

¹EKPC backstop proposal: procurement quantity and credit/financial settlement components

(Appendix: overview and observations of PJM's Stage 1 CIFP Proposal)

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Introduction

EKPC maintains a preference for a voluntary, bilateral Reliability Backstop Procurement in which PJM primarily plays a match-making function and takes on no negotiation or counterparty responsibilities. However, should PJM pursue a central procurement structure to satisfy the capacity needs of Large Loads, EKPC offers the proposal below for **(1) how to establish the target procurement quantity and (2) how to ensure the cost-causer is allocated the cost and held responsible to satisfy necessary credit and collateral requirements.**

The appropriate entity to engage for determining the procurement target and for being responsible for the cost and credit requirements is the Load Serving Entity who is required under law or by contract to supply the Large Load. The Electric Distribution Company (EDC), who supplies the delivery service to the end-consumers, is not the appropriate entity for these roles. To the extent that an EDC is the LSE, then only by virtue of its role as LSE is it the appropriate entity.

EKPC's proposal is a parallel procurement and payment framework that relies on the same principles founding the RPM procurement and financial responsibility requirements. It addresses incentives and cost-causation objectives.

Legal Foundation

PJM's Operating Agreement requires all Load Serving Entities who rely on PJM's markets to become a party to the Reliability Assurance Agreement. That agreement requires the LSEs to pay the result of all RPM auctions' capacity commitments for each Delivery Year. The current effort to create a Reliability Backstop Procurement (RBP) focuses on procuring capacity and establishing up to 15 years of capacity purchase obligations. Only LSEs sell that product to the retail, end-consumers they serve. In retail rate regulated states like Kentucky, the LSE and Electric Distribution Company (EDC), or distribution utility, are one and the same. Although identifying an appropriate LSE in advance of a Delivery Year is not something that must occur under the RPM construct today, it is reasonable (and practical) to build upon the current PJM Tariff and Reliability Assurance Agreement (RAA) capacity market rules for purposes of creating an RBP. EKPC's proposal builds upon the current legal framework for PJM's current capacity construct.

PJM's governing documents do not contain a definition of EDC nor do EDCs execute any PJM governing document for purposes of carrying out their role of an EDC. The only role that an EDC plays in the PJM realm is administrative. PJM looks to the EDC to identify the Peak Load Contribution of LSEs in order to appropriately bill them for capacity charges and transmission

¹ At this time, EKPC takes no position on "connect and manage."

charges. Additionally, PJM looks to both EDCs and LSEs to provide Large Load Adjustments in the load forecasting process outlined in Manual 19. The LSEs, however, bear the financial obligations that result from these administrative determinations. Also, PJM looks to EDCs to facilitate PJM's implementation of the DR/DER the opt-in/opt-out rules and DR and DER registration validation. Of course, these responsibilities also do not place affirmative financial responsibilities on EDCs in PJM's wholesale markets. Note too that the use of EDC invokes a different subset of entities for these purposes. For capacity and network transmission service allocation purposes, PJM looks to the zonal EDC, who identifies the appropriate allocation by virtue of reading the meters of all and transmission dependent distribution utilities, cooperatives and municipalities. which in many cases include other distribution utilities. For purposes of DR and DER, PJM looks to the individual distribution utility.

Moreover, the FERC does not have jurisdiction over EDCs. They are distribution utilities. Distribution utilities and local distribution facilities themselves are excluded from FERC's general rate and transmission jurisdiction under the Federal Power Act Section 201. The FERC's "affecting" jurisdiction under Federal Power Act Section 205 has been argued to enable coordination between federal and non-federal entities in order to ensure that markets can deliver reliable and cost-effective results, but directly assigning financial obligations and credit assurance responsibility for products procured in the organized wholesale market to enable LSEs to perform their tariff or contract obligations to end consumers is not within FERC's "affecting" jurisdiction. Only via contract has PJM established a legally binding relationship with entities not subject to FERC's jurisdiction – the Reliability Assurance Agreement (RAA) among Load Serving Entities. In order for LSEs to use the organized wholesale competitive markets PJM Administers to carry out their retail responsibilities to serve end-consumers, PJM's Operating Agreement requires LSEs to become Parties to the RAA.

