

**STATE OF NEW JERSEY  
BOARD OF PUBLIC UTILITIES**

IN THE MATTER OF THE BOARD'S	)	
INVESTIGATION OF CAPACITY	)	
PROCUREMENT AND TRANSMISSION	)	BPU DOCKET NO. EO11050309
PLANNING	)	

**COMMENTS OF GERDAU AMERISTEEL US INC.**

COMES NOW, Gerdau Ameristeel US Inc. ("Gerdau") and submits these Comments in the above-referenced proceeding. These Comments are in response to the New Jersey Board of Public Utilities' ("Board" or "BPU") Order Initiating Proceeding, dated May 16, 2011 ("Order"), which established, *inter alia*, procedures for evaluating supply adequacy and deliverability within New Jersey, the competitiveness of New Jersey's power market, and whether New Jersey should pursue additional resources beyond the 2,000 MWs of generation procured under the Long-term Capacity Agreement Pilot Program ("LCAPP"). Inherent in the questions posed by the Order is the issue of who pays for any of these initiatives and how. Gerdau's Comments focus on that issue, and adhere to the position that the costs of LCAPP and any costs incurred beyond LCAPP must be allocated to and recovered from each customer based on the customer's contribution to the need for the additional investment. Because the additional investment is driven by perceived needs for additional capacity and because the costs to be recovered are the differences between a project's actual capacity costs and the capacity revenue they derive from the Reliability Pricing Model ("RPM") auctions, the costs of the investment should be recovered from customer's based on each customer's capacity obligation.

Gerdau recognizes that the current capacity construct in the PJM region has not addressed the chronic lack of investment in transmission and supply resources in certain load pockets in New Jersey, leading to chronically high prices in those areas. LCAPP is one approach to addressing this shortcoming of the PJM market design, but whether the LCAPP approach will benefit an energy-intensive and globally competitive customer such as Gerdau depends critically on the details of how the costs to support these initiatives are collected from ratepayers. To that end, and for the many reasons discussed below, Gerdau respectfully requests that the Board find and conclude, in any order issued as an outgrowth of this investigative proceeding, that any non-bypassable charge to recover LCAPP costs and any incremental, state-mandated investment will be assessed to customers based on the customers' Peak Load Contributions ("PLC"), which is the basis for assessment of other transmission and capacity-related charges. Not only would this approach ensure that the design of the LCAPP charge aligns with traditional ratemaking principles, it would also ensure that customers are receiving the appropriate price signals to manage peak demands and help ease the State's concerns about supply and transmission adequacy.

## **I. BRIEF BACKGROUND**

On January 28, 2011, in P.L. 2011, c.9, Governor Christie signed into law a statute that has come to be known as the LCAPP, to foster an increase in electric generation in New Jersey. LCAPP is intended to address the lack of long-term, capacity-based revenue stability available from the RPM auctions. The purpose of RPM is to provide incentives to generators to provide adequate capacity in the PJM footprint, including New Jersey.

The LCAPP statute directs the Board to establish a process to solicit offers for Standard-Offer Capacity Agreements ("SOCAs") between the state's EDCs and "eligible generators." In

turn, the Board must approve the SOCAs, which will reflect negotiated Standard-Offer Capacity Prices ("SOCPs"), and the generators will participate in and be accepted in PJM's annual Base Residual Auction ("BRA") held each May.

Inevitably, and as the law contemplates, when Board-approved SOCAs or other resources procured by the State participate in the PJM BRA, there will be a difference between the SOCPs and the Resource Clearing Price ("RCP"). The RCP is the clearing price established in each auction and cannot be forecasted with precision. In RPM, different RCPs may be established for resources in each of PJM's Locational Deliverability Areas ("LDAs"). The LCAPP law demands that New Jersey ratepayers incur the cost of, or receive the credit for, any difference between the SOCPs and the RCP. The Board is tasked with establishing a method for providing payments to the eligible generators (if the SOCP is higher than the RCP) or credits to customers (if the RCP is greater than the SOCP). The LCAPP law requires that the charge be assessed on a nonbypassable basis. However, the LCAPP law does not specify whether the charge should be recovered on a demand basis, an energy basis, or some combination of the two.

