UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

PJM INTERCONNECTION, L.L.C.) Docket No. ER16-76-000

COMMENTS OF THE PJM POWER PROVIDERS GROUP

The PJM Power Providers Group ("P3")[1] hereby submits these comments in reply to the October 15, 2015, filing by PJM Interconnection, L.L.C. ("PJM").[2] PJM requests revisions to Attachment K-Appendix of the PJM Open Access Transmission Tariff ("Tariff"), and the identical provisions of Schedule 1 of the Amended and Restated Operating Agreement of PJM Interconnection L.L.C. ("Operating Agreement"), to modify various offer cap and price formation provisions in advance of the 2015-2016 winter, until such time that the Federal Energy Regulatory Commission ("Commission") provides more permanent guidance or issues a formal rule regarding offer price caps.[3]

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[1] P3 is a non-profit organization dedicated to advancing federal, state and regional policies that promote properly designed and well-functioning electricity markets in the PJM Interconnection, L.L.C. ("PJM") region. Combined, P3 members own over 84,000 MWs of generation assets, produce enough power to supply over 20 million homes and employ over 40,000 people in the PJM region covering 13 states and the District of Columbia. The comments contained in this filing represent the position of P3 as an organization, but not necessarily the views of any particular member with respect to any issue. For more information on P3, visit www.p3powergroup.com

[2] On October 23, 2015, P3 filed a doc-less Motion to Intervene in the above-captioned proceeding.

[3] *See, e.g., Settlement Intervals and Shortage Pricing in Markets Operated by Regional Transmission Organizations and Independent System Operators*, Notice of Proposed Rulemaking, Docket No. RM15-24-000 (September 17, 2015) ("NOPR").

PJM requests that the Commission issue an order by no later than December 14, 2015, with an effective date of December 14, 2015, for the proposed revisions, in accordance with the 60-day notice requirement in section 35.3(a)(1) of the Commission's regulations.[4]

I. COMMENTS

P3 encourages the Commission to approve the PJM proposal with the understanding that there are several flaws inherent in the PJM filing that prevent it from being sound market policy over the long term. The PJM proposal is inconsistent with Commission precedent, as well as PJM's own recently-articulated views of proper energy market price formation. While approval is appropriate in in the near term to prevent PJM from entering the winter with an unjust and unreasonable energy market offer cap, the Commission should require PJM to put in place in the near future an energy market cap that will allow market participants to reflect their costs in their offers and, if marginal, to allow those units to set the market price.

The PJM proposal raises the energy market offer cap for cost-based offers to $2,000/MWh, provided those offers are consistent with PJM's cost development guidelines and the generator's fuel cost policy. Market-based offers remain capped at the current $1,000/MWh unless a unit's costs exceed $1,000/MWh, in which case the market-based offer can rise to the level of its cost-based offer. Under the proposal, offers up to $2,000/MWh can set the Locational Marginal Price ("LMP"), while offers that exceed $2,000/MWh and clear will be paid for via an uplift mechanism, rather than being reflected in the LMP.

The Commission must understand that the PJM proposal is the result of a stakeholder compromise that was forged with the explicit understanding from all sides that the proposal would only be a short-term energy market offer cap structure. Rather than advocating a proposal

[4] *PJM Interconnection, L.L.C.,* Docket No. ER16-76-000, filed on October 14, 2015.

that reflected PJM's own vision of a proper energy market offer cap, PJM developed and pushed a proposal that could achieve super majority stakeholder support. PJM was successful at achieving the necessary votes in order to avoid the 206 process.[5] However, PJM fell short of submitting to the Commission an energy market offer cap that will be just and reasonable over the long term.

A. The current PJM energy market offer cap is not just and reasonable.

As the Commission is aware, in both the winters of 2014 and 2015, fuel costs rose to levels that prevented generators from submitting offers that allowed for the full recovery of fuel costs while still respecting the $1,000/MWh offer cap. In January of 2014, natural gas prices in the PJM Region hit record-setting prices averaging over $120/MMbtu and including high prices up to $140/MMbtu for trades on January 21, 2014, and on January 22, 2014.[6]

With gas prices at that level, the $1,000/MWh offer cap proved insufficient, creating a situation that PJM described as "patently unfair."[7] As PJM stated at the time, "[G]enerators cannot lawfully be required to buy fuel at a cost of millions of dollars for the purpose of generating power and selling it at a loss."[8] On January 21, 2014, approximately 5,000 MWs of Day-Ahead energy market offers were priced at $999/MWh – the maximum value permitted by PJM's market software - indicating that costs for these units were above the offer cap.[9] As a

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[5] Section 206 of the Federal Power Act, 16 U.S.C.§824e.

[6] PJM Interconnection, L.L.C., Request of PJM Interconnection, L.L.C., For Waiver, Request For 7 Day Comment Period, and Request For Commission Action By February 10, 2014, ER 14-1145-000, Jan 23, 2014, ("PJM Waiver Request"), at p 4.

[7] *Id* 1-2.

