Reliability Backstop Auction Initial Proposal

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Goals

The Reliability Backstop Auction (RBA) has two overarching design goals:

- Address resource adequacy shortfalls
- Protect ratepayers

Every aspect of this proposal is designed around those two goals.

Resource Adequacy

Success of the RBA will be measured by how much capacity goes into service how soon. This has several implications.

- Must be attractive for developers
- Must be attractive for buyers.
  - For large loads, RBA is a path out of connect-and-manage.
  - For native load, RBA is a tool to preserve adequate reserve margins.
- Flexible on timing. Projects that can be built quickly are especially valuable, but financial guarantees are especially import for projects with longer build times.
- Must addresses reasons projects are not getting built.
  - High prices **and** powerful incentives for on time delivery address issues under developers' control.
  - PJM has said repeatedly and often that the queues are now working.
  - Network upgrade times and cost are major causes of dropouts.
  - RRI projects so far are suffering at about the same rate as others

The last three points argue that **a new fast track will not help us**. Rather, the RBA should focus on post-queue barriers that are under PJM's control.

Ratepayer Protection

The RBA must protect ratepayers from:

- Direct costs associated with new supply to serve large loads
- The risk of stranded assets or private defaults.

But that is not enough. Because the capacity market is now past VRR Point A, capacity prices will only go down if the RBA also includes a way to bring on new supply to serve native load, not just new large loads.

- PJM should never assign costs for RBA transactions to non-participating load. Entities with captive ratepayers that purchase capacity in the RBA may allocate costs to load as approved by their regulators.
- The RBA should not transfer forecast or project risk to the public through PJM.
- Capacity procured through RBA must flow into RPM.
- RBA should also allow buyers to procure capacity for native load growth.

Proposed Auction Structure

Our proposed Reliability Backstop Auction (RBA) is…

- between voluntary buyers and sellers, including large loads (and the LSEs who love them) and entities acting on behalf of native load;
- a risk pool for those voluntary buyers and sellers;
- open to any technologies that can deliver new UCAP;
- for locational capacity that feeds into RPM;
- an off ramp from connect-and-manage for loads;
- **not another fast track.** Works with existing queue cycles; and
- cleared and settled by PJM.

Buyers and Sellers

To protect ratepayers, the RBA will match voluntary buyers and sellers.

- PJM will not purchase capacity.
- Procurement target is simply the amount of buy bids placed in the auction.
- We are specifically proposing that PJM **not** take on responsibility for long-term resource adequacy planning. Rather, this auction becomes a tool for other parties to support long-term resource adequacy.
- Sellers: Any supplier of *new* UCAP (defined on slide 15)
- Buyers: Any PJM member eligible to purchase capacity in an Incremental Auction or bilateral transaction. Likely buyers include, but are not limited to:

  Large Loads, to secure capacity and exit connect-and-manage status

  Competitive LSEs, to be able to offer firm service to future customers

Timing

While the Governors' letter called for an auction in September, that may not be optimal.

- There is no opportunity for new supply that is not already in the queue. A September auction will still be mostly for a supply stack from 2020.
- Only new information will be that TC2 will have passed Decision Point II, but a September auction will be too late to inform drop/stay decisions.
- A September 2026 RBA ends up being little more than RRI 2.

We propose that the RBA be held during the Final Agreement phase of every queue cycle, after PJM has issued GIAs but before the signing deadline.

- First RBA would be held in December 2026 or January 2027, only a few months after the Governors' request.
- Supply offering into the RBA would know their interconnection timeline and costs. Interconnection costs can be reflected in RBA offers. This is huge, and probably the single biggest factor that could make the RBA a success.
- The RBA becomes a consistent, market-based, non-discriminatory way for developers to make new entry decisions.

Product

The RBA will procure UCAP by LDA for a forward period of 10-15 years.

- Auction must be zonal, same as RPM. That raises deliverability issues: the RBA needs to respect CETL, but shouldn't consume all the import capacity into and LDA and force BRAs to bind. We propose that the RBA can use transfer capability:
    - For years in which the BRA has not taken place, until remaining CETL is 1.15 * CETO + 1 MW. i.e., until just before the point where an LDA is treated as possibly separating in RPM.
    - For years in which the BRA has taken place, all available CETL.
- Constraints identified in the RBS could inform LTRTP.

Term

The RBA will procure UCAP by LDA for a forward period of 10-15 years.

