

May 17, 2023

VIA ELECTRONIC MAIL

The PJM Board of Managers
c/o Mark Takahashi, Chair, PJM Board of Managers
PJM Interconnection, L.L.C.
2750 Monroe Boulevard
Audubon, Pennsylvania 19408

Re: Stakeholder Efforts to Undermine PJM's Capacity Performance Framework

Dear Chairman Takahashi and PJM Board of Managers:

The undersigned Members urge PJM to exercise its independent judgement and not file retroactive changes to the capacity market rules, including modification to the capacity penalty rate, penalty stop-loss, and penalty triggers (collectively, the "Proposed Penalty Reductions"), which the PJM Members Committee endorsed on May 11, 2023. The Proposed Penalty Reductions would significantly change the risk of Capacity Performance commitments for the 2023/24 and 2024/25 Delivery Years to the detriment of system reliability, market stability, and investor expectations. The Proposed Penalty Reductions will also provide customers with less performance assurance than they paid for, discriminate against market participants who have followed and reasonably relied on the PJM rules, and instigate litigation over two more Delivery Year auctions. Litigation over the Proposed Penalty Reductions will distract from the important capacity market reform tasks that the Board has directed PJM and stakeholders to undertake and could undermine chances for successful holistic reform.

PJM has the sole discretion and responsibility to only file Tariff revisions with the Federal Energy Regulatory Commission ("FERC") that are just, reasonable, and not unduly discriminatory in support of PJM's reliability mandate (with very limited exceptions related to matters reserved to the Transmission Owners, which are not at issue here). PJM has exclusive Section 205 filing rights over Attachment DD of the PJM Tariff.¹ PJM, as the reliability coordinator, alone has both the independent authority and responsibility to maintain reliability.² PJM has no obligation under its governing documents to make the Proposed Penalty Reductions filing. While stakeholder support may serve as an important factor in developing tariff reforms it is not dispositive. PJM's filing rights under Attachment DD do not require that it file a stakeholder-supported proposal. Rather, PJM should only make the choice to submit tariff revisions if it determines that, based on substantial evidence, it is able to demonstrate that those proposed revisions are just and reasonable and not unduly discriminatory, as it is required to do under the Federal Power Act and the PJM governing documents.

Given that PJM staff has explicitly expressed concerns regarding core elements of the Proposed Penalty Reductions, we urge the Board to exercise PJM's independent judgment and not file these proposed tariff revisions. There is simply no justification for submitting Proposed Penalty Reductions that PJM staff has publicly opposed. Indeed, PJM staff has criticized core elements of the Proposed Penalty

¹ PJM Tariff Section 9.2 ("PJM shall have the *exclusive and unilateral right to file* pursuant to Section 205 of the Federal Power Act and the FERC's rules and regulations thereunder to make changes in or relating to the terms and conditions of the PJM Tariff (including but not limited to provisions relating to creditworthiness, billing, and defaults) as well as all charges for recovery of PJM costs.") (emphasis added).

² Unlike the situation regarding End-of-Life transmission planning, which addressed stakeholder endorsed changes to the Operating Agreement, the present revisions concern Attachment DD of the Tariff where PJM's discretion is even clearer.

Reductions, calling into question whether the proposed reforms would severely diminish incentives for generator performance to a degree that threatens reliability. The undersigned Members agree with PJM that reducing penalties tenfold in the wake of underperformance during Winter Storm Elliott is contrary to ensuring reliability.³ Moreover, proposing revisions for Delivery Years for previously-cleared auctions undermines the settled expectations of market participants and contravenes the filed rate doctrine, placing into question the revisions' legality and inviting litigation and additional uncertainty. When the transition to the Capacity Performance product was effectuated in 2015, PJM and the FERC did not simply revise existing capacity supply obligations *via* regulatory fiat; instead, new auctions were run for Delivery Years 2016/2017 and 2017/2018 to reflect the change in product obligations. PJM should not file the Proposed Penalty Reductions.⁴ Functioning markets depend on certainty, including certainty that the terms of an obligation will not be rewritten after the fact.