[8] *Id*.

[9] See, https://www.pjm.com/~/media/committees-groups/task-forces/crstf/20140602/20140602-item-02-crstf-pjm-offer-cap-education.ashx at pages 19-21.

result of the offer cap and other tariff provisions, uplift charges in PJM soared to over $500 million in January 2014.[10]

Appropriately, in January of 2014, the Commission approved two emergency tariff waiver requests filed by PJM in order to address this "concrete problem."[11] The first waiver allowed cost-based offers above $1,000/MWh to be submitted with cleared offers above that level being paid via an uplift mechanism.[12] The second waiver allowed cost-based offers above $1,000/MWh to be submitted and set LMP.[13] The second waiver closely tracks PJM's articulated position in the Energy Price Formation docket.[14] However, both of these waivers expired on March 31, 2014.

Given the events of the winter of 2014, and the patent need to address an unjust and unreasonable market design, PJM filed a "temporary tariff change" on December 15, 2014. Unlike the first waiver request, PJM requested that a $1,800/MWh cap be put on market seller offers with costs above $1,800/MWh being funded through a make whole provision. PJM submitted these revisions as "temporary tariff revisions."[15] The Commission approved PJM's

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[10] Presentation of Andy Ott and Mike Kormos, "Operational Events and Market Impacts January 2014 Cold Weather," May 9, 2014 at 24.

[11] 146 FERC ¶ 61,078, at P 40 (2014).

[12] Request of PJM Interconnection, L.L.C. For Waiver and For Commission Action By January 24, 2014, Docket No. ER14-1144-000 (January 23, 2014).

[13] Request of PJM Interconnection, L.L.C. For Waiver, Request For 7-Day Comment Period, and Request For Commission Action By February 10, 2014, Docket No. ER14-1145-000 (January 23, 2014).

[14] *Price Formation in energy and Ancillary Service Markets Operated by Regional Transmission Organizations and Independent System Operators*, Docket No. AD14-14-000 (June 19, 2014). ("AD14-14")

[15] PJM Interconnection, L.L.C., Docket No. EL15-31-000 (December 15, 2014).

filing for the winter of 2015[16] and during that winter PJM did receive cost-based offers that exceeded $1,000/MWh.[17] Consistent with the PJM request, these tariff revisions were withdrawn earlier this year, restoring as binding tariff provisions the $1,000/MWh energy market offer cap, which the Commission has found on three separate occasions to be unjust and unreasonable.

P3 continues to agree with PJM and the Commission that a $1,000/MWh energy market offer is cap is unjust and unreasonable. The events of the past two winters make it abundantly clear that a cap at this level distorts market signals, encourages inefficient outcomes and simply does not work. A permanent solution is required. Unfortunately, the PJM filing merely represents an improvement to the status quo and not an answer that will withstand the test of time.

B. In order for an energy market to function properly, units must be able to offer in their costs and those costs should be reflected in price.

Earlier this year, PJM very clearly told the Commission that it is appropriate to eliminate the cap on cost-based offers. As PJM stated,

> "Resources should be allowed to recover their costs of providing energy and not be limited by any arbitrary cap. **Not allowing resources that provide energy the opportunity to recover their costs of operating would result in unjust, unreasonable, and likely confiscatory rates. While some may argue that not having a cap on cost-based offers would invite offers that would unreasonably raise prices on consumers, PJM does not believe this would be true**. In PJM, cost-based offers must be submitted in accordance with PJM's Cost Development Guidelines, which in of themselves limit the type of costs that can be included in cost-based offers. Absent fraud or an inadvertent

[16] 150 FERC ¶ 61,020.

[17] "On February 20, 2015, for the second consecutive year, PJM set its all-time winter peak demand, which was 143,826 MW (based on preliminary telemetered data). On the same date, 13 available generation units submitted cost-based offers of $1,000/MWh or greater and 11 other generation units also had cost-based offers above $1,000/MWh but were unavailable. The highest offer on an available generation resource was $1,795/MWh, plus applicable startup and no-load costs" (AD14-14) Comments of PJM March 6 at page 3.

> failure to adhere to the Cost Development Guidelines, the Cost Development Guidelines effectively cap cost-based offers at the approximate actual costs incurred by generation resources when operating." (emphasis added)[18]

P3 agrees with PJM's position and logic as articulated a mere eight months ago. Generators have been submitting cost-based bids under PJM's Cost Development Guidelines since the inception of its energy markets in 1997.[19] Competitive pressures from other generators also serve as an effective check on energy market offers. Moving to a long term structure, as articulated by PJM in March, would not create the price escalation that many fear. Instead, allowing generators to reflect their costs, developed consistent with PJM's guidelines, and having those offers set LMP would create the efficient market outcome the Commission desires.