EKPC Proposal

(1) Procurement Target

In the prior CIFP-Large Load process, EKPC advocated that only Large Load attested to by an LSE obligated to serve that load be included in the load forecast that is used to establish the Reliability Requirement in RPM. The purpose of this proposal was to ensure that there is "skin in the game" by the entities who ultimately will be held accountable to pay the resultant prices from RPM auctions. The current Large Load Adjustment process in Manual 19 looks to EDCs (and LSEs who are transmission dependent upon the zonal EDC) to inform PJM of the expected large load additions and looks only to the agreements those EDCs have in place with the large loads. This misses the mark as most EDCs are not responsible for supplying the capacity and energy requirements of the anticipated Large Loads. Although it is appropriate to include the EDC in the process, as they may validate the location of the anticipated Large Loads since they directly or indirectly have to account for those loads' metered energy usage, they do not have the same "skin in the game" to ensure that the value that drives a capacity procurement target is most accurate.

PJM's RBP proposal seems to address this shortcoming in the current Large Load Adjustment process by requiring the EDC to communicate with the LSEs intending to supply the Large Loads, and/or the Large Loads themselves, to determine whether the anticipated capacity needs is accurate and whether there are new resources under development to supply their future needs. However, this proposal unnecessarily places the EDC in a middle-man role. This proposal would require the EDC to

attempt to attain commercially sensitive information (i.e., need enough information to assess whether the supply plan is “real” and feasible), and could create a conflict of interest for some EDCs (i.e., they could be viewed as competitors to supply the Large Load). Instead of creating a middle-man role, PJM could obtain this information in a confidential process directly from the entities that possess the information – the LSEs and even the Large Loads themselves if they wished to interface directly with PJM for this purpose.

PJM’s proposal to subject Large Loads to a “connect and manage” construct should they not bring new capacity sufficient to cover their capacity needs in the next several Delivery Years is touted as the incentive for participation in the RBP. Indeed, that should be the incentive for the Large Loads to ensure that any procurement activities on their behalf are appropriately and specifically tied to them in order for them to avoid being subject to “connect and manage”. Thus, the “connect and manage” avoidance incentive should incent Large Loads to identify the LSE that will be responsible for supplying their capacity needs in the Delivery Years subject to the RBP. Given that these are loads greater than 50 MWs, it also is reasonable to assume that if they have reached an agreement with the EDC for the interconnection of their load meriting their representation in the PJM Large Load Adjustment load forecasting process, they are working with the entity they are planning to use as their LSE. In some instances, the EDC may be their LSE; but in retail choice states the LSE may be a completely separate corporate entity, unaffiliated with the EDC. Indeed, in some retail regulated states the entity PJM may be viewing as the EDC in its proposal may be a completely separate entity from the municipality or cooperative that, in fact, is the EDC serving the end consumer. (E.g., a zonal EDC may serve transmission dependent municipalities and cooperatives). Even if the Large Loads themselves are directly securing resources, they likely are accounting for those activities in their contractual arrangements with an LSE.

The LSE, therefore, would be in the best position to know what amount of load is covered through resource procurement activities outside of PJM’s markets and what amount of load would need to be included in the RBP. The LSE also is in the best position to ensure that it has appropriate contractual provisions (or Tariff provisions if the LSE is a regulated utility or a municipality or cooperative) to hold the Large Load financially responsible for the cost and credit implications of the RBP. *[If the Large Load is not yet working with an LSE to address the energy and capacity needs of that Large Load, query whether that load is “real” and the appropriateness of including it in the procurement target.]* Alternatively, for purposes of RBP, it may be appropriate for the Large Load to take on the RBP responsibility directly. Either the LSE or Large Load directly playing this role would allow the RBP and RPM costs to net and mitigate potential double billing risk.

Procurement Target Proposal

EKPC proposes that PJM establish a registry whereby a Large Load or the LSE serving that Large Load indicates (1) the Large Load MW assigned to that specific LSE and (2) what amount of that Large Load obligation will be satisfied by new resources under development and not yet committed in PJM’s capacity market. PJM can utilize a confidential process to receive any necessary documentation to support the information provided. This process would enable the tracking of the development of new capacity resources tied to the Large Load for purposes of the yet to be developed “connect and manage” construct, which in turn would enable EDCs to understand which specific customers may be subject to “connect and manage.” To the extent that the Large Load or

the LSE serving that Large Load indicates that it wishes to be subject to “connect and manage” and not have any BRP capacity secured for it, they would so indicate in the registry.

Based on the information reported in the registry (or Large Load directly if they desire), PJM would determine the procurement target and conduct the BRP.

