UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

PJM Interconnection, L.L.C.	)))	Docket No. ER15-623-000

COMMENTS OF THE ORGANIZATION OF PJM STATES, INC.

The Organization of PJM States, Inc. ("OPSI")[1] hereby files with the Federal Energy Regulatory Commission ("Commission") comments regarding the proposal of PJM Interconnection, L.L.C. ("PJM") to modify substantially the Reliability Pricing Model ("RPM") and related rules in the PJM Open Access Transmission Tariff and the Reliability Assurance Agreement Among Load Serving Entities ("RAA"). PJM has requested an effective date of April 1, 2015, for its proposed revisions.

I. Executive Summary

PJM has proposed extensive and complex changes to RPM that could substantially raise prices to end-users. These proposed amendments arise following a heretofore unused and highly accelerated evaluation process. The proposal currently before the

[1] These comments are supported by the following OPSI members: Delaware, District of Columbia, Illinois, Indiana, Kentucky, Maryland, Michigan, New Jersey, North Carolina, Tennessee, Virginia and West Virginia. Pennsylvania abstained. Ohio abstained from the request for a hearing but supports retention of the 2.5% holdback.

Commission was never presented to stakeholders for review and comment. As a result, sufficient data have not been provided to permit OPSI members and other stakeholders to develop adequately informed positions as to the need for, benefits to load or effectiveness in protecting reliability of, these revisions to RPM. These complex revisions require the scrutiny that can only be afforded by an evidentiary hearing. OPSI believes that many of PJM's more aggressive market redesign proposals should not be considered for adoption until after the implementation of several other near-term programs this winter and the evaluation of their operation has been completed.

As PJM has advised OPSI members, these near term initiatives – gas/electric system coordination, gas generating unit commitment practice changes, weatherization and testing of certain generation, targeted winter auctions and other steps – along with existing RPM incentives for new generation development, may prove sufficient to resolve current reliability and operability concerns. Market rule changes that impose large pricing burdens on end-users, and that present the potential of unintended results and risks for all market participants, should not be adopted if more focused and limited actions will resolve realistic reliability and operational concerns. RPM is intended to send long-term price signals to resources. Deferring action on changes to these long-term price signals is warranted until PJM can provide stakeholders proper analyses of the effects of such changes and a sufficient time to fully evaluate those analyses to consider the implications on state retail market designs, business plans and other issues.

II. The Significant Proposed Revisions to RPM Should be Implemented Only if an Evidentiary Hearing Supports Them

PJM has met its obligation to procure sufficient capacity to meet the reliability needs of its customers. PJM conducts a capacity auction for generation three years in advance of the delivery year. For the 2015-2016 Delivery Year, PJM has procured 164,561 megawatts ("MW") of capacity at a cost of $9.7 billion.[2] This amount of capacity exceeded PJM's reliability requirement by 5,855 MW. For the 2017-2018 Delivery Year, PJM has procured 167,003 MW of capacity at a cost of $7.5 billion.[3] This amount was 6,187 MW in excess of the reliability requirement.

The events of the winter of 2014 have caused PJM to rush to judgment on changes to RPM without the analysis and study that should accompany reforms of the magnitude proposed. The reliability and operational concerns that PJM seeks to address were identified in a whitepaper entitled "Problem Statement on PJM Capacity Performance Definition", released August 1, 2014. This whitepaper was followed by PJM's initial Capacity Performance ("CP") Proposal released on August 20, 2014. After receiving stakeholder comment for 28 days, PJM released its "PJM Capacity Performance Updated Proposal" on October 7, 2014. This revised proposal was issued before PJM responded to action items on its initial proposal.[4] PJM then utilized what it called an "Enhanced Liaison Committee" process which bypassed the ongoing stakeholder process, and only allowed comments to PJM's Board at a meeting on November 4, 2014. The revisions to

[2] Monitoring Analytics, Analysis of the 2015-2016 RPM Base Residual Auction, at p. 5 (Sep. 24, 2014).

[3] Monitoring Analytics, Analysis of the 2017-2018 RPM Base Residual Auction, at p. 5 (Oct. 6, 2014).

[4] For example, in response to a stakeholder data request that PJM "demonstrate how the solutions will solve the stated problems", PJM had responded as of October 17, 2014: "Further cost analysis will be provided after the Final Whitepaper is posted (the analysis may not address all aspects of this action item)." (Action Item 88, Schedule 126). In response to similar stakeholder requests 89 through 92 (Schedules 127-130): "PJM staff and Monitoring Analytics should provide a cost impact analysis and conduct a review session on that analysis to better enable market stakeholders to understand the potential implications of any rule changes".

RPM were then approved by the Board and filed with the Commission on December 12, 2014.