Pursuant to the PJM Open Access Transmission Tariff ("Tariff") and Reliability Assurance Agreement ("RAA"), RPM costs are recovered on the basis of each customer's PLC for each Delivery Year. Each customer's capacity obligation depends on the demand that the customer is placing on the PJM system during the five hours each year when the system is experiencing its peak loads for the year. It bears mentioning that LCAPP and the Board's current investigation are aimed at supplementing RPM to ensure adequate capacity and transmission for New Jersey's electricity consumers. As such, the Board should establish a method for recovering costs from customers using the same approach that PJM uses to assess capacity costs.

## II. COMMENTS

### A. **The Electric Distribution Companies In New Jersey Already Calculate Customer's Peak Demands For Purposes Of Allocating Capacity Costs.**

Gerdau appreciates the opportunity to offer these Comments to the Board and respectfully urges the Board to establish clearly, as part of this investigation, that recovery of the LCAPP investment and any additional investment required by the State will follow the demand-based capacity pricing methodology adopted by PJM, and approved by the Federal Energy Regulatory Commission ("FERC"). As the Board is generally aware, there are two primary methods for pricing a consumer's use of electricity—energy and capacity (the latter also referred to as "demand"). While the price of electricity is almost always based on a customer's "use," the reality is that "use" can mean different things in different contexts, and it is important to understand the type of "use" in order to determine the appropriate method for pricing.

Capacity is priced in PJM based on customers' use during the relevant peak periods, because customers' use during peak periods determines how much capacity is needed and, thus, aligns cost responsibility for capacity with the behavior that drives the cost of the capacity. In PJM, the capacity pricing methodology is relatively straightforward. In each zone in PJM, each load-serving entity ("LSE") is assigned a Locational Deliverability Area Reliability Requirement and "is obligated to pay a Locational Reliability Charge for each Zone in which it serves load based on the Daily Unforced Capacity Obligation of its loads in such zone."<sup>1</sup> As specified in the PJM Reliability Assurance Agreement:

Except to the extent its capacity obligations are satisfied through the FRR Alternative, each Party shall pay, as to the loads it serves in each Zone during a Delivery Year, a Locational Reliability Charge for each such Zone during such Delivery Year. The Locational Reliability Charge shall equal such Party's Daily Unforced Capacity Obligation in a Zone, as determined pursuant to Schedule 8 of

---

<sup>1</sup> PJM Open Access Transmission Tariff,, Attachment DD, Section 5.14(e). LDA

this Agreement, times the Final Zonal Capacity Price for such Zone, as determined pursuant to Attachment DD of the PJM Tariff.<sup>2</sup>

Schedule 8 of the RAA sets forth the requirements for determining Daily Unforced Capacity Obligation, in relevant part, as follows:

For each billing month during a Delivery Year, the Daily Unforced Capacity Obligation of a Party that has not elected the FRR Alternative for such Delivery Year shall be determined on a daily basis for each Zone as follows:

Daily Unforced Capacity Obligation = OPL x Final Zonal RPM Scaling Factor x FPR

Where:

OPL = Obligation Peak Load, defined as the daily summation of the weather-adjusted coincident summer peak, last preceding the Delivery Year, of the end-users in such Zone (net of operating Behind The Meter Generation, but not to be less than zero) for which such Party was responsible on that billing day, as determined in accordance with the procedures set forth in the PJM Manuals

Final Zonal RPM Scaling Factor = the factor determined as set forth in sections B and C of this Schedule

FPR = the Forecast Pool Requirement.<sup>3</sup>

Schedule 8 also describes the steps that must be taken by Jersey Central Power & Light Company ("JCPL") and other electric distribution companies ("EDCs") to calculate a capacity obligation for each retail customer:

D. 1. No later than five months prior to the start of each Delivery Year, the Electric Distributor for a Zone shall allocate the most recent Weather Normalized Summer Peak for such Zone to determine the Obligation Peak Load for each end-use customer within such Zone.

