

170 FERC ¶ 61,256
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Neil Chatterjee, Chairman;
Richard Glick and Bernard L. McNamee.

PJM Interconnection, L.L.C.

Docket Nos. ER18-988-001
EL14-48-001
ER14-1461-002

ORDER DENYING REHEARING AND CLARIFICATION

(Issued March 26, 2020)

1. This order denies requests for rehearing and/or clarification of two Commission orders concerning Incremental Auctions in the PJM Interconnection, L.L.C. (PJM) capacity market: the Commission's May 8, 2018 Order in Docket Nos. ER18-988-000 and EL14-48-000,¹ and the Commission's May 9, 2014 Order in Docket Nos. ER14-1461-000, ER14-1461-001, and EL14-48-000.²
2. As summarized in detail in the May 2018 and May 2014 Orders, PJM filed proposals designed to discourage capacity market sellers from exploiting price differentials in PJM's Base Residual Auctions and Incremental Auctions.³ In PJM's view, consistent price differentials between PJM's Base Residual Auctions and Incremental Auctions may encourage some Capacity Market Sellers to obtain a capacity supply obligation in the Base Residual Auction, with the expectation that they will buy out of such obligations with lower-priced replacement capacity in subsequent Incremental Auctions, when PJM releases excess capacity.
3. As explained in the May 2018 Order, and as reaffirmed here, PJM failed to justify the Incremental Auction modifications that have been proposed. Moreover, in light of recent capacity market reforms and other changes in PJM markets, the Commission

¹ *PJM Interconnection, L.L.C.*, 163 FERC ¶ 61,101 (2018) (May 2018 Order).

² *PJM Interconnection, L.L.C.*, 147 FERC ¶ 61,108 (2014) (May 2014 Order).

³ *Id.* PP 3-7; *see also* May 2018 Order, 163 FERC ¶ 61,101 at PP 2-6.

upholds its decision to terminate the Federal Power Act (FPA) section 206⁴ proceeding in Docket No. EL14-48-000. As indicated below, although we deny rehearing based on the record presented here, we encourage PJM and stakeholders to continue to monitor the issues raised in this proceeding and to develop, if appropriate, solutions to address them.

I. Background

A. May 2014 Order

4. On March 10, 2014, as amended on March 14, 2014, PJM proposed an integrated package of tariff revisions to prohibit the submission of speculative sell offers in its capacity market auctions, i.e., offers not tied to an underlying physical capacity resource.⁵ PJM asserted that, under PJM market rules, a seller that obtained a capacity commitment in PJM's annual Base Residual Auction effectively can count on being able to buy out of that commitment in PJM's Incremental Auctions at a price lower than what it receives from the Base Residual Auction. PJM claimed that the ability to buy out at lower prices encourages sellers to submit in the Base Residual Auction speculative sell offers unsupported by physical resources.

5. To address this concern, PJM proposed, among other things: a "Replacement Capacity Adjustment Charge" on every replacement capacity transaction equal to the difference between the annual Base Residual Auction clearing price and the incremental auction price for any year in which the Base Residual Auction price is higher than the incremental auction price; a "sell-back floor" price for sales of excess capacity by PJM in incremental auctions equal to the relevant delivery year's Base Residual Auction clearing price; and new tariff language stating that every sell offer submitted into PJM's capacity auctions constitutes a legally binding representation by the seller that the offer contemplates physical delivery.⁶

6. The May 2014 Order recognized that offers submitted into PJM's capacity auctions should be tied to physical resources that will be available to PJM in the relevant delivery year.⁷ Nonetheless, the Commission found PJM's integrated package of revisions to be unjust and unreasonable, given the uncertain evidence presented by PJM on the issue of speculation and likely adverse market effects of PJM's proposed rule changes. Specifically, the Commission cited increased risks on sellers, undue barriers to

⁴ 16 U.S.C. § 824e (2012).

⁵ See May 2014 Order, 147 FERC ¶ 61,108 at PP 8-32.