In the wake of generator underperformance during the 2014 Polar Vortex, PJM proposed, the IMM supported, and the FERC accepted PJM's Capacity Performance framework to "ensure that resources committed as capacity to meet PJM's reliability needs will deliver the promised energy and reserves when called upon in emergencies."⁵ To provide adequate incentives for performance during emergencies, PJM imposed a carrot-and-stick approach, penalizing resources that failed to perform, and rewarding those that exceeded expectations. The Proposed Penalty Reductions severely mute the incentives of that framework resulting in capacity market incentives similar to those in place prior to the 2014 Polar Vortex events.

The Proposed Penalty Reductions would undermine reliability in the region at a time when more frequent weather extremes and diminishing capacity margins make it more important than ever that resources satisfy their capacity commitments. Until Winter Storm Elliott, the performance obligations that came with those capacity payments were largely untested as PJM's operators rarely had to take emergency actions. As was witnessed, the capacity market design provided PJM operators with sufficient resources to maintain system reliability. Capacity suppliers bore the risk of their performance commitment and the lights stayed on. However, as a result of Winter Storm Elliott and the penalties assessed to generators for failure to perform, some stakeholders are now seeking to shift resource performance risk back to retail and wholesale suppliers and customers who have little ability to manage that risk. Incredibly, the Proposed Penalty Reductions would reduce incentives below those that were in place during Winter Storm Elliott. In the rush to mute their performance obligations, the proponents of the Proposed Penalty Reductions have not provided any information or support to justify these changes, particularly their impact on reliability, instead focusing on how much they can lower the penalty and stop loss limit and dull the incentives for performance. Fortunately, PJM staff has appropriately been focused on the need for strong performance incentives and has expressed concern regarding the potential negative impact of these changes.

Given the dearth of information on the reliability impact—and with the knowledge that the current framework helped keep the lights on during Winter Storm Elliott—rather than supporting the Proposed Penalty Reductions, the Board should be sending a strong message to resource owners to invest in improvements that will ensure they can perform when needed. Such improvements might include

³ Given zones had different clearing prices in the already-cleared 2023/24 and 2024/25 auctions, basing penalties on auction clearing prices could also create discrepancies in penalty and bonus payment rates depending on where the capacity is located.

⁴ To the extent the Board believes the any elements of the Proposed Penalty Reductions should be considered on a prospective basis as part of comprehensive changes to PJM's Capacity Performance construct, the Board could add that to the work already underway in the Critical Issue Fast Path process.

⁵ *PJM Interconnection, L.L.C.*, 151 FERC ¶ 61,280, at P 8 (2015).

firming fuel supplies, upgrading equipment to improve start times, weather-hardening resources, hedging risk through transactions with more reliable resources, all of which were responses Capacity Performance was intended to motivate. Resource owners routinely evaluate the risks of penalties for non-performance against the costs of such reliability improvements and invest accordingly. Indeed, based on experience during Winter Storm Elliott, some of the undersigned have taken actions to ensure they will perform during future weather extremes; others hedged their risk of non-performance by buying back capacity in the most recent Incremental Auction, often at a cost far exceeding their capacity market revenues. Changing the rules now would punish these resource owners who prudently manage their resources' non-performance risk. Upending capacity market rules after the auctions have been run and commercial decisions have been made undermines the incentives a forward-looking market is designed to promote. More importantly, it devalues investments and actions resources have undertaken to improve their reliability and calls into question whether similar investments or actions will be made in the future.

Certain stakeholder support for the proposed retroactive rule changes appears to come from an unfounded concern that some resources will be forced into default if they are subject to Capacity Performance penalty rules. To date, few resources have actually defaulted.⁶ PJM already has implemented changes to its market rules in response to these concerns, allowing for flexibility to retain resources that are in default⁷ and extending the time over which resource owners can repay non-performance penalties to reduce financial stress.⁸ And, as PJM knows, resources in default (and even bankruptcy) are able to continue to participate in the PJM markets. Indeed, if a unit requires better management or incremental investment, then it will likely be sold to another owner that can more effectively manage the risk of a capacity market commitment. Decisions to retire resources that are financially challenged due to underperformance will depend on the likelihood of profitability in the future. Thus, PJM's focus on the upcoming Critical Issue Fast Path process to comprehensively reform the capacity market is the most productive path to addressing the overstated concern about existing resources' financial viability.

