THE P3 GROUP

Comments of the PJM Power Providers Group (P3)[1] on the Capacity Market Critical Issues Fast Path Process

As an initial matter, P3 thanks the Board for convening the CIFP to begin to address the challenges facing PJM's Capacity Markets. In starting the CIFP process, the Board appropriately recognized that PJM has a looming reliability problem driven by accelerated retirements of resources that are needed to maintain reliability, and tepid new entry that is not of the quality and quantity necessary to replace those resources that are retiring. Given this troubling reality, the Board was right to observe that, "near-term changes to the Reliability Pricing Model (RPM) are necessary to ensure that PJM can maintain resource adequacy into the future."

As P3 informed the Board in its March 7th letter, the organization believes that the capacity market is the single most important tool available to ensure PJM has sufficient capacity and the lowest cost. The capacity market has proven that it can drive investment in new resources and facilitate the retirement of less efficient resources if structured properly. P3 believes that the core elements of the capacity construct are solid – forward commitment, sloping demand curve, locational delivery areas, penalties for non-performance and bonuses for over performance. However, while the general structure is solid, the capacity market is currently in an unsustainable spot due to parameters that have been placed around these core elements.

Reserve margins are projected to deteriorate at an alarming pace while the capacity market continues to send signals that even more resources should retire. The last three capacity auctions cleared at $50, $34 and $28. Those prices are clear signals to resources in the market to retire and to those looking to enter the market a flashing "do not enter" sign unless your resource has an out of market revenue stream. The current queue which is dominated by subsidized (and intermittent) wind and solar is reflective of that reality. Investment in PJM is almost exclusively being driven by subsidies because the markets are not structured for success.

Clearly significant change is needed, but, unfortunately, the PJM proposal is at best an incremental improvement that falls far short of the change that is required to turn capacity markets into the reliability sustaining mechanism that it is capable of being. The PJM proposal addresses half of the issues that the PJM Board specifically asked be addressed (risk modeling and accreditation) while leaving the FRR and the Market Mitigation issues incomplete.

[1] P3 is a non-profit organization dedicated to advancing federal, state and regional policies that promote properly designed and well-functioning electricity markets in the PJM Interconnection, L.L.C. ("PJM") region. Combined, P3 members own over 87,000 MWs of generation assets and produce enough power to supply over 63 million homes in the PJM region covering 13 states and the District of Columbia. The comments contained herein represent the position of P3 as an organization, but not necessarily the views of any particular member with respect to any issue. For more information on P3, visit www.p3powergroup.com.

The biggest single flaw in the PJM proposal is the lack of meaningful changes to the market power mitigation provisions. The Board needs to thoughtfully consider the current state of market power mitigation in PJM. In the PJM market, seller market power is "mitigated" by requiring every single capacity supplier to have its costs, forward revenues and risks evaluated by both PJM and the IMM. Meanwhile, buyer market power is "mitigated" with a MOPR about which the PJM IMM has said, "PJM markets would be better off, more competitive, and more efficient with no MOPR." The lack of a balanced approach to mitigation is not sustainable if the capacity markets are to succeed.

Capacity market reforms will be largely symbolic unless those entities that have invested billions of dollars in PJM's markets can reflect their views of costs, forward revenues, and risks in the pricing of their product in the PJM market. Although it attempts to provide additional clarifications on the calculation of CPQR, the PJM proposal continues the world in which every seller, regardless of that seller's ability to exercise market power, must engage in an annual debate with both PJM and the IMM over how much it costs to provide capacity, how much future energy revenues that resource will garner and what is that resource's risk that it will face potentially crippling fines. What rational investor would be attracted to such a market? The current PJM queue provides a clear answer – subsidized resources that do not have a must offer obligation.

