PJM INTERCONNECTION, L.L.C.

FOR THE QUARTER ENDED SEPTEMBER 30, 2019

INDEX

PJM INTERCONNECTION, L.L.C.
Consolidated Statements of Financial Position ($ in thousands)

		September 30, 2019		December 31, 2018
Assets				
Current assets:				
Deposits on hand	$	1,553,481	$	1,500,794
Operating cash		22,886		362,285
Receivables		40,556		39,694
Study and interconnection receivables		5,873		9,457
Prepaid income taxes		1,674		2,481
Prepaid expenses and other		11,438		9,778
Note receivable		988		1,786
		1,636,896		1,926,275
Non-current assets:				
Fixed assets, net of accumulated depreciation and amortization of $703,304 and $675,440		88,523		97,551
Land		1,420		1,420
Projects in development		49,566		35,047
Deferred recovery of pension and postretirement costs		32,142		30,092
Deferred income taxes, net of valuation allowance		26,814		26,431
Note receivable		803		550
Other		25,378		22,300
		224,646		213,391
Total assets	$	1,861,542	$	2,139,666
Liabilities, paid-in capital, retained earnings and accumulated other comprehensive income				
Current liabilities:				
Accounts payable and accrued expenses	$	21,231	$	33,962
Due to members		61,104		404,980
Study and interconnection payables		6,095		9,247
Accrued payroll and benefits		25,987		28,383
Revolving line of credit		13,334		-
Current portion of long-term debt		2,886		2,886
Current portion of capital lease		1,763		1,707
Deferred regulatory liability		17,233		6,393
Deferred revenue		1,018		3,443
Postretirement healthcare benefits liability		1,398		1,327
Other employee benefits		371		227
Deposits		1,553,481		1,500,794
		1,705,901		1,993,349
Non-current liabilities:				
Long-term debt		14,428		16,593
Long-term capital lease		13,738		15,067
Deferred regulatory liability		18,025		17,843
Interest rate swap		774		325
Pension benefits liability		22,386		15,415
Postretirement healthcare benefits liability		44,644		43,459
Other employee benefits		31,250		27,646
		145,245		136,348
Total liabilities		1,851,146		2,129,697
Commitments and contingencies (Note 13)				
Paid in capital		722		722
Retained earnings		9,506		8,286
Accumulated other comprehensive income		168		961
Total paid-in capital, retained earnings and accumulated other comprehensive income		10,396		9,969
Total liabilities, paid-in capital, retained earnings and accumulated other comprehensive income	$	1,861,542	$	2,139,666

The accompanying notes are an integral part of these consolidated financial statements.

PJM INTERCONNECTION, L.L.C.
Consolidated Statements of Income, Comprehensive Income and Paid-in Capital, Retained Earnings and Accumulated Other Comprehensive Income (Loss)
($ in thousands)

	Three months ended 2019	Three months ended 2018	Nine months ended 2019	Nine months ended 2018
Income				
Operating revenue:				
Service fees	$ 86,790	$ 83,181	$ 243,174	$ 234,051
Deferred regulatory (expense)	(17,070)	(11,408)	(25,377)	(21,757)
FERC fees reimbursement	17,635	17,499	48,627	48,587
Study and interconnection fees	1,064	944	3,063	2,957
Membership fees	862	925	2,718	2,739
Other	1,476	801	3,825	3,643
Total operating revenue	90,757	91,942	276,030	270,220
Operating expenses:				
Compensation	34,446	36,230	110,008	105,099
FERC fees	17,635	17,499	48,627	48,587
Outside services	15,063	13,179	44,582	40,635
Depreciation and amortization	8,903	11,929	27,875	35,328
Software licenses and fees	4,661	4,877	14,085	13,168
Other expenses	2,175	2,750	8,583	10,002
Pension benefits	2,275	1,923	6,762	5,985
Computer maintenance and office supplies	1,677	1,178	6,589	5,015
Study and interconnection services	1,064	944	3,063	2,957
Lease expenses	492	490	1,467	1,428
Postretirement healthcare benefits	220	393	693	1,179
Total operating expenses	88,611	91,392	272,334	269,383
Operating income	2,146	550	3,696	837
Other (expense) income:				
Interest income	8,463	4,273	26,423	9,386
Interest expense	8,806	4,437	27,464	9,056
Total other (expense) income	(343)	(164)	(1,041)	330
Income before income taxes	1,803	386	2,655	1,167
Income tax expense	1,023	243	1,435	675
Net income	$ 780	$ 143	$ 1,220	$ 492
Paid in capital, retained earnings and accumulated other comprehensive income (loss)				
Beginning balance	9,579	9,184	9,969	8,590
Net income	780	143	1,220	492
Other comprehensive income (loss)	37	45	(793)	290
Ending balance	$ 10,396	$ 9,372	$ 10,396	$ 9,372

The accompanying notes are an integral part of these consolidated financial statements.