At each step of the process, PJM has made substantial changes to the CP proposal without documenting the cost impacts on end-users or fully addressing the proposal's impacts on markets. In its December 12, 2014 filing, PJM identifies 11 key changes to RPM as follows:

> 1. A new capacity product—the Capacity Performance Resource—that provides greater assurance of delivery of energy and reserves during emergency conditions;
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> 2. A redefined capacity product—the Base Capacity Resource—that is essentially the existing capacity product but with enhanced assurance of delivery of energy and reserves during hot weather operations;
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> 3. Virtually eliminating the current excuses for Capacity Resource non-performance, leaving only certain narrowly drawn exceptions for actions specifically approved or directed by PJM;
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> 4. Charges assessed for poor performance (subject to a reasonable "stop-loss" provision), and credits given for superior performance, patterned closely on provisions recently approved for ISO–New England, Inc., to provide a strong incentive for performance;
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> 5. Capacity sell offer rule changes that recognize the costs and risks of offering Capacity Performance Resources by increasing the offer-price cap for such resources to the Net Cost of New Entry, while also allowing offers in excess of the Net Cost of New Entry if the seller can demonstrate that the costs of improving resource performance, including firm fuel costs and documented and verifiable expenses solely attributable to the risks of offering Capacity Performance Resources exceed that value;
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> 6. A distinct "must-offer" requirement specifically for resources capable of qualifying as Capacity Performance Resources, to prevent physical withholding of such resources;
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> 7. Conforming changes to Load Serving Entity capacity obligations, to reflect the reliability value added by resource performance during winter-season emergencies;

8. Preservation of existing capacity products through May 31, 2020, subject to a reliability-based cap on the quantity of such products that may clear the capacity auctions, to allow market participants time to adapt their resources as necessary to ensure satisfaction of the region's expectation that all committed capacity will deliver energy and reserves during emergencies;

9. An allowance for differential price clearing during that transition, to recognize the higher value of Capacity Performance Resources;

10. Elimination of the current market rule that intentionally understates the region's reliability needs in the RPM Base Residual Auction, to eliminate a possible source of underpricing of any resources (including Capacity Performance Resources) in that auction; and

11. Conforming changes to various capacity rules, including the RPM credit requirements (to reflect increased credit exposure from the new Non-Performance Charge) and the Fixed Resource Requirement alternative to RPM (to establish equivalent requirements and incentives for resource performance).[5]

PJM identified eight changes to the October 7, 2014 proposal that were incorporated into its December filing and therefore never discussed with stakeholders:[6]

1. Requirement and performance payment structure. This includes the concept that penalties collected from under-performing resources will be allocated to over-performing generators. The concept is described as an added incentive for energy-only resources to perform during emergency conditions, viewed as an opportunity for intermittent and non-capacity resources.

2. Adoption of a "no excuses" approach to performance requirements, except for retaining an exemption for resources following PJM scheduling and dispatch instructions.

3. Narrowing of the 2015 procurement for reliability and reduction of the quantity of transitional CP procurement in the transition auctions for 2016/17 and 2017/18 to 60% and 70% of requirement, respectively.

[5] PJM's Transmittal Letter at 2-3.
[5] See December 3, 2014 letter of Terry Boston to PJM Members Committee.

4. Expansion of the applicability of coupled resource offers to allow more flexibility for intermittent resources.

5. Elimination of the multi-year pricing mechanism.

6. Modified cost allocation for capacity performance to include all compliance hours.

7. Maintaining demand response as a supply-side resource with the DR product adapted to be a peak shaving commitment which conforms to the CP approach.[7]

8. Implementation of an adjustment to the forward load forecast to recognize the observed reduction in correlation with economic indicators.[8]

These are substantial and potentially interacting changes to the RPM. The public policy implications of each change and the resulting impacts on markets and end-user costs need to be more thoroughly evaluated *prior to* implementation. To better quantify the impact of the proposal on customers' rates, and on system operations and grid reliability, however, requires the development, presentation and evaluation of data that have not yet been provided by PJM.

As an example, PJM has not provided estimates of the extent to which existing generation will need, or be able, to make large capital investments to comply with the new requirements, or if existing generation is already able to comply without such investments.[9] Also PJM has not, to OPSI's understanding, yet provided persuasive data that such major expenditures are actually needed to assure reliability of service. This

[7] PJM notes that Capacity Performance will function with DR on either the supply or the demand side, and that the issues raised in *Electric Power Supply Ass'n v. FERC,* 753 F.3d 216 (D.C. Cir. 2014), are "separable" from this initiative, and that the uncertainties surrounding DR in wholesale markets will be addressed in a separate proceeding.

[8] This is related to PJMs proposed elimination of the short-term resource procurement target (i.e., the 2.5% holdback).

