FERC Decision Creates Capacity Choice

PJM capacity prices have been on the decline, but a recent FERC order may strengthen the trend. What lies ahead may be an opportunity for customers to accept some market-based risk and opt for pass-through structures.

A Little History

For more than a decade, a Reliability Pricing Model (RPM) has allowed for three-year forward visibility into capacity prices to encourage the building of new generation based on clearing prices. In response to the 2014/2015 Polar Vortex, PJM implemented an enhanced model that allows capacity providers to sell at a higher price based on increased investments in fuel availability, deliverability, or maintenance to ensure reliability.

Current Events

On September 2, 2021, FERC ordered PJM to change its Capacity Market Seller Offer Cap or “ceiling price.” FERC prescribes using a Net Avoidable Cost Rate as a cap, which could result in dramatically lower capacity offer values. The default for existing Wind, Solar, and Combined Cycle natural gas generation is set at \$0.00/MW-day. Natural gas combustion turbines are capped below \$23/MW-day, and dual unit Nuclear at less than \$50/MW-day. The 2022/2023 delivery year PJM capacity auction clearing price for most of the PJM footprint fell to \$50/MW-day, down from \$140/MW-day for the unconstrained RTO in the delivery year 2021/2022 capacity auction.

Future

PJM intends to request a delay in the upcoming 2023/2024 capacity auction currently scheduled for December 2021 to late January 2022. It also plans to request two-month delays in each subsequent capacity auction. We expect market participants, including capacity providers and PJM itself to request a rehearing at FERC, propose modifications, or pursue legal action in Federal Courts. Each one is a potentially lengthy process. At this point, it seems these new rules will apply to the 2023/2024 delivery year. It's uncertain whether changes will be pursued and adopted before the next capacity auction for the delivery year 2024/2025.

Successful management of price risk can be a balancing act. In some cases, accepting some market-based risk may be the better option.

Taking Action

A capacity pass-through structure can be a win for both the customer and supplier. Customers eliminate the supplier premiums. Customers only pay what is owed with no variance due to changes in consumption. Your ENGIE Business Development contact has the tools and expertise to explain capacity rates for your organization