PJM INTERCONNECTION, L.L.C.
Consolidated Statements of Cash Flows
($ in thousands)

	Nine months ended September 30, 2019	Nine months ended September 30, 2018
Cash flows from operating activities:		
Net income	$ 1,220	$ 492
Adjustments:		
Depreciation and amortization expense	27,875	35,328
Deferred income taxes, net of valuation allowance	(383)	(4,743)
Deferred recovery of pension and postretirement costs	(2,050)	158
Deferred regulatory liability	25,363	21,775
Employee benefit expense greater (less than) than funding	11,975	(41,323)
Net fair value changes related to interest rate swap	449	(458)
Changes in assets and liabilities:		
(Increase) decrease in receivables	(862)	54,713
Decrease (increase) in study and interconnection receivables	3,584	(4,058)
(Increase) in prepaid expenses and other	(6,804)	(612)
Decrease in deferred FERC fees	-	1,672
Decrease in prepaid income taxes	807	6,268
(Decrease) in accounts payable and accrued expenses	(14,149)	(15,706)
(Decrease) increase in study and interconnection payables	(3,152)	3,948
(Decrease) in accrued payroll and benefits	(2,396)	(4,385)
(Decrease) in deferred revenue	(2,425)	(2,450)
Refunds to members	(14,341)	(2,189)
Net cash provided by operating activities	24,711	48,430
Cash flows (used in) investing activities:		
Cost of projects in development	(31,948)	(28,508)
Note receivable	545	1,467
Net cash (used in) investing activities	(31,403)	(27,041)
Cash flows (used in) from financing activities:		
Borrowings under line of credit	470,745	452,855
Repayments under line of credit	(457,411)	(452,855)
Borrowings of long-term debt	-	20,200
Repayments of long-term debt	(2,165)	(20,746)
(Decrease) increase in due to members	(343,876)	67,398
Increase in deposits	52,687	225,468
Net cash (used in) provided by financing activities	(280,020)	292,320
Net (decrease) increase in cash and cash equivalents	(286,712)	313,709
Cash and cash equivalents balance (including customer deposits), beginning of year	1,863,079	1,767,065
Cash and cash equivalents balance (including customer deposits), end of period	$ 1,576,367	$ 2,080,774
Noncash activity:		
Projects in development additions included in ending accounts payable and accrued expenses	1,418	1,494

The accompanying notes are an integral part of these consolidated financial statements.

1. Company Overview

Basis of Presentation

The accompanying consolidated financial statements have been prepared on an accrual basis in accordance with generally accepted accounting principles (GAAP) and include the accounts of PJM Interconnection, L.L.C. and its wholly-owned subsidiaries (collectively referred to herein as PJM or the Company). All intercompany transactions and balances have been eliminated.

The preparation of financial statements in conformity with GAAP in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying disclosures. These estimates are based on management's best knowledge of current events and actions the Company may undertake in the future. Actual results may ultimately differ from estimates.

The interim financial data as of September 30, 2019 and for the three-month and nine-month periods ended September 30, 2019 and September 30, 2018 are unaudited; however, in the opinion of the Company, the interim data includes those adjustments of a normal recurring nature necessary for a fair statement of the results of the interim periods.

These footnotes should be read in conjunction with the Company's 2018 consolidated financial statements and footnotes.

PJM has performed an evaluation of subsequent events through November 8, 2019, which is the date the financial statements were issued.

Adoption of New Accounting Standards

Revenue Recognition

In May 2014, the Financial Accounting Standards Board issued authoritative guidance to provide a single, comprehensive revenue recognition model for contracts with customers. The guidance contains principles that the Company will apply to determine the measurement and timing of revenue recognition. The guidance is effective for annual reporting periods beginning after December 15, 2018, and was adopted by PJM on January 1, 2019. The guidance has been adopted utilizing the modified retrospective approach whereby prior periods have not been restated.

The Company has reviewed its revenue recognition policies to ensure compliance with the requirements of the guidance and has determined adoption did not have a material impact on current revenue recognition policies. Under the standard, PJM is required to provide more comprehensive revenue disclosures to allow financial statement users to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers.