[9] See PJM Capacity Performance Action Items (Updated as of October 17, 2104) ,stakeholder request 74, Slide 112.

data is essential to understanding both the level of potential market power that could be created by the new dual product market and the extent of need for the proposed major and costly incentives for additional investment built into the CP Proposal's new market design.

PJM has also not provided definitive data on the price increase effect of its CP program. Very late in the process held on the proposal, PJM released its CP Initiative, a joint analysis performed in association with the PJM Market Monitor. This document indicates an expected Capacity Performance Program cost during the four year 2015/2016 to 2018/2019 period of between $300 million and $6 billion, with a continuing annual cost thereafter of $300 to $700 million per year.[10] These costs, however, assume the presence of $7.4 billion of energy cost savings attributable to the program during this four year period. The late publication of this estimate prevented OPSI and other parties from questioning PJM about its basis. OPSI has a number of concerns that the estimated costs are understated and that the cost savings are significantly overstated.

Clearly, a program with costs (without considering possible but undemonstrated claims of energy cost savings) potentially as high as $13.4 billion merits very thorough and careful review by the Commission in an evidentiary process where affected States and market participants have a reasonable opportunity to obtain data needed to understand the program and to present their views on it to the Commission.

Importantly, PJM's proposed RPM reforms are not the only initiative being pursued to address and resolve concerns respecting the reliability of regional grid

[10] CP Initiative, at p. 4 (Oct. 23, 2014).

operation. For example, the Commission has a major initiative to improve coordination of the natural gas and electric market and transmission systems.[11] A lack of coordination between these two industries is viewed as a significant contributor to the operational and reliability problems experienced during the January 2014 extreme cold weather. PJM also has been developing several programs for weatherizing and testing generation to avoid, in part, excessive and unnecessary generation outages experienced during extreme cold weather. PJM is also implementing modifications to natural gas-fired generation commitment procedures to avoid fuel unavailability problems experienced at times last winter.[12] These programs have the potential to lessen near-term concerns over reliability and operability of the regional grid.

State regulators appreciate the reliability of the PJM system as much as any PJM stakeholder, if not more. When customers experience outages, state regulators are extremely concerned. State regulators, however, also are very concerned that customers not receive energy bills that are higher than they can afford and be forced to adjust purchases of medicines and food, balance rent or mortgage payments, and expenses for other necessities. State regulators must seek a balance to ensure that increased costs are necessary and appropriate and provide sufficient public benefits to justify the increased costs. OPSI respectfully suggests that the cost effectiveness of the proposed CP proposal

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[11] See Order Initiating Investigation into ISO and RTO Scheduling Practices and Establishing Paper Hearing Procedures, 146 FERC ¶ 61,202 (Mar. 20, 2014).

[12] See, e.g., PJM Operating Committee, Gas Unit Commitment Coordination – 2014/2015 Winter Scope Proposal Review (Oct. 17, 2014); PJM Operating Committee, Cold Weather Resource Improvement Final Proposal, (Sep. 18, 2014); PJM Operating Committee, Special Cold Weather Resource Improvement Final Proposal Report, (Sep. 4, 2014). These programs include a Generation Resource Cold Weather Checklist to be employed by generation owners to assure unit readiness at the start of cold weather periods, and an operational exercise to further assure readiness. These documents are available at the Operating Committee webpage at the PJM website.

has not been justified with sufficient detail. The simple recitation that costs will increase and benefits will occur does not provide the OPSI jurisdictions with the necessary information to support the proposed reforms. A hearing with sufficient opportunity to identify, evaluate and resolve issues is vitally necessary for state regulators to make an informed decision regarding the justness and reasonableness of the proposed reforms.

A second concern of state regulators is that the transition program to achieve reliance on new CP-qualified generation conflicts with price certainty established in state retail auctions. For example, PJM proposes that 60 percent of all capacity employed to serve load shall be CP-qualified beginning in 2016-2017. This capacity would be obtained through incremental auctions from new and existing capacity, including capacity already committed to providing service as Annual Capacity Resources in these years.[13] It is expected that CP resources will receive significantly higher compensation than existing Base or Annual Capacity Resources. These additional costs would be recovered from retail customers.[14] However, retail load serving entities have already committed in state retail auctions and obtained contracts from generators based on existing auction prices to provide service. PJM appears to be proposing that these established retail service prices must be raised to reflect the new capacity performance cost structure, but has not provided any clear estimate as to how great this price addition would be. The intention to impose a plan that would produce additional price increases requires considerable further evaluation *before* implementation of such a plan.

[13] PJM Capacity Performance Updated Proposal at p. 34.

[14] Indeed, according to industry commenters, this additional compensation may increase by 50 to 100% of existing RPM capacity charges. See, e.g., Comments of Exelon Corporation; Comments of NextEra Energy Resources.