Indeed, the Commission has been very firm on this point. In granting the waiver to PJM during the winter of 2014, the Commission found that proper market design allows the marginal unit to set the clearing price for all units. As the Commission stated last year when evaluating PJM's waiver request:

> "By limiting legitimate, cost-based bids to no more than $1,000/MWh, the market produces artificially suppressed market prices and inefficient resource selection. By paying an uplift, PJM is in effect paying one price for energy dispatched through the market (e.g. $1,000), and a second higher price (e.g. $1,200) for the resource dispatched out-of-merit (while treating the latter in the dispatch stack as if it had a bid of $1,000). This would not be consistent with longstanding Commission precedent."[20]

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[18] AD14-14, at p3.

[19] Cost guidelines were in place during the split savings cost dispatch regime that preceded PJM energy markets.

[20] Docket No. ER14-1145-000 ORDER GRANTING WAIVER at paragraph 40.

C. PJM's proposal creates an additional and unnecessary avenue for unhedgable uplift.

It is ironic, and at some level troubling, that at a time when PJM and the Commission are undertaking arduous efforts to limit the opportunities for uplift to occur in the market, that PJM proposes to the Commission an offer cap structure that provides a clear path for uplift to distort the market. As the PJM filing states, "PJM proposes to allow Market Sellers of generation resources with demonstrated costs above $2,000/MWh, calculated in accordance with the Cost Development Guidelines and applicable fuel cost policy, to recover those costs through make-whole payments."[21]

PJM and the Commission have been resolute in their desire to reduce unhedgeable uplift from the market. The Commission has clearly articulated its view of proper energy pricing in stating that, "[L]ocational marginal prices for energy and ancillary services ideally would reflect the true marginal cost of production, taking into account all physical system constraints, and fully compensate all resources for the variable cost of providing service."[22] The Commission has gone even further, offering that "volatile uplift charges may also create financial uncertainty for customers, depress liquidity and reduce market efficiency."[23]

For its part, PJM recognizes the problems associated with uplift. As PJM stated to the Commission last year, "Unfortunately, uplift payments lack market transparency. This lack of transparency can inhibit investment because the market is not providing the appropriate price to signal needed locational investment (via higher prices). Uplift costs are out-of-market and, as

[21] PJM Filing at 7.

[22] Staff Analysis of Shortage Pricing in RTO and ISO Markets, Oct at 1.

[23] Uplift in RTO and ISO Markets, August 2014 at 2.

such, are not included in the price signals that are visible to the entire market. Unlike energy prices, these uplift charges are not predictable and cannot be hedged on a forward basis."[24]

Less than two years ago, PJM proposed and the Commission accepted an energy market offer cap, in the form of a temporary waiver, that allowed costs to be reflected in offers and not did not include a mechanism to create uplift.[25] As referenced above, such a policy is consistent with "longstanding Commission precedent." To foster a stakeholder compromise, PJM advocated a proposal that is quite inconsistent with "longstanding Commission precedent" and contrary to efforts to eliminate vehicles for unhedgeable uplift to occur. While P3 members reluctantly support the compromise proposal before the Commission as an improvement over the status quo, P3 is greatly troubled by this departure from Commission policy and requests that PJM be required to rectify this situation in the long term.

D. Given that PJM's proposal is inconsistent with both the Commission's and PJM's vision of a proper energy market offer cap, the Commission should move quickly to provide PJM and other RTOs the guidance necessary to establish proper and enduring energy market offer caps.

As evinced above, P3 is troubled by the PJM filing on many levels. While the filing represents an improvement to the status quo, it is also contrary to PJM's and the Commission's well-articulated positions. PJM elected to pursue a short-run stakeholder compromise, instead of leading with a more durable long term solution that would have been less popular, but consistent with Commission policy and better long run economics. P3 strongly urges the Commission to require PJM to further improve its energy market cap so it is economically rational and sustainable. After the experiences of the last two winters, and lengthy discussions at the

[24] Energy and Ancillary Services Uplift in PJM F. Stuart Bresler, III Vice President - Market Operations PJM Interconnection FERC Uplift Workshop Docket No. AD14-14: Price Formation in Energy and Ancillary Service Markets Operated by Regional Transmission Organization and Independent System Operators September 8, 2014 at page 3.

[25] See, PJM Interconnection, L.L.C., 146 FERC ¶ 61,078 (2014).

Commission and at PJM, the correct answer is apparent. In fact, the correct answer was already approved, on a temporary basis, in the winter of 2014 in the form of the second waiver.[26] PJM re-articulated in March of 2015 the correct framework for an appropriate energy market cap, but PJM now appears unwilling to pursue that framework absent direction from the Commission. Whether in the context of this docket or in the Energy Price Formation docket, PJM is clearly searching for a beacon. P3 urges the Commission to provide one and provide PJM further direction to improve its offer price caps on a long term basis consistent with these comments.

II. CONCLUSION

The Commission should approve the PJM proposal as a short term improvement but should also require PJM to address the issue on a long term basis as described.

Respectfully submitted,

On behalf of the PJM Power Providers Group

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[26] *Id.*

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the Official Service List compiled by the Secretary in this proceeding.

Dated at Washington, D.C., this 4th day of November, 2015.

On behalf of the PJM Power Providers Group

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