Disaggregated Revenues

The Company has included in the table below disaggregation of PJM service fee revenues by subsidiary Schedule as defined in Schedule 9 of the Company's Open Access Transmission Tariff (Tariff).

	Three-months ended September 30, 2019	Nine-months ended September 30, 2019
PJM stated rate revenues		
Control area administration service	$ 49,055	$ 135,264
FTR administration service	8,014	24,339
Market support service	23,049	63,453
Regulation and frequency response	675	1,958
Capacity resource and obligation management service	3,726	11,052
	84,519	236,066
PJM Settlement service fees	2,271	7,108
Total service fees	$ 86,790	$ 243,174

For the three-month and nine-month periods ended September 30, 2019, PJM Connext, LLC (PJM Connext) recorded consolidated revenue of $1.5 million and $3.8 million, respectively, which is included in other income in the Consolidated Statements of Income, Comprehensive Income and Paid-in Capital, Retained Earnings and Accumulated Other Comprehensive Income.

Contract Balances

PJM and PJM Connext membership fees, which are billed and collected in advance of the year for which they apply, are recognized as revenue ratably over the related annual membership period. Under the revenue guidance, membership fees, recorded as deferred revenue, are considered contract liabilities. The January 1, 2019 opening balance of deferred revenue resulting from contracts with customers was $3.4 million. The September 30, 2019 closing balance of deferred revenue resulting from contracts with customers was $1.0 million. The amount of revenue recognized in the period that was included in the opening contract liability balance was $2.4 million. PJM expects to recognize $1.0 million of PJM membership fees revenue during the remaining three months of 2019.

There were no material contract assets as of September 30, 2019.

PJM's accounts receivables at September 30, 2019, consisted of the following:

	September 30, 2019
Billed:	
PJM Connext	$ 977
	977
Unbilled:	
PJM service fees, net of refunds to members	27,290
PJM recovery of pass-through charges	8,224
Default allocation assessment	4,065
	39,579
	$ 40,556

PJM's member companies are billed on a monthly basis for recovery of PJM and PJM Settlement's administrative costs under the Tariff.

All study and interconnection receivables were billed at September 30, 2019.

2. Deferred Regulatory Liability

PJM recovers fees for the administrative services it provides under its Tariff, pursuant to a stated-rate.

The stated-rate tariff provides for the accumulation of a financial reserve. PJM is permitted to maintain a reserve as a deferred regulatory liability in an amount up to 6 percent of its annual stated-rate revenues, except that beginning for 2020 and every third year thereafter, the financial reserve must be reduced to 2 percent of annual stated-rate revenues. The amount accumulated under the financial reserve provision is classified as a non-current liability in the Company's Consolidated Statements of Financial Position. On a quarterly basis, PJM refunds the deferred regulatory liability balance in excess of the permitted financial reserve for the previous quarter. The quarterly refund rate is established after the financial close of each quarter, and refunds are distributed to the members on a prospective basis in the following quarter. During the first nine months of 2019 and 2018, PJM made refunds of $14.3 million and $2.2 million, respectively.

Any under or over refund amounts will be reflected in the deferred regulatory liability activity in the following quarter.

For PJM Settlement, Inc. (PJM Settlement) the deferred regulatory liability is defined in its rate schedule in the Tariff and is equal to revenues collected in excess of accrual-basis expenses. This balance is refunded quarterly. The quarterly refund rate is established after the financial close of each quarter, and refunds are distributed to the members on a prospective basis in the following quarter. The PJM Settlement rate schedule does not include a financial reserve element.

PJM recognizes deferred regulatory income in the revenue section of the Consolidated Statements of Income, Comprehensive Income and Paid-in Capital, Retained Earnings and Accumulated Other Comprehensive Income for the amount by which service fee revenues pursuant to the rate schedules differ from applicable expenses in the reporting period. The amount by which cumulative revenues under the rate schedules exceed cumulative expenses and refunds is reported as a deferred regulatory liability in the Consolidated Statements of Financial Position. In circumstances in which revenues are less than expenses, PJM reduces the deferred regulatory liability with an offset to deferred regulatory expense.

At September 30, 2019 and December 31, 2018, the deferred regulatory liability was $35.2 million and $24.2 million, respectively. At September 30, 2019 and December 31, 2018, the current portion of the deferred regulatory liability was $17.2 million and $6.4 million representing PJM and PJM Settlement's expected refunds to members during the subsequent quarter. The non-current portion of the deferred regulatory liability of $18.0 million and $17.8 million represents the amount of PJM's reserve at September 30, 2019 and December 31, 2018, respectively.

PJM Settlement recovers its administrative costs under a separate schedule in the Tariff.