The Board's direction to PJM in the February 2023 letter was clear: use the Critical Issue Fast Path process to consider comprehensive reform to PJM capacity markets to ensure that next time there is an event like Winter Storm Elliott, the PJM market will be better prepared. In fact, the Board stated that during Winter Storm Elliot, the "system was stressed," and emphasized the "need to focus on PJM's rules and processes to ensure reliability is maintained both now and during the transition." While the Board requested a *delay* in the next auction to put new rules in place as soon as possible, it *did not* authorize PJM to make rule changes retroactively for the simple reason that this would be unlawful under the Federal Power Act.⁹ Significant changes such as those embodied in the Proposed Penalty Reductions that would change obligations for a Delivery Year starting in less than a month should not be rushed through

⁶ Risk Management Committee, *PJM Presentation on Performance Assessment Interval (PAI) Penalties*, at 9 (Apr. 23, 2023)

⁷ *PJM Interconnection, L.L.C.*, 183 FERC ¶ 61,010 (2023).

⁸ *Id.*

⁹ See [FAX COVER \(pjm.com\)](https://www.pjm.com) at 3 ("The Board is also considering whether the aforementioned capacity market enhancements should apply to auctions earlier than the 2027/2028 Base Residual Auction as targeted by the RASTF Issue Charge. The Board recognizes that this may require a delay to future auctions and has therefore directed PJM to put together possible alternative auction schedules and discuss them with stakeholders for feedback.")

the stakeholder process as a one-off when the Critical Issue Fast Path process is in place to consider comprehensive changes.¹⁰

For the foregoing reasons, the undersigned Members respectfully ask that the Board direct PJM to not file any changes to the Capacity Performance framework that PJM cannot demonstrate are just and reasonable and not unduly discriminatory. As noted above, PJM staff members have expressed significant concerns regarding the Proposed Penalty Reductions' ability to incent performance when PJM's system is most stressed. Moreover, the Proposed Penalty Reductions upend the settled expectations of market participants by changing the rules for already cleared Delivery Years with little to no notice and no opportunity to adjust capacity supply obligations. The Board should direct PJM to exercise its Section 205 filing rights under Attachment DD only if it believes it can demonstrate with evidence that the proposed revisions are just, reasonable, not unduly discriminatory, and are consistent with system reliability, which is PJM's core responsibility. For these reasons, we urge the Board to conclude that PJM should exercise its discretion and not file any element of the Proposed Penalty Reductions.

We appreciate the Board's steadfast commitment to commercial and legal reliance, cost-effective markets, independence, and, most importantly, ensuring reliability. We respectfully request that the Board exercise that independence and not file any portion of the Proposed Penalty Reductions that is not just and reasonable or is unduly discriminatory or that has an adverse impact on reliability.

We appreciate your consideration of this request and await your response.

Respectfully,

Avangrid Renewables, LLC

Calpine Energy Services, L.P.

Constellation Energy Generation, LLC

Duquesne Light Company

Exelon Business Services Company, LLC on behalf of Atlantic City Electric Company, Baltimore Gas and Electric Company, Commonwealth Edison Company, Delmarva Power & Light Company, PECO Energy Company, and Potomac Electric Power Company

NextEra Energy Resources

PPL Electric Utilities Corp.

Public Service Electric and Gas Company and PSEG Power LLC

Vistra Corp.

Vitol Inc.

¹⁰ If the Proposed Penalty Reductions are indeed needed, stakeholders should be given a meaningful opportunity to understand the individual elements and how these mechanisms work in conjunction (or not) with other Capacity Performance elements to ensure reliability. Unfortunately, the Proposed Penalty Reductions were rushed through the stakeholder process with insufficient time to consider the full ramifications of the changes themselves, let alone enough time to consider how they fit in with the broader market rule changes being considered in the Critical Issue Fast Path process.