- Both bids and offers can have a variable starting date. This raises questions about how to clear the auction, but it should be doable—less complex than clearing the day ahead market.
  - Different types of supply take vastly different times to come on-line, and we see no other way to allow all technologies to compete.
  - Capacity is needed beginning less than a year after the first RBA. The auction needs to be able to procure capacity that's available that soon without excluding resources that take longer to build.
  - Load needs vary over time, and buyers should be able to purchase what they need.
- Open question on end date of contracts:
  - Fixed end date makes clearing simpler and might not disadvantage load.
  - Variable end date recognizes benefits of projects that need shorter guaranteed funding and moves capacity back to RPM sooner.

Interface with RPM

Existing RPM auctions remain the primary short-term resource adequacy mechanism, and the RBA will feed into that.

- All capacity that clears the RBA will be required to offer into every RPM auction for its term as a self-scheduled resource. This implies that RBA suppliers will take on full RPM risk exposure for every year they have cleared. That is intentional.
- This corresponds to the Board's CIFP decision that all loads will remain in RPM. If the loads are in RPM, supply procured to serve them needs to be also.
- RPM revenues for RBA resources will flow to RBA buyers, similar to Auction Specific MW Transactions.
- RPM deficiency penalties flow to RBA buyers. Open question how to treat other RPM penalties/bonuses.
- Once the RBA commitment ends, suppliers take on an RPM must-offer obligation in the normal way.

We urge the board to reconsider their decision that all loads are reflected in the VRR curve, at least while the RBA is in effect.

- As long as large loads remain in the BRA, actions taken to procure new capacity for native load growth will not provide price relief. Instead, prices will remain high until large loads have brought their own supply, essentially holding the public hostage to

Settlement and Risk Management

We envision a pool of money funded by RBA buyers and a pool of capacity supplied by RBA sellers.

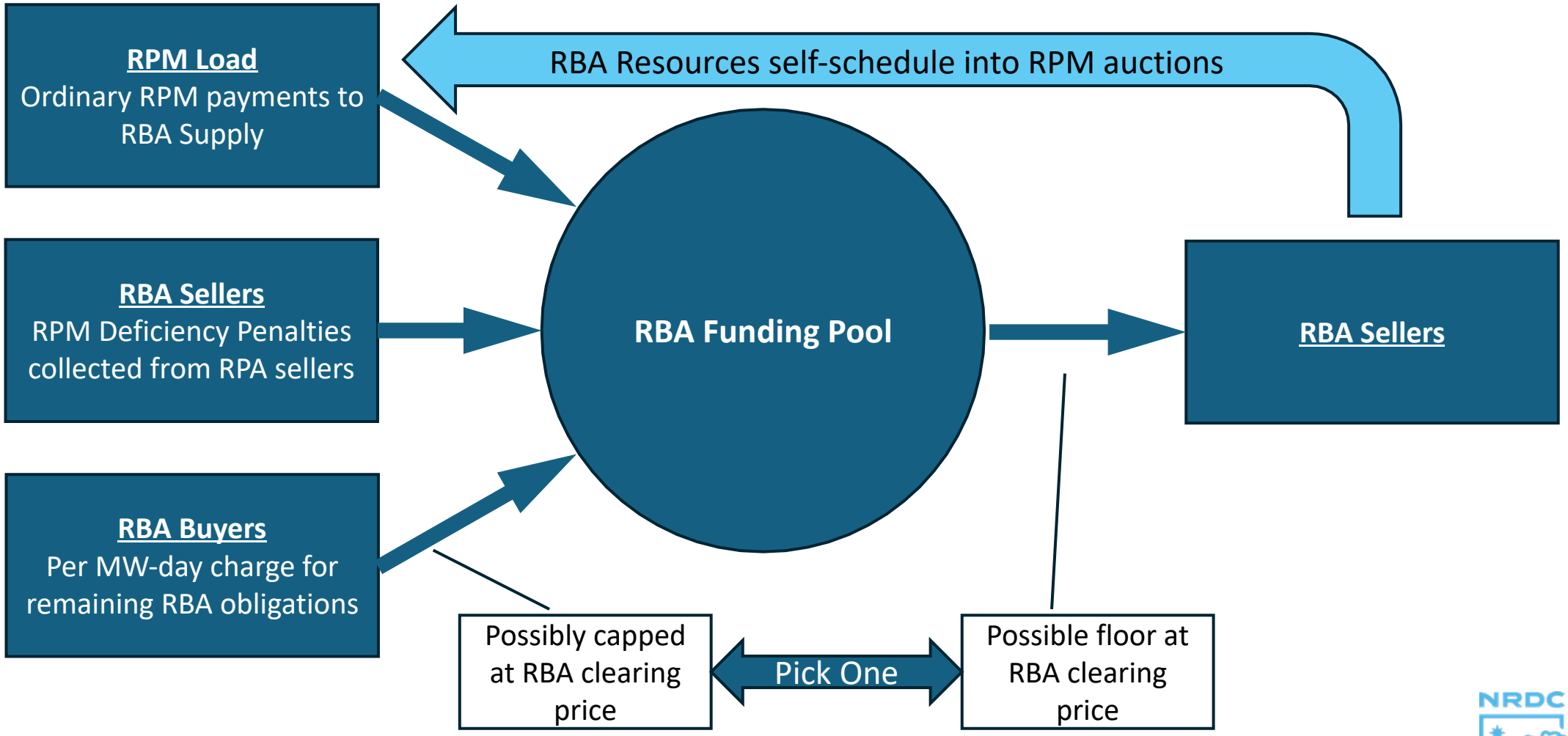
- Considered a "blind date bilateral" approach, but it raised problems:
  - Matching terms and quantities between buyers and sellers is difficult
  - Added too much random risk: if a party defaults, the consequences fall on one unlucky counterparty
- A pooled approach resolves those problems while protecting innocent bystanders. Details on next slide.
- Nothing here prevents buyers and settlers from entering into their own bilaterals outside of the RBA. That capacity would enter the BRA on normal terms, and should also provide an off-ramp from connect and manage for the buyer.

