



STATE OF NEW JERSEY
BOARD OF PUBLIC UTILITIES



November 3, 2011

Mr. Howard Schneider
Chair, Board of Managers
PJM Interconnection, L.L.C.
955 Jefferson Avenue
Norristown, PA 19403-2497

Dear Mr. Schneider:

The Maryland Public Service Commission, the New Jersey Board of Public Utilities, the Delaware Public Service Commission, and the District of Columbia Public Service Commission (“State Commissions”) write to express our view that the Brattle Group’s Performance Assessment of PJM’s Reliability Pricing Model (“RPM”) dated August 26, 2011, (“Performance Assessment”) is deficient in its attempt to satisfy its obligation to “report on the performance of RPM”¹ because the Performance Assessment does not identify, much less analyze and respond to, the well-publicized concerns of PJM’s Independent Market Monitor (“IMM”). This letter, however, should not be construed as supporting specific recommendations from the IMM or the Brattle Group on how to improve the RPM or as supporting RPM itself.

¹ PJM Interconnection, L.L.C., 117 FERC ¶ 61,331 (Order Denying Rehearing and Approving Settlement Subject to Conditions) (2006).

Each year the IMM publishes a voluminous State of the Market report, with a substantial portion dedicated to the capacity market and certain aspects of the energy market that are related to the capacity market. The absence of a response to the IMM's RPM-related concerns is a serious omission that precludes us and FERC from properly evaluating RPM. The IMM is not just another stakeholder, but a neutral entity upon which market participants and regulators rely to identify flaws in PJM's markets. State Commissions in particular do not have the resources to review the wholesale market in detail. We rely heavily on the unbiased analysis of the IMM to bring to light market structure issues.

The explicit purpose and scope of the performance assessment demands a detailed review of and response to the IMM's concerns about RPM. Brattle conducted stakeholder interviews to identify key areas of concern, evaluate individual RPM design elements, and develop recommendations for possible modifications (if any) to improve the effectiveness of RPM. Brattle also interviewed the IMM, which is responsible for an ongoing review of RPM and is, therefore, a unique and valuable resource to Brattle in its effort to conduct its own study. Yet Brattle barely mentions the IMM's long-running efforts. This failure to address the concerns the IMM has identified, at length, calls into question the efficacy of the performance assessment of the RPM.

The IMM's concerns should be the starting point for Brattle, but instead were relegated in whole to the Appendix to the Performance Assessment; Brattle noted in the Appendix that "we did not separately summarize comments by the independent market monitor as they were consistent with the IMM's public statements, documents, and presentation posted at www.monitoringanalytics.com." Perhaps, if Brattle had listed the IMM's detailed recommendations on obligations of capacity resources, strengthening the incentives in the RPM Capacity Market, and that the terms of Reliability Must Run Service be reviewed, refined and standardized, which can be found succinctly summarized on page 363 of the 2010 State of the Market Report for PJM, they would have seen fit to address them in the body of the report. We are, quite frankly, bewildered at the disconnect between the Performance Assessment and the IMM's efforts regarding these issues.

The IMM recommends in the 2010 State of the Market Report, for example, that "the obligations of capacity resources be more clearly defined in the market rules."² The Performance Assessment notes that a key design element of RPM is "explicit market monitoring and mitigation rules, including a must offer requirement for existing generating resources and IMM review and mitigation of new entrant offers," but there is no elaboration on the critical and contentious must-offer requirement elsewhere. The IMM had four detailed recommendations in the 2010 State of the Market Report concerning the obligations of capacity resources in RPM:

² 2010 State of the Market Report at 363.

- The MMU³ recommends that there be an explicit requirement that capacity unit offers into the Day-Ahead Energy Market be competitive, where competitive is defined to be the short run marginal cost of the units.
- The MMU recommends that protocols be defined for recalling the energy output of capacity resources when PJM is in an emergency condition. PJM is developing these protocols.
- The MMU recommends that a unit which is not capable of supplying energy consistent with its day-ahead offer should reflect an appropriate outage rather than indicating its availability to supply energy on an emergency basis.
- The MMU recommends that PJM review all requests for Out of Management Control (OMC) carefully, develop a transparent set of rules governing the designation of outages as OMC and post those guidelines. The MMU also recommends that PJM consider eliminating lack of fuel as an acceptable basis for an OMC outage.⁴

These and other recommendations are not discussed in the report. In addition, the IMM stated in the State of the Market Report:

The MMU recommends that the performance incentives in the RPM Capacity Market design be strengthened. The MMU recommends that capacity resources be paid on the basis of whether they produce energy when called upon during any of the hours defined as critical.

The Performance Assessment contains no analysis of why generators should be paid 50% of their capacity payment even if they do not perform, despite the obvious fact that capacity payments, or the lack thereof, are essential to the entire RPM construct. The Performance Assessment's only comment on penalty mechanisms was to observe that penalties were comparable between demand response and generation. On a related subject, there was no analysis of why PJM experiences emergency generation events even in off-peak seasons when the *raison d'être* of RPM is to obtain sufficient resources to reliably meet customers' electricity needs during the peak hour of the peak day of the year.

The performance assessment is *the* opportunity for consumers to evaluate whether they are getting value for the billions of dollars a year they pay for capacity. Because of the failure of the study to address the concerns of the IMM, we still have no answer to this question. Although State Commissions may not always agree with the IMM's

³ Consistent with the terminology in PJM's Tariff dating to when the IMM was internal to PJM, the Independent Market Monitor is sometimes referred to as the Market Monitoring Unit, or MMU.

⁴ 2010 State of the Market Report at 363.

Mr. Howard Schneider

November 3, 2011

Page 4

recommendations, the failure of the RPM Performance Assessment to address the IMM's concerns results in a fatal flaw in this vital review.

Accordingly, the State Commissions request that the PJM Board require a supplemental Performance Assessment that comprehensively and objectively evaluates the performance of the RPM market before any changes to RPM are formally proposed by PJM.

DATED: November 3, 2011

BY:

/s/ Douglas R. M. Nazarian

DOUGLAS R. M. NAZARIAN

CHAIRMAN

On behalf of the Maryland Public Service Commission

/s/ Lee A. Solomon

LEE A. SOLOMON

PRESIDENT

On behalf of the New Jersey Board of Public Utilities

/s/ William O'Brien

WILLIAM O'BRIEN

EXECUTIVE DIRECTOR

On behalf of the Delaware Public Service Commission

/s/ Betty Ann Kane

BETTY ANN KANE

CHAIRMAN

On behalf of the District of Columbia Public Service Commission