2. During the Delivery Year, no later than 36 hours prior to the start of each operating day, the Electric Distributor shall provide to PJM for each Party to this Agreement serving load in such Electric Distributor's Zone the Obligation Peak Load for all end-use customers served by such Party in such Zone. The daily Unforced Capacity Obligation of a Party for such Operating Day shall not be subject to change thereafter.<sup>4</sup>

---

<sup>2</sup> Reliability Assurance Agreement Among Load-Serving Entities, Section 7.2 (emphasis added).

<sup>3</sup> RAA, Schedule 8, Section A.

<sup>4</sup> *Id.*, Section D.

Certain rules in Attachment M-2 of the PJM Tariff show the precise methodology used by JCPL, for example, to determine a customer's allocation of costs for RPM. Rules 7-13 of the Energy Procedure Manual for Determining Supplier Peak Load Share state this calculation as follows:<sup>5</sup>

RULE 7: The LDC Zonal capacity allocation determined by PJM is based on the various zonal loads at the time of the five PJM Pool peak hours. The method used by PJM includes, but is not Limited to weather normalization, unrestricted loads (i.e., add-backs, such as curtailed loads), historical smoothing (regression analysis), seasonal smoothing (i.e., 5 CPs) and zonal loads at the system (or Interchange) level (i.e., includes losses). Furthermore, PJM Business Rules include requirements related to customer peak load tickets, such as those promulgated under Demand Response and Behind the Meter. In calculating customer peak load tickets, the Company shall include load components reflective of the zonal allocation method and business rules currently in effect by PJM.

RULE 8: The basic framework for performing the annual customer peak load allocation (tickets) requires using available customer data. Such customer data varies by meter type, consequently different algorithms are required to calculate the customer peak load tickets for the various meter types. The Company will use the usage data, which in the Company's judgment most closely reflects the customer actual usage at the time of the peak hours.

RULE 9: Actual metered loads for (hourly) interval-metered customers are adjusted to include any load curtailed as a result of Active Load Management (ALM) events. The adjusted loads are referred to as "unrestricted loads".

RULE 10: Not all customers have hourly usage metering, therefore the customer allocation process will necessarily require using load profiles.

RULE 11: The Company will ensure that the sum of the peak load tickets corresponding to the customers active on each of the five peak days used in the calculation will average to equal the LDC's zonal allocation.

RULE 12: The Company will adjust each customer's loads for losses consistent with the most recent state commission filing of loss factors by voltage classes.

RULE 13: Within the Zone there can and do exist "load zones" (i.e., municipalities, cooperatives, etc.) which may or may not be directly PJM Suppliers. These load-zones will have their aggregate customer peak load tickets determined consistent with the methodology used for all customers, unless a) an alternate methodology is agreed to by the Company, the Supplier and PJM, or b) PJM directs the Company to follow a different methodology as a matter of PJM requirements.

---

<sup>5</sup> PJM Tariff, Attachment M-2 (page 1964 of 2755 of full Tariff, found at <http://www.pjm.com/markets-and-operations/~media/documents/agreements/tariff.ashx>).

Thus, the 5CP approach measures a customer's usage during the five times throughout the year when the most electricity is being consumed on the PJM system. A customer's RPM-related capacity charge is determined based on the customer's usage during those system peak periods. Moreover, as demonstrated by the provisions quoted above, JCPL and other New Jersey EDCs already have in place the processes necessary to use a PLC approach for allocating LCAPP costs and other State-directed, capacity-related investments.

**B. The Board Has The Authority And The Obligation To Allocate These Capacity-Related Costs On The Basis Of Each Customer's PLC.**

The Board has both the authority and obligation to set "just and reasonable rates."<sup>6</sup> In exercising this authority, the Board must "ensure" that "no cross-subsidization exists between or among classes of customers."<sup>7</sup> In addition to ensuring that no customers bear cost burdens unrelated to their use of the system, the Board must also reach an outcome that achieves an appropriate balance among competing interests, including those of customers and the utilities.<sup>8</sup> Even though the Board enjoys broad discretion in the conduct of its proceedings, all Board orders must be supported with adequate evidence.<sup>9</sup> The evidence amassed in this investigation, and the plainly stated objectives of the LCAPP statute and the well-accepted methods for recovering PJM capacity costs, compel the Board to apply capacity pricing principles in setting the non-bypassable charge. The Board would be exceeding the bounds of its discretion to apply the non-bypassable charge on any other basis.