(2) Settlement Mechanics – Holding the Cost-Causer Responsible

PJM would hold the LSEs identified in the registry responsible for credit requirements associated with the conduct of the RBP as well as the financial settlements in the Delivery Years associated with RBP committed resources (MW quantity, not necessarily specific resources) associated with Large Loads they serve. PJM, therefore, will charge appropriate LSE (or Large Load if they desire) for any costs and credit obligations associated with the RBP. In turn, those LSEs are able to use their tariffs (if regulated utility) or contracts (if non-utility) to ensure that the Large Loads are allocated these costs and no other end-consumers are charged for costs associated with the RBP. To facilitate this billing, LSEs may at their election seek to set up sub-accounts in PJM’s settlement system to separate wholesale billing associated with serving large loads from serving other load in a zone.

As noted above, to the extent any Large Load who is not its own LSE (as may be appropriate under state law) desires to enter into a contractual obligation directly with PJM for the credit responsibility and costs associated with the RBP, PJM could consider establishing a special category of Member for this limited purpose. EKPC has not done an analysis of the legalities or feasibility of this suggestion but notes it to the extent there is any desire of Large Loads to directly manage the credit and financial obligations associated with the RBP as this is a new construct with a multi-year commitment unlike any other PJM administered market mechanism.

EKPC’s proposal ensures that the most accurate procurement target is utilized and the correct loads pay the cost of any RBP because the LSE that is responsible under retail tariff or contract for supplying the capacity needs of the Large Load (or the Large Load itself) is the entity PJM will hold accountable for that load.

Settlements Mechanics

Since the LSEs identify the procurement target with an understanding of which Large Loads are comprising it for each Delivery Year covered by the RBP, the MW quantity would be fixed for each Delivery Year based on a pro-ration of the MWs committed in the RBP on-line in those Delivery Years.

The LSE would be held financially responsible for that quantity for each Delivery Year regardless of the PLC of the load it is serving that Delivery Year. The RBP financial settlement would be separate from RPM settlement, but ultimately needs to net to ensure that an LSE does not double pay for load represented in both the RBP and RPM.

PJM could provide a mechanism for LSEs to transfer this responsibility to other LSEs in situations where the Large Load seeks to switch suppliers, or if some Large Loads do not grow as fast as forecasted and others grow faster than forecasted. It would be expected that PJM place appropriate credit requirements on any such transfers. Of course, if the Large Load were to directly take on the RBP obligation, the obligation would track with it as it may change LSEs over time.

Appendix: Overview and Observations from PJM's State 1 CFP Proposal

PJM's proposal assigns procurement target setting, contractual commitments, and cost-recovery and credit assurance obligations to EDCs, not the LSEs who hold those obligations under the existing wholesale and retail constructs. This misalignment is particularly problematic in retail choice states, where EDCs provide wires service only and large loads are customers of competitive LSEs.

This misalignment raises concerns about the construct's legal durability, which could impact the interest of the supply community's participation in the auction. This misalignment also increases the risk of defaults occurring should the downstream adjustments in state law necessary for this proposal to be successful -- to allow the EDC to collect funds and handle the credit assurance responsibilities -- not timely occur (or not occur at all). Defaults, of course, impact all LSEs in PJM -- those whose load was part of the RBP and those whose load was not.

The proposal is fundamentally inconsistent with the current PJM construct

1. Procurement authority is separated from capacity obligation

Under RPM, the LSE, the entity responsible for supplying the energy and capacity needs of the load, bears the capacity obligation and settlement risk. By contrast, the RBP proposal contemplates procurement by EDCs, which neither select nor control the supply portfolios of datacenter customers and other large loads. Only an EDC that is also an LSE plays this role. This breaks the established causation chain linking load growth to the entity responsible for supplying the capacity needs of that load.

2. EDCs are positioned as contract counterparties without a tariff role

Because EDCs are not RAA signatories and are not recognized capacity market participants, long-term backstop contracts held by EDCs would seem to exist outside the tariff framework that governs capacity performance, enforcement, and remedies under RPM.

3. Cost allocation through EDCs bypasses LSE-level settlement logic

In retail choice states, large loads may be served by competitive suppliers or self-supplied (if the state allows the load to be its own LSE). Assigning costs through EDCs risks socializing capacity costs across unrelated default service customers, even where the incremental capacity need was caused by a specific LSE's decision to serve a large load customer. In contrast, RPM billing relies upon PLC determinants for load tagged to the appropriate LSE.

4. Retail choice states are disproportionately disrupted

In vertically integrated states where the EDC and LSE are the same entity, one might assume the issues are muted. However, PJM's proposal requires the creation of a new charge not envisioned by an EDC tariff and/or contract. All 14 retail jurisdictions in PJM would need to make significant regulatory adjustments which may, in certain instances, require statutory authorization. In retail choice jurisdictions the proposal effectively re-regulates procurement through a wires entity (delivery service entity), undermining competitive supply and reallocating risk away from market participants who caused the capacity need.