateral thresholds for affiliated companies. Second, provisions were added to allow foreign entities to serve as guarantors for

[3] Illinois Commerce Commission Final Order in docket number 09-0373, December 28, 2009.

ComEd's RFPs. Third, the credit ratings requirements for banks providing letters of credit were made consistent across procurements.

Once it was agreed that separate REC RFPs would be held this year, there was a concerted effort to harmonize the contractual terms and processes as much as possible between Ameren and ComEd. Key areas that were brought closer together include a) setting a common bidder pre-qualification schedule, b) establishing a common REC delivery schedule and payment method, c) having equivalent credit rating requirements for banks issuing letters of credit, d) requiring single REC bids instead of blocks of 5,000 RECs as Ameren required in the past, and e) setting a single bid participation fee that allowed participation in either RFP.

Recommendation 4: Consider allowing annual products for Ameren Energy RFP

This year bidders for the Ameren Energy RFP were given the option to bid for multi-month products in addition to the individual monthly products. Bidders appeared to like this option, as evidenced by the selection of multi-month products in this year's winning pool. For next year, we would advise considering allowing annual products as well. This is currently done for ComEd's Standard Products RFP and has resulted in some bidders winning annual products.

Recommendation 5: For Ameren's Capacity RFP, the Act requires potential Demand Response suppliers to serve "eligible retail customers" which limits the pool of potential bidders to this RFP; within the context of what is allowed by the Act, participation in this RFP should be made less restrictive with the goal of increasing competition.

For the first time, Ameren's Capacity RFP allowed Planning Resource Credits (PRCs) to be provided by both supply-side resources (a power plant) and demand-side resources (demand response such as shutting off an appliance).

In addition to meeting MISO requirements, Demand Response Resources that participated in this RFP must have complied with five requirements that are specified in the Act. These five requirements for Demand Response Resources are the following: (a) "be procured by a demand-response provider from eligible retail customers"; (b) "at least satisfy the demand-response requirements of the regional transmission organization market in which the utility's service territory is located, including, but not limited to, any applicable capacity or dispatch requirements"; (c) "provide for customers' participation in the stream of benefits produced by the demand-response products"; (d) "provide for reimbursement by the demand-response provider of the utility for any costs incurred as a result of the failure of the supplier to perform its obligations thereunder"; and (e) "meet the same credit requirements as apply to suppliers of capacity, in the applicable regional transmission organization market."[4]

The most restrictive of these five is that a bid must be from a demand-response provider serving eligible retail customers – this leaves out other retail customers and some of the larger industrial customers, with high potential to offer such demand response, who are served by third-party suppliers. Within the context of what is allowed by the Act, participation in this RFP should be made less restrictive with the goal of increasing competition.

Recommendation 6: The IPA should address in its procurement plan for next year the implication, if any, of proposed Congressional financial regulatory legislation on derivatives.

Concern has been raised that proposed congressional legislation might limit the use of derivatives by non-bank entities. We understand derivatives are used for financial hedging by bidders in the Illinois RFPs and that Ameren's energy swap product might itself be viewed as a derivative. If this type of legislation is passed, the IPA should assess the implications that it could have on bidder participation and product design for next year.

VI. OTHER

Finally, please note that comments on the RFP for long-term PPAs to procure renewable resources process, which is new this year, are being withheld until the conclusion of that process. Currently, the IPA has provided little information about when this process will be held. We expect that the process of designing Standard Contracts and RFP rules for these procurements will be time consuming. A prompt start to the long-term renewable resources procurement would help complete that procurement prior to the start of procurements for 2011.

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[4] Illinois Power Agency Act at 16-111.5(b)(3)(ii)