3. Note Receivable

On March 21, 2008, FERC approved a settlement to restructure the relationship between PJM and PJM's former Market Monitoring Unit. As part of the settlement, the Market Monitoring Unit and its functions transitioned from being an internal PJM department to an external independent market monitor, Monitoring Analytics, LLC (MA). MA operates independent of PJM management and the Board of Managers. In order to facilitate the externalization of this function and as part of the settlement agreement approved by FERC, PJM entered into a revolving loan agreement with MA in March 2008. The revolving loan agreement was extended in November 2018 to March 31, 2026.

The purpose of the PJM revolving loan to MA is to fund capital needs associated with MA's technology systems and working capital needs related to MA's responsibilities per Attachment M of the Tariff to monitor the markets administered by PJM. The revolving loan has a capacity of $11 million and is secured by MA's accounts receivable and future collections of accounts receivable. At September 30, 2019 and December 31, 2018, the interest rate on the revolving loan agreement between PJM and MA was 5.00 percent and 5.50 percent, respectively. The interest rate on all loan advances is equal to the PNC Bank Base Rate. The PNC Bank Base Rate is the highest of (A) the Prime Rate, (B) the sum of the Federal Funds Rate plus 50 basis points (0.50 percent), or (C) the sum of the Daily London Interbank Offered Rate (LIBOR) plus 100 basis points (1.0 percent).

At September 30, 2019 and December 31, 2018, the outstanding balance due from MA recorded by PJM as a note receivable was $1.8 million and $2.3 million, respectively. At September 30, 2019 and December 31, 2018, the current portion of the note receivable was $1.0 million and $1.8 million, respectively. The current balance at September 30, 2019 represents the amount to be repaid in the next twelve months. The non-current portion of the note receivable was $0.8 million at September 30, 2019 and $0.5 million at December 31, 2018.

4. Short-Term Debt

PNC Revolving Line of Credit

On March 1, 2018 PJM amended and restated the existing revolving credit agreement with PNC Bank (PNC), increasing the capacity from $100 million to $150 million. PJM received approval from FERC to continue to borrow under this amended facility and to increase the unsecured promissory note on January 19, 2018. The facility terminates on January 31, 2020, and can be extended automatically through February 28, 2021, with FERC authorization. The revolving line of credit is unsecured and available to fund short-term cash obligations.

Under the loan covenants for the revolving credit agreement, PJM is required to meet certain financial and non-financial covenants. PJM was in compliance with these covenants as of September 30, 2019. At September 30, 2019 there was $13.3 million outstanding under the revolving credit agreement. At December 31, 2018, there were no amounts outstanding under the revolving credit agreement. The interest rate on borrowings under this revolving credit agreement is based on the 30-day LIBOR. At September 30, 2019, the interest rate was 2.640 percent.

The amended facility also has a commitment fee of 6.00 basis points on the unused balance. This fee is calculated daily and paid quarterly.

5. Long-Term Debt and Derivative Financial Instrument – Interest Rate Swap

Bank of America Bank Loan Agreement

On June 28, 2018, FERC approved PJM's request to refinance the Company's bank loan with PNC through a new term loan from Bank of America (BoA). On July 20, 2018, PJM entered into a $20.2 million loan agreement with BoA. The BoA term loan has a seven-year term and is unsecured. Payments on the term loan are due quarterly.

As of September 30, 2019 and December 31, 2018, the outstanding borrowings under the term loan were $17.3 million and $19.5 million, respectively. As defined in the loan agreement, the term loan bears interest at a rate per annum equal to the LIBOR rate plus a spread of 65 basis points (0.65 percent). As of September 30, 2019 the interest rate was 2.74 percent.

Under the loan agreement, PJM is required to meet certain financial and non-financial covenants. PJM was in compliance with these covenants as of September 30, 2019.

Derivative Financial Instrument - Interest Rate Swap

To manage interest rate risk associated with the $20.2 million loan agreement with BoA, the Company entered into an interest rate swap agreement with BoA effective August 1, 2018. The interest rate swap agreement effectively fixes the interest payments of the Company's floating rate debt instrument at a rate of 3.62 percent. The term of the interest rate swap matches the term of the loan.

While PJM has entered into an economic hedge of its interest rate, the Company has elected not to designate this instrument as a cash flow or fair value hedge for accounting purposes. Accordingly, the interest rate swap is carried at fair value in the Consolidated Statements of Financial Position with changes in fair value recorded through earnings. At September 30, 2019 and December 31, 2018, the fair value of the swap was a liability of $0.8 million and $0.3 million, respectively.