⁶ See *id.*

⁷ *Id.* P 68.

entry, reduced opportunities for beneficial trade, and PJM's likely procurement of excess capacity.⁸ The May 2014 Order also found, however, that PJM's existing tariff may be unjust and unreasonable to the extent it fails to promote long-term reliability in PJM's capacity market by possibly permitting speculative sell offers in the PJM capacity market. Accordingly, the May 2014 Order instituted a proceeding under FPA section 206, in Docket No. EL14-48-000, and directed Commission staff to convene a technical conference to facilitate the development of a just and reasonable solution.

7. On August 18, 2014, PJM informed the Commission that it had convened a stakeholder process to consider a new, comprehensive package of reforms, i.e., the tariff revisions subsequently included in its Capacity Performance filing in Docket No. ER15-623-000, et al. Given these developments, PJM requested that the Commission hold any further action in Docket No. EL14-48-000 in abeyance, subject to the Commission's order on PJM's Capacity Performance filings.⁹ In subsequent notices, submitted October 29, 2015 and November 23, 2016, PJM renewed its request to defer action in Docket No. EL14-48-000, pending PJM's review and analysis of its initial incremental auction results under its Capacity Performance protocols. In its November 2016 report, PJM stated that, while it remained concerned that the issues set for a technical conference may still warrant tariff changes, the results of its September 12, 2016 Incremental Auction were not determinative, especially given the phased roll-out of PJM's Capacity Performance rule changes. No party filed an objection to PJM's informational filing.

B. May 2018 Order

8. Subsequently, on March 9, 2018, PJM again filed a package of proposed tariff revisions designed to address its Incremental Auction concerns. PJM's 2018 proposed revisions were similar in certain respects to its 2014 proposed revisions, but did not contain all of the components included in the 2014 proposal. For example, unlike the 2014 proposal, PJM's 2018 proposal did not contain a Replacement Capacity Adjustment Charge.¹⁰

⁸ *Id.*

⁹ On December 12, 2014, PJM submitted its Capacity Performance Filing, in Docket No. ER15-623-000, et al., proposing to establish a new capacity product, a Capacity Performance Resource, on a phased-in basis, and implement related energy market changes. *See PJM Interconnection, L.L.C.*, 151 FERC ¶ 61,208, at PP 41-42 (2015), *order on reh'g*, 155 FERC ¶ 61,157 (2016).

¹⁰ May 2018 Order, 163 FERC ¶ 61,101 at PP 10-12.

9. The Commission identified as problematic PJM's proposed sell-back offer floor, which was also a component of PJM's 2014 proposal.¹¹ As the Commission explained, prior to the Base Residual Auction, PJM establishes a downward sloping capacity demand curve, which reflects the relationship of the price of capacity to quantity, taking into account the amount of capacity that PJM anticipates it needs to meet its reliability targets. Based on updated reliability requirements due to revised load forecasts between the Base Residual Auction and the Incremental Auctions, PJM updates the capacity demand curve and, through the Incremental Auctions, either procures additional capacity, or more frequently, sells back excess capacity. In most cases, as PJM pointed out, PJM over-procures capacity in the Base Residual Auction, and the large amount of excess capacity offered in the Incremental Auction consistently drives the prices in those auctions to relatively low levels.¹²

10. In light of its concern that relatively low prices in Incremental Auctions could encourage speculative sell offers in the Base Residual Auctions, PJM proposed to submit sell-back offers in the Incremental Auctions at the relevant Base Residual Auction clearing price, without regard to the capacity demand curve.¹³

11. The Commission's May 2018 Order explained that, on three separate occasions (in 2009, 2014, and 2017), the Commission has rejected as unjust and unreasonable PJM's proposals to set a pre-determined price for its sales of excess capacity in the Incremental Auctions (rather than relying on PJM's capacity demand curve valuation).¹⁴ The Commission found PJM's 2018 proposal was likewise flawed because it was inconsistent with the principle that the value of a given amount of capacity changes when the reliability requirement changes, a concept reflected in PJM's updated capacity demand curve. Consistent with its precedent, the Commission rejected PJM's 2018 proposal to establish an artificial sell-back offer floor for excess capacity in the Incremental Auctions.