The LCAPP law is a law about capacity. The statute unambiguously refers to "capacity" repeatedly throughout its text. In fact, the word "capacity" is used forty-three times, including:

---

<sup>6</sup> N.J.S.A. 48:2-21; *Bergen Cty. v. Bd. of Pub. Util. Comm'rs*, 349 A.2d 537, 450 (N.J. Super. 1975).

<sup>7</sup> N.J.S.A. 48:2-24.

<sup>8</sup> *Application of Rockland Elec. Co.*, 555 A.2d 1140, 1149 (N.J. Super. 1989).

<sup>9</sup> *In re New Jersey Power & Light Co.*, 89 A.2d 26, 31 (N.J. 1952)(citing *Central R. Co. of N.J. v. Dept. of Pub. Util.*, 81 A.2d 162 (N.J. 1951)).

(1) in the very title of the law; (2) in discussing RPM, which the law refers to as the "ineffective capacity procurement mechanism," and in seeking to cure New Jersey's "capacity deficiencies";<sup>10</sup> (3) in referencing New Jersey's "capacity deficit";<sup>11</sup> (4) in stating the purpose of the law, which is to help "ensure sufficient capacity resources";<sup>12</sup> (5) in referring to RPM as the "capacity-marketing model...that secures capacity on behalf of load-serving entities;"<sup>13</sup> (6) in definitions and descriptions of both the SOCA and SOCP;<sup>14</sup> and (7) in describing the obligations of EDCs to procure 2,000 MW worth of SOCAs from eligible generators of "new generation capacity."<sup>15</sup> Basing a pricing methodology on anything but capacity-pricing principles would subvert the clear intent of the law and undercut many of the justifications for the legislation itself. Consistent with the clear capacity-related objectives of the law and the law's ties to RPM, the Board should conclude that the non-bypassable LCAPP charge, and any other non-bypassable charges established to cover differences relative to RPM auction-clearing prices, must be assessed on the basis of customers' PLCs.

In addition, there are practical reasons to base capacity-related non-bypassable charges on capacity-pricing principles. Consider, for example, that the credits or payments mandated by the statute refer to the difference between the RCP (in PJM's RPM) and the SOCP. Because the PJM RCP price is based on capacity-pricing/demand-based principles, it would be inconsistent to base the credits/payments to State-procured resources on anything but the same principles and methodology. Basing this charge or refund amount on the amount of energy consumption, for example, would cause some New Jersey consumers to over-fund capacity availability and cause

---

<sup>10</sup> LCAPP § 1(b).

<sup>11</sup> *Id.* at § 1(e).

<sup>12</sup> *Id.* at 1(i).

<sup>13</sup> *Id.* at s. 3.

<sup>14</sup> *Id.*

<sup>15</sup> *Id.* at s. 3(c)(1).

others to under-fund their portion of the same costs. Basing the charge or refund amount on a capacity basis (e.g., on the basis of each customer's PLC) would, by contrast, equilibrate the non-bypassable charge with the way in which PJM-related capacity costs are recovered from customers. Therefore, for simple reasons of fairness and consistency with current practice, it behooves the Board to ensure that capacity procured in the LCAPP or through other State-mandated procurement processes is priced in the same way that PJM prices its RPM capacity payments.

Furthermore, straying from capacity pricing methodologies would violate basic fairness principles in other ways. As noted throughout these Comments, the stated intent of the LCAPP law is to ensure that the state's electricity consumers have *access* and *availability* to adequate capacity that might otherwise not be provided as a result of PJM's RPM auctions. The LCAPP law also implies that there is currently enough power, but that the available power is over-priced because not enough capacity exists in the market. By introducing more capacity, clearing prices in the RPM auctions should stabilize and decrease, thereby benefitting all consumers based on their capacity obligations.