In regulated states, PJM's proposed applicability of CP requirements to fixed resource requirement ("FRR") entities would require a retroactive redefinition of capacity previously included in approved self-supply plans and would require modifications to existing contracts to incorporate the higher cost of these requirements. Additionally, unless a state has decided to restructure its regulatory scheme, generation facilities are under the sole authority of states and state utility commissions. Federal case law has determined that Section 201 of the Federal Power Act is honored regarding wholesale capacity auctions, such as PJM's proposed RPM, as long as states have a choice (i.e., a way to "opt out "of the RPM auction process).[15] The FRR – as it currently exists – meets this opt-out requirement. However, PJM's proposed RPM revisions, as they pertain to FRR entities, would impermissibly infringe on state authority.

PJM's proposal would also increase concerns regarding the exercise of market power under a new dual product RPM, which could adversely affect the end-user price of service. This concern is exacerbated by the market power mitigation safe harbor proposed to be provided up to the level of Net CONE and undefined limits on market price decline between delivery years. Market power concerns have already increased by the recent approval of PJM's request for a substantial increase in the slope of the VRR Curve used to procure capacity in the RPM. Once implemented, such increased slope will exacerbate even further the potential exercise of market power, since profits achievable from such exercise would be significantly increased. Again, PJM has not as

[15] ***Conn. Dep't of Pub. Util. Control v. FERC***, 569 F.3d 477, 482-84 (D.C. Cir. 2009).

yet provided any data or analysis that allays these concerns.[16]

III. Retain the 2.5% Holdback

PJM proposes to eliminate the 2.5% holdback based on PJM's assertion that it is no longer needed. PJM has historically withheld procuring 2.5% of its generation resource requirement in the Base Residual Auction (“BRA”). Two rationales support the holdback. First, the holdback is a mechanism to provide an opportunity for short-term resources to participate, and, second, the holdback prevents systematic over-procurement of capacity.[17] OPSI supports continuation of the 2.5% holdback, which has been effective in reducing over-procurement of resources and in light of PJM’s documented tendency to over-forecast its reliability requirement.[18] Over the past three BRAs, PJM’s reliability requirement was adjusted downward between 3.3%-6.9% after those BRAs to reduce over-procurement. These adjustments are well in excess of the 2.5% holdback.[19]

Moreover, a recent study by the Brattle Group (prepared for the Sustainable FERC Project) concludes that PJM’s forecasting process has failed to fully include the effects of existing and planned energy efficiency programs. Any such failure further confirms the need to retain the holdback to avoid over-procurement of capacity and unneeded cost

[16] PJM Interconnection, L.L.C., 149 FERC ¶ 61,183 at pp. 17-19 (2014); The Brattle Group, Third Triennial Review of PJM’s Variable Resource Requirement Curve at pp. 45-47 (May 15, 2014); PJM Capacity Performance Updated Proposal at pp. 14, 30-31; Comments of PJMICC (Sep. 16, 2014).

[17] See PJM’s Response to the 2013 State of the Market Report, at p. 12 (May 7, 2014).

[18] See OPSI Resolution # OPSI-201101 (adopted May 5, 2011).

[19] Affidavit of James F. Wilson in support of the Protest of the PJM Load Group, Table 2 at p. 25, filed in PJM Interconnection, L.L.C., Docket No. ER14-2940-000 (October 16, 2014).

imposition on end-users.[20]

OPSI members assert that both the consistent over-forecasting and the ability of customers to implement demand reduction plans when required to maintain system reliability support the retention of the 2.5% holdback. OPSI agrees that PJM should prepare a reasonable load forecast for the BRA; however, the 2.5% holdback should not be eliminated until that effort has been completed. Moreover, as measured by PJM's Independent Market Monitor, the additional price effects imposed on end-users from elimination of the holdback would be approximately $2.4 billion, an increase of about 32 percent in capacity market costs.[21]

IV. Conclusion

For the reasons stated above the Organization of PJM States, Inc., strongly urges that PJM's proposed RPM revisions be set for an evidentiary hearing.

Respectfully submitted,

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[20] The Brattle Group, Quantifying the Amount and Economic Impacts of Missing Energy Efficiency in PJM's Load Forecast (Sep. 2014). Brattle concluded that PJM overstates load growth by approximately 30% per year as the result of this failing.
[21] See Monitoring Analytics, Analysis of the 2017/2018 RPM Base Residual Auction at p. 5 (Oct. 6, 2014).

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I am on this date serving a copy of the foregoing document upon each person designated on the official service list compiled by the Federal Energy Regulatory Commission in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure.

Dated in Newark, Delaware this 19th day of January, 2015

Respectfully submitted,

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Document Content(s)