12. Because PJM submitted its 2018 Incremental Auction proposal as an integrated package of reforms, the Commission did not address other aspects of the proposal.¹⁵ In addition, the Commission explained that, upon consideration of the speculative behavior concerns articulated by PJM in the 2014 and 2018 proposals, it did not find PJM's

¹¹ *Id.* P 39.

¹² *Id.* P 38.

¹³ *Id.* P 37.

¹⁴ *Id.* P 43.

¹⁵ *Id.* PP 37-43.

position persuasive. Moreover, recent changes in PJM markets, including improved load forecasting, would further reduce the likelihood of speculative behavior. Accordingly, the Commission found that further consideration of potential solutions for the speculative behavior problem was unnecessary, and terminated the FPA section 206 proceeding in Docket No. EL 14-48-000.¹⁶

II. Requests for Clarification and Rehearing

13. PJM and the Indicated PJM Utilities Coalition (Utilities Coalition)¹⁷ seek rehearing or, in the alternative, clarification of the May 2014 Order. PJM seeks clarification that the May 2014 Order did not foreclose any element of PJM's filing from being adopted as a just and reasonable remedy, in response to the issues identified by the Commission in establishing a section 206 proceeding. In the alternative, PJM requests rehearing, arguing that, in the May 2014 Order, the Commission failed to establish that any individual element of PJM's filing was unjust and unreasonable and further erred in its conclusion that PJM had failed to support its claim regarding the occurrence of speculation in its capacity market.

14. The Utilities Coalition similarly argues that the May 2014 Order erred in summarily rejecting PJM's filing. The Utilities Coalition asserts that the Commission erred in its findings regarding the likely market impact of PJM's proposal. In the alternative, the Utilities Coalition seeks clarification that, by rejecting PJM's package of reforms as a whole, the Commission did not make any determination that any individual component of that package is unjust and unreasonable and that, accordingly, such components may be considered in the section 206 proceeding as possible solutions to existing tariff provisions that may be determined to be unjust and unreasonable.

15. PJM also seeks rehearing and clarification of the May 2018 Order. PJM argues that the Commission ignored the factual record in terminating the section 206 proceeding, and that termination is unsupported by substantial evidence.¹⁸ In addition, PJM requests clarification concerning the components of its 2018 Incremental Auction proposal not specifically addressed in the May 2018 Order, and/or alternative approaches to deterring speculative sell offers.¹⁹ PJM also asks the Commission to clarify that rejection of the

¹⁶ *Id.* PP 44-46.

¹⁷ American Electric Power Service Corporation, the Dayton Power & Light Company, and FirstEnergy Service Company, each on behalf of its affected affiliates, and Duke Energy Ohio, LLC and East Kentucky Power Cooperative, Inc.

¹⁸ PJM Rehearing Request at 3-6.

¹⁹ *Id.* at 7.

remaining components of PJM's 2018 proposal is without prejudice to PJM proposing a subsequent section 205 tariff revision directed to the same concerns.²⁰

16. Monitoring Analytics, LLC, in its capacity as the Independent Market Monitor for PJM (Market Monitor), likewise seeks rehearing and clarification of the May 2018 Order. The Market Monitor argues that the Commission should have accepted PJM's 2018 proposal.²¹ According to the Market Monitor, the Commission's decision was based on the erroneous finding that prices for capacity in a Base Residual Auction and an Incremental Auction for a given delivery year represent consistent equivalent values.²² The Market Monitor also argues that the section 206 proceeding should not have been terminated.²³ According to the Market Monitor, record evidence demonstrates that speculative activity is harming the efficiency of PJM markets.²⁴

17. PJM Power Providers Group and Exelon Corporation (P3 and Exelon) jointly also seek rehearing and clarification regarding the May 2018 Order. Specifically, P3 and Exelon challenge the Commission's decision to terminate the section 206 proceeding, and seek clarification from the Commission concerning components of PJM's 2018 filing not specifically addressed in the May 2018 Order.²⁵

III. Discussion

A. Termination of the Section 206 Proceeding

18. PJM, the Market Monitor, and P3 and Exelon seek rehearing concerning the termination of the section 206 proceeding in the May 2018 Order. We reaffirm the May 2018 Order and deny rehearing.