Charging for capacity on a volumetric basis mutes the price signal for demand response. Charging for capacity on a PLC basis, by contrast, allows some consumers, to reduce usage in times when system-wide usage is high (i.e., peak periods). These consumers base their business models around not contributing to system peak periods—and, thus, not paying peak prices—and do not contribute to the stress and availability issues that capacity pricing seeks to address. Therefore, it would be unfair to punish "peak-conscious" customers by imposing peak-related costs on a basis other than well-accepted capacity pricing principles.

The potential acquisition of additional capacity (beyond the amounts procured under the LCAPP) does not alter this basic rationale. Any BPU effort to obtain additional supply or transmission resources will likely be rooted in some form of determination that insufficient capacity (whether supply or transmission) exists in New Jersey to meet customers' needs reliably and cost-effectively. Because any extension of the LCAPP efforts taken to date would necessarily revolve around the dearth of capacity in the existing system, it seems only logical that any costs for additional capacity will be recovered from all customers based on the customer's contribution to the need for that additional capacity.

**C. Allocating Capacity Costs On The Basis Of Energy Consumption Is Inappropriate.**

Some parties have taken the position that LCAPP and other capacity costs should be recovered from New Jersey ratepayers on the basis of energy consumption. The New Jersey EDCs generally support this approach as a matter of administrative convenience. New Jersey Rate Counsel contends that recovering capacity costs on an energy basis is defensible because the new units that are being supported by New Jersey ratepayers will produce energy that will be consumed by most customers at some point. Both arguments fail upon closer scrutiny.

First, recovering capacity-related charges on an energy basis is not necessarily more administratively convenient than recovering capacity-related charges on a capacity basis. As discussed above, each EDC in New Jersey is already obligated, under the PJM RAA, to calculate PLCs for each customer on the system. These PLCs are in the EDCs' systems, and are used daily to determine load-serving entities' responsibility for other capacity-related and transmission charges. For customers with interval meters, the PLC is specific to the customer, based on the customer's actual consumption during the relevant peak periods. For customers that do not have interval meters, the PLCs are calculated based on profiled loads for the class. In each case, a

PLC is calculated for each customer. Consequently, each EDC has on its system a PLC that could be used as a billing determinant for recovery of LCAPP and other capacity-related costs.

Second, any contention that capacity-related costs should be recovered on an energy basis, because the capacity produces energy, misses the point. The LCAPP charge and, ostensibly, any similar non-bypassable capacity-related charge, are intended to completely hedge the new resource against any risk of not recovering its capacity cost through the RPM auctions. For example, if a resource's capacity cost is \$200/MW-day for a Delivery Year, and the Base Residual Auction clears at \$180/MW-day for that Delivery Year, New Jersey ratepayers are obligated to pay the \$20/MW-day differential. Customers also pay, separately, for any energy that is produced by the resource. For example, if a customer with an LMP-based contract is consuming during the hours in which the LCAPP resource is generating and selling electricity, that customer will be paying the resource for energy by paying the LMP. Imposing capacity-related costs on customers via an energy charge places the costs in the wrong cost recovery bucket. Capacity-related costs must be recovered on the basis of a customer's capacity-related billing determinant (i.e., the customer's PLC). Likewise, energy-related costs must be recovered on the basis of the customer's energy-related billing determinant (i.e., the customer's kilowatt-hour usage during the relevant hours). Aligning capacity-related costs with capacity-related charges, and energy-related costs with energy-related charges, sends the correct and optimal price signals to customers. Conversely, crisscrossing costs and charges (e.g., by allocating capacity-related costs on an energy basis) subverts price signals to consume efficiently. Arguments that LCAPP and other capacity-related charges should be recovered on an energy basis must be rejected.