Absent the ability for resource owners to reflect their estimation of operational risk under capacity performance, and the ability to reflect uncertainty of energy and ancillary service revenues in capacity market, many of the other reforms that PJM is suggesting will not have their desired effect. The PJM markets need to send a signal that investment in its markets is attractive. Unnecessary and burdensome market power mitigation sends the opposite signal. Mitigation must change and the PJM proposal comes up short in that regard.

Beyond the mitigation issue, P3 offers the following thoughts on other aspects of the PJM proposal:

- **Seasonal Capacity** – P3 supports PJM's "second option" which allows for continued discussion of a seasonal capacity construct. P3 recognizes the different reliability challenges facing the grid in the winter and summer and is open to addressing those challenges in a seasonal construct – provided it is set up the right way and allows needed "one season" resources to recover their costs and risks.

- **Accreditation –** P3 supports PJM's efforts to put in place a more granular level of accreditation that specifically reflects the ability of individual capacity resources to contribute to reliability. It is important that the accreditation be fair and transparent allowing PJM and the resource owner to develop an agreeable capacity accreditation prior to the auction.

- **Penalties/Bonuses** – The CP penalties and bonus conversation is directly tied to the market mitigation issue. Until PJM and FERC address the mitigation issue, it will be very difficult to address the appropriate level of penalties and bonuses. P3 supports the ability of suppliers to transfer compliance obligations provided the appropriate parameters are placed around this activity. Additionally, P3 does not believe that bonus payments should be limited to "committed" capacity as proposed by PJM.

- **Risk Modelling** – P3 supports the PJM proposal.

- **Generator Testing** – P3 supports testing so long as revenue "clawbacks" are reasonable.

- **FRR** – The Board charged PJM with developing "FRR rules to ensure that supply resources and consumers are held to comparable standards." P3 does not believe that the PJM proposal meets this standard.

How should the Board move forward?

Considering the comments above, P3 respectfully submits the following recommendations to the Board on the actions it can take following the August 23rd meeting. P3 suggests that the Board:

- **Defer action on a seasonal capacity construct** so that further stakeholder discussions can occur. P3 looks forward to actively participating in those discussions; however, injecting a change of this magnitude needs much more time to be fully vetted and understood.

- **Immediately, demand a better proposal from PJM related to the Market Seller Offer Cap**. The Board still has a window to demand a MSOC proposal that better balances supplier risks and can still meet the early October deadline. The Board, before August 25th, should direct PJM to commence a hyper-focused stakeholder process to develop a MSOC proposal that:
  - Only mitigates the units that are truly capable of exercising market power.
  - Provides a safe harbor below which bids will not be mitigated. There are certain minimal risks associated with being a capacity supply resource that must be recognized. Other RTO's have such a safe harbor – PJM should too.
  - Reinstates an MSOC that is objective and not subjective. The current PJM proposal is riddled with opportunities for PJM, the IMM and suppliers to disagree. Net CONE * B is simple to understand and execute.
  - Is consistent with the August 15, 2023, finding of the federal court, "that suppliers do not play second fiddle when their proposed offers deviate from that of the Independent Market Monitor."
  - Delivers this proposal to the PJM by the third week of September so that it can be included in an October filing.
  - If desired, the Board can host a meeting during the 4th week of September in which the Board exclusively receives stakeholder input on proposed revisions to the MSOC.

- Direct PJM staff to **move forward with changes in risk modelling consistent** with the PJM proposal.

- Direct PJM staff to **move forward with changes to accreditation.** Marginal ELCC is an important change to PJM's markets and this issue is ready to move forward.

- **Defer action on FRR**. While P3 has long supported changes to the FRR to allow FRR entities to participate in PJM in a fair and equitable manner, the PJM proposal is not sufficiently developed at this time and FRR could prove to be a distraction at FERC. P3 recommends further stakeholder discussions on FRR.

- Finally, given the breadth of the changes being considered, **instruct PJM to do a tariff "page turn" session with stakeholders** to solicit comments prior to submission to FERC. Such an exercise could improve the quality of the filing and reduce the likelihood of a FERC deficiency letter or rejection.