Settlement and Risk Management: Pooled Approach

We propose a risk pool for RBA buyers and sellers, similar in concept to how FTRs are funded.

- RBA sellers paid from a pool that is funded by RBA buyers, RPM payments, and RPM deficiency penalties.
- RBA costs allocated on a per-MW basis by zone using similar algorithms to RPM. This includes a version of CTRs if RBA zones separate.
- Two options if RBA is underfunded, e.g., if a buyer defaults:
  - Passed on to sellers as a lower per-MW payment
  - Passed on to remaining buyers as a higher per-MW cost
  - **Any other arrangement does not protect non-participating ratepayers**
- Options if RBA is undersupplied, e.g., seller defaults or underperformance:
  - Reduce capacity allocations to buyers, putting some of their load back into connect-and-manage
  - Allocate shortfall to the zone or sub-zonal LDA, increasing that

Settlement and Risk Management: Pooled Approach



Conclusion

In conclusion, we present a backstop auction design that we believe:

- Addresses most of the barriers to new entry in PJM
- Protects rate payers as completely as possible
- Provides clear paths for both capacity procurement for large load and enhanced long term resource adequacy planning.

The remaining slides provide details on a few specific issues.

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Appendix: New Supply

The following resources qualify as new:

- New construction generation or storage that has completed Phase III of a cycle or begun the SIS process but has not yet taken on an RPM must-offer requirement.
- Increased capacity from uprates. Open question if uprates need to have completed Phase III.
- Imports that have qualified to offer but have never cleared an RPM auction
- For C&I demand response, sites that do not register for any of the 2025/26 through 2027/28 delivery years, or any increase in capacity of sites that have registered.
- For mass market demand response programs, an increase in UCAP

Appendix: Avoided Retirements

We urge caution on 'avoided retirements' to avoid creating gaming opportunities. More philosophically, the RBA should be about the future, not the past. Possible criteria include:

- Existing resources with an IMM approved ACR higher than the top of the VRR curve
- Existing resources that have put in a deactivation request that can only be withdrawn if they clear an RBA

Offers from resources claiming 'avoided retirement' should be subject to additional conditions:

- Unlike other resources, their RBA offer prices should be subject to market mitigation.
- The term of RBA offers that include new investment should be mitigated by the IMM to ensure that they are no longer than needed to recover that investment.
- RBA offers that include operating costs but not new investment may be of any duration. However, there should be a process for early termination of RBA purchases from such units if it is determined that the unit is no

Appendix: ELCC Risk

We propose strict delivery terms with large penalties for non-delivery. This creates risk for resources subject to declining capacity value due to changes in ELCC.

For discussion, three possible ways of managing that risk:

- Leave it on the seller.
  - Provides maximum protection for load.
  - Only tenable if sellers can cure capacity deficiencies through bilaterals.
  - Should be paired with PJM commitment to eliminate any barriers to resources quickly and easily firming up their ELCC by adding storage or increasing the duration of existing storage.
- Lock in seller's ELCC rating.
  - Transfers risk to future new entrants.
  - Already rejected by FERC.
- Reduce delivered UCAP without penalty.
  - Obligation becomes "ICAP corresponding to first year UCAP", similar to Unit-Specific bilaterals for cleared capacity.
  - Transfers risk either to RBA buyers or load in general.