19. Based on the record in Docket No. ER18-988-000, in which the Commission rejected another set of potential revisions to the Incremental Auction process proposed by PJM, and other proceedings that have changed the Incremental Auction process in the

²⁰ *Id.* at 6.

²¹ Market Monitor Rehearing Request at 3-5.

²² *Id.*

²³ *Id.* at 5-9.

²⁴ *Id.*

²⁵ P3 and Exelon Rehearing Request at 8-19, 20-21.

interim, we see no reason to reverse our determination to terminate²⁶ the section 206 proceeding initiated in Docket No. EL14-48-000. The record evidence in this proceeding does not demonstrate a sufficient speculative behavior problem warranting continuation of the section 206 proceeding. As the May 2018 Order explained, PJM's evidence that numerous resources, in particular Demand Resources, seek to buy out of their Base Residual Auction commitments may not necessarily demonstrate that resources are engaging in speculative behavior.²⁷ Moreover, PJM has sought to ensure that Demand Resources do not engage in speculative behavior by proposing tariff revisions, accepted by the Commission in 2014, requiring Demand Resource providers to designate, prior to the Base Residual Auction, that Demand Resources will actually be available in the Delivery Year.²⁸

20. As explained in the May 2018 Order, other changes in PJM market conditions may help alleviate speculative behavior issues, to the extent they exist.²⁹ Under PJM's Capacity Performance construct, a resource that is unable to meet its share of system needs during a Performance Assessment Interval risks a large penalty.³⁰ This creates a substantial downside risk for would-be speculators or any market participant—a market participant that fails to buy out its capacity obligation in the incremental auction will face large non-performance penalties.

21. A cause of price differentials between the Base Residual Auction and incremental auctions is the overestimation of system needs in the Base Residual Auction.³¹ PJM revised its load forecasting methodology in 2015 in an effort to more accurately estimate load for a given delivery year, which should reduce over-procurements.³² In light of these developments, we see no reason to extend the section 206 proceeding while market

²⁶ May 2018 Order, 163 FERC ¶ 61,101 at P 46.

²⁷ *Id.* P 44; *see also* Market Monitor Rehearing Request at 6 n.8 and attachment (citing and attaching report concerning replacement rates of different resources).

²⁸ *See* May 2018 Order, 163 FERC ¶ 61,101 at P 45 (citing *PJM Interconnection, L.L.C.*, 146 FERC ¶ 61,150, at PP 1, 22 (2014)).

²⁹ May 2018 Order, 163 FERC ¶ 61,101 at P 45.

³⁰ *Id.* (citing *PJM Interconnection, L.L.C.*, 151 FERC ¶ 61,208 at P 158).

³¹ *See id.* P 38.

³² *Id.* P 45 & n.105.

conditions continue to evolve.³³ Accordingly, the Commission denies rehearing concerning termination of the FPA section 206 proceeding.

22. As the Commission stated in the May 2014 Order, we continue to recognize the need for PJM to ensure that offers into its market represent physical resources,³⁴ and we remain committed to addressing any demonstrated issues with speculative sell offers that may arise. Although we deny rehearing based on the record presented here, we encourage PJM and stakeholders to continue to monitor these issues and to develop, if appropriate, solutions consistent with the determinations in these orders or to make other appropriate filings with the Commission.