**D. Structuring The Nonbypassable Charge Correctly Is Extremely Important To Gerdau And Other Customers That Respond To Price Signals By Actively Managing Their Peak Load Contributions.**

By way of background and as the Board is aware, Gerdau operates a steelmaking facility in Sayreville, New Jersey. Over the past several years, Gerdau has undertaken detailed and comprehensive measures at the plant to minimize its demands during the 5CP hours, in order to minimize Gerdau's exposure to capacity and transmission charges. Gerdau's ability to reduce its 5CP loads provides significant value to other New Jersey ratepayers by reducing the need for capacity in New Jersey and, thus, reducing the cost of capacity.<sup>16</sup> Allocating capacity-related costs on a basis other than 5CP loads would mute the price signals that are producing this value.

The proper rate design for the LCAPP non-bypassable charge (and any charge developed to recover investment incremental to LCAPP) is critically important to Gerdau. As the Board is well aware, Gerdau has been an outspoken advocate of properly allocating costs and designing rates to ensure that cost responsibility follows directly from cost-causation. In the case of the LCAPP charge and any charges that eventually result from this investigation, there is a clear and undeniable link between the non-bypassable charge and the PJM capacity charges that would otherwise apply. The charges resulting from New Jersey requirements will be, in essence, a direct substitute for PJM capacity charges that would otherwise apply and, for that reason alone, the charges should be developed to apply on the basis of PLC.

This issue also carries important economic development implications. Gerdau's Sayreville facility has invested time and resources to effectively manage its peak load contributions and, thus, reduce its capacity costs. The difference between recovering non-

---

<sup>16</sup> Gerdau notes the Market Monitor's estimates that 2,000 MWs of new generation bidding at \$0/MW-day would reduce RPM revenues of New Jersey suppliers by approximately \$560 million/year. Proportionally, a 50 MW reduction in demand would equate to approximately a \$14 million/year reduction in RPM costs to New Jersey ratepayers.

bypassable charges on an energy basis versus a capacity basis could represent a significant and material cost differential for Gerdau if the SOCP substantially exceeds the RCP.

Consider the difference between adopting an approach that bases the non-bypassable charge/credit on energy (megawatt-hours) and an approach that bases the non-bypassable charge/credit on PLC (megawatts). For example, the estimated energy usage for the JCPL zone in PJM was 24,045 GWh,<sup>17</sup> while the annual peak load was 6,310 MW in 2009.<sup>18</sup> Assume further that a hypothetical industrial customer effectively manages its load during the peak periods and substantially reduces its PLC while still consuming substantial amounts of energy during non-peak hours. Assume further that the SOCP exceeds the RCP by \$100/MW-day for the 2,000 MWs, and that the JCPL zone's share of the total EDC cost is approximately 32%. If the non-bypassable charge is assessed on the basis of energy consumption, the hypothetical industrial customer would incur non-bypassable charges that are more than 17 times the level of non-bypassable charges the customer would incur if the charge were assessed on the basis of PLCs. Whether the non-bypassable charge is implemented on an energy or PLC basis matters, and it matters quite a bit, to energy-intensive manufacturers that effectively manage their PLCs.

Establishing any capacity-related non-bypassable charge on the basis of each customer's PLC aligns precisely with the objectives of the LCAPP law and would align with any further directives that stem from this investigation, is well-grounded in fundamental ratemaking principles, provides an equitable approach to recovering costs from customers, and avoids penalizing customers that have undertaken a concerted effort to avoid consumption during

---

<sup>17</sup> PJM Load Forecast Report (January 2010) found at: <http://pjm.com/faqs/~media/CEDC88A734AC4719ADB11AF1CBC8034D.ashx>

<sup>18</sup> *Id.* at Table B-1.

system peak periods. Gerdau respectfully urges the Board to find and conclude that any capacity-related non-bypassable charge must be assessed on the basis of each customer's PLC.

### **III. CONCLUSION**

Gerdau sincerely appreciates this opportunity to provide Comments to the Board regarding the critical issue of how to structure capacity-related non-bypassable charges. For the reasons set forth above, Gerdau urges that the Commission find that all capacity-related charges or credits, including LCAPP charges or credits, should be assessed based on the basis of each customer's capacity obligation, consistent with the approach used for the recovery of all other capacity-related costs.

Respectfully submitted,

Gerdau Ameristeel US Inc.

/s/ David Forsyth

---

David Forsyth  
Regional Energy Manager