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PJM PROPOSES TO ENHANCE ELECTRIC ENERGY PRICE FORMATION

Proposal Would Reward Resource Flexibility, Enhance Shortage Pricing

(Valley Forge, Pa. – Nov. 15, 2017) – PJM Interconnection today released a proposal to ensure that its wholesale electricity market prices do the best possible job of reflecting the resources required to serve customers and of maintaining an optimal mix of resources in the long term.

In the paper published today, [*Proposed Enhancements to Energy Price Formation*](#), PJM recommends an enhancement to locational marginal pricing to allow inflexible units scheduled by PJM to set price under certain circumstances. (Inflexible units are unable to increase or decrease their output within a specified period, require a minimum run time or minimum down time.)

“For the past 20 years, PJM’s competitive wholesale markets have ensured power grid reliability at the lowest reasonable cost and market rules have adapted to an evolving industry,” said Stu Bresler, senior vice president – Operations and Markets. “Now, the changing resource mix and flattening supply curves reveal a need to enhance energy market price formation.

“We need to more accurately reflect the resources required to serve load, to incent flexible resources, and to minimize out-of-market uplift payments. We need to begin the stakeholder discussion and consideration of our proposal.”

Both flexible resources and inflexible resources are necessary to meet the demand on the power system. However, inflexible units are not currently permitted to set price. Therefore, PJM said, energy prices do not always accurately reflect the true cost to serve load because the cost of an inflexible unit needed to serve demand may not be included in the price.

This limitation of locational marginal pricing was hidden because flexible units, which tended to be higher-cost units, historically set price often enough to ensure that needed resources had the opportunity to earn sufficient revenues to cover their total costs, from combined energy, capacity and ancillary service revenues.

The recommendation in the PJM paper would enable all units scheduled by PJM to compete to set energy market prices, provide incentives for flexibility and resource performance and reduce uplift payments. The paper said customers would benefit from improved market transparency and operational efficiency.

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The net impact of the proposed changes is estimated to be an increase in total energy and capacity market costs of between 2 percent and 5 percent.

“The proposal values flexibility for load-following,” Bresler said. “This is important going forward in part because of the anticipated continuing increase in intermittent resources. All market participants will benefit from ensuring appropriate price signals.”

The proposal also includes enhanced shortage pricing. The plan would better align reserve pricing and the value of reserves by basing the operating reserve demand curves on how reserves enhance reliability. PJM’s shortage pricing proposal offers more complete modeling of all needed reserve products.

PJM’s current shortage pricing mechanism does not result in increased energy and reserve prices until the system is short 10-minute reserves. Implementation of a real-time, 30-minute operating reserve product would enhance shortage pricing by sending price signals to incent response prior to a shortage of 10-minute reserves, thereby providing price signals that would incent resources to respond and avoid severe shortages of 10-minute reserves.

[PJM Interconnection](#), founded in 1927, ensures the reliability of the high-voltage electric power system serving 65 million people in all or parts of Delaware, Illinois, Indiana, Kentucky, Maryland, Michigan, New Jersey, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia and the District of Columbia. PJM coordinates and directs the operation of the region’s transmission grid, which includes over 82,000 miles of transmission lines; administers a competitive wholesale electricity market; and plans regional transmission expansion improvements to maintain grid reliability and relieve congestion. PJM’s regional grid and market operations produce annual savings of \$2.8 billion to \$3.1 billion. For the latest news about PJM, visit PJM Inside Lines at insidelines.pjm.com.

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