B. Sell-Back Offer Floor

23. The Market Monitor requests rehearing concerning the Commission's rejection of the 2018 Incremental Auction proposal. We deny rehearing because, as explained in the May 2018 Order, PJM has not shown that it is just and reasonable to set an artificial floor for sales of excess capacity in the Incremental Auctions.³⁵ As previously explained, the capacity demand curve represents a just and reasonable approximation of the value of excess capacity to load, and on three prior occasions, the Commission has rejected PJM proposals to set Incremental Auction sell-back offer prices without reference to the capacity demand curve. The record in this proceeding does not warrant a different result.³⁶

24. The Market Monitor argues that the May 2018 Order rests on the erroneous premise that prices for capacity formed in Base Residual Auctions and prices for capacity exchanged in Incremental Auctions represent equivalent values. According to the Market Monitor, Base Residual Auction capacity prices and Incremental Auction capacity prices

³³ The Commission has discretion, particularly for proceedings which it has initiated, in determining whether to terminate proceedings instituted under section 206. *See Wisconsin v. FPC*, 373 U.S. 294, 311 (1963) (finding the Commission did not abuse its discretion in terminating an investigation where "the Commission concluded that the record, relating to the test year 1954, was too stale in 1960 to permit a finding as to the justness and reasonableness of . . . current rates").

³⁴ May 2014 Order, 147 FERC ¶ 61,108 at P 68.

³⁵ *Id.* PP 37, 43.

³⁶ *Id.* PP 37-43.

“do not have a common economic basis and cannot be compared as though differences in price reflect changes in the general value of capacity.”³⁷

25. The Market Monitor’s argument is unpersuasive. The capacity offered in PJM Base Residual Auctions is the same product offered in PJM Incremental Auctions. Capacity prices in the Base Residual Auctions are formed by reference to a downward sloping demand curve reflecting the value of the capacity that PJM anticipates it needs to meet its reliability targets. After a given Base Residual Auction takes place, updated load forecasts may result in updated reliability requirements and an updated capacity demand curve. It is just and reasonable for prices in a given Incremental Auction to reflect these changes.

26. The Market Monitor argues that PJM has demonstrated that there is value to holding extra capacity that is not captured in the sell offer values based on the Variable Resource Requirement curve, and this uncaptured value is realized when capacity resources offer into the PJM Day-Ahead Energy Market. The Market Monitor thus contends that the Base Residual Auction price represents a lower bound on the value of excess capacity.³⁸ The Market Monitor’s argument appears to be based on the premise that buying extra capacity results in energy market price reductions that are greater than the cost of the capacity, i.e., that the economic value of capacity exceeds the reliability value of capacity. This argument appears inconsistent with the foundational premise of PJM’s capacity market demand curve, which is based on the full reliability value of capacity. To the extent any party believes that the premise underlying the demand curve should be changed, they may initiate a new proceeding.

27. In any event, as noted in the May 2018 Order, we do not find it advisable to design a market on the assumption that over-procurement in capacity auctions will result in lower energy market prices. Each market ought to be designed properly.³⁹

28. P3 and Exelon seek clarification concerning aspects of PJM’s 2018 Incremental Auction proposal apart from the sell-back offer floor.⁴⁰ As the Commission explained in the May 2018 Order, PJM submitted the 2018 Incremental Auction proposal as a package

³⁷ Market Monitor Rehearing Request at 3-5.

³⁸ *Id.*

³⁹ May 2018 Order, 163 FERC ¶ 61,101 at P 43 & n.101.

⁴⁰ P3 and Exelon Request for Rehearing at 20-21.

of reforms, and thus, we decline to address every component of the proposal.⁴¹ Absence of discussion on any component of the proposal, however, is not an indication of how the Commission would rule on the merits of those components, if submitted in a future proceeding. Accordingly, we deny clarification.

29. In light of our disposition of PJM's 2018 Incremental Auction proposal, we deny the requests for rehearing and clarification of the May 2014 Order.

The Commission orders:

(A) The requests for rehearing and clarification of the May 2018 Order are hereby denied, as discussed in the body of this order.

(B) The requests for rehearing and clarification of the May 2014 Order are hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

⁴¹ See May 2018 Order, 163 FERC ¶ 61,101 at P 43; see also *NRG Power Mktg., LLC v. FERC*, 862 F.3d 108, 114-15 (D.C. Cir. 2017) (Commission may accept or reject a proposal under section 205 of the Federal Power Act, but may not make changes to the proposal "without the consent of the utility"); *City of Winnfield v. FERC*, 744 F.2d 871, 876 (D.C. Cir. 1984) (same).