For the three-month periods ended September 30, 2019 and September 30, 2018, PJM recognized a $0.1 million loss and $0.1 million gain, respectively, as interest expense in the Consolidated Statements of Income, Comprehensive Income and Paid-in Capital, Retained Earnings and Accumulated Other Comprehensive Income.

For the nine-month periods ended September 30, 2019 and September 30, 2018, PJM recognized a $0.5 million loss and $0.5 million gain, respectively, as interest expense in the Consolidated Statements of Income, Comprehensive Income and Paid-in Capital, Retained Earnings and Accumulated Other Comprehensive Income.

The Company does not hold or issue financial instruments for speculative or trading purposes for its own account.

6. Financial Transmission Rights

PJM Settlement is the central counterparty to member's pool transactions, which includes financial transmission rights (FTR). As central counterparty, PJM Settlement has flash title pass through the entity when markets settle and as charges and credits are assessed on pool transactions.

A FTR is a financial instrument that enables market participants to reduce their congestion-related price risk when delivering or selling energy on the grid. FTRs provides an economic hedging mechanism against congestion charges that can be transacted by members separately from transmission service.

In PJM Settlement's role as administrator of the FTR market, at auction clearing PJM Settlement is temporarily the counterparty to both the FTR buyer and the FTR seller. PJM Settlement is neither the buyer nor seller of FTRs and does not bear the economic risks and rewards of the financial instrument. Accordingly, FTRs do not present a credit risk to PJM.

For reporting purposes, FTR positions net to zero in the Consolidated Statements of Financial Position and the Consolidated Statements of Income, Comprehensive Income and Paid-in Capital, Retained Earnings and Accumulated Other Comprehensive Income. Because there are ongoing open FTR positions at period end, the Company is disclosing the fair value of these instruments for informational purposes.

The fair value of FTRs as of September 30, 2019, was $468 million. A total of 285 members are FTR holders related to a total of 3.1 million megawatt-hours. As of September 30, 2019, PJM held $1.9 billion in collateral related to these FTR transactions. The collateral held is based on the calculated net value of the positions held in each member's FTR portfolio and can be in the form of cash or a letter of credit. The collateral position disclosed reflects the totality of collateral related to the FTR market. Individual member portfolios could have a different level of credit exposure.

Roll-forward of FTR activity for the quarter ended September 30, 2019, consisted of the following.

($ in millions)	
Balance at July 1, 2019	$ 686
Auction additions	(67)
Settlement and change in fair value	(151)
Balance at September 30, 2019	$ 468

On April 1, 2019 the Federal Energy Regulatory Commission (FERC) approved changes to the Company's credit requirements, specifically the adoption of mark-to-auction provisions. Mark-to-auction provides a valuation of the cleared FTR portfolio based on the most recent auction prices and also takes into consideration the value of Auction Revenue Right entitlements allocated to firm transmission service customers. The value of FTRs as of September 30, 2019 under a mark-to-auction model was $368 million.

7. Fair Value Disclosures

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). In determining fair values, PJM utilizes market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. The authoritative guidance pertaining to fair value establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). The three levels of the fair value hierarchy defined by this guidance are as follows:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Pricing inputs are other-than quoted prices in active markets included in Level 1, which are directly or indirectly observable as of the reporting date. Level 2 includes those financial instruments that are valued using broker quotes in liquid markets, and other observable pricing data. Level 2 also includes those financial instruments that are valued using internally developed methodologies that have been corroborated by observable market data through correlation or by other means. Significant assumptions are observable in the marketplace throughout the full term of the instrument, can be derived from observable data or are supported by observable levels at which transactions are executed in the marketplace.

Level 3 – Pricing inputs include significant inputs that are generally less observable than those from objective sources.

PJM utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. PJM is able to classify fair value balances based on the observability of the inputs. In accordance with the authoritative guidance, financial assets and liabilities are classified in their entirety based on the lowest level of observability for an input that is significant to the fair value measurement. PJM's assessment of the significance of a particular input to the fair value measurement requires the exercise of judgment, and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels.

The following table presents PJM's cash and cash equivalents as well as financial assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2019 and December 31, 2018 by level within the fair value hierarchy.

($ in millions)	**September 30, 2019**				**December 31, 2018**
	Level 1	**Level 2**	**Level 3**	**Carrying Value**	**Carrying Value**
Cash and cash equivalents	$ 1,576	$ -	$ -	$ 1,576	$ 1,863
Deposit liabilities	1,553	-	-	1,553	1,501
Derivative liabilities	-	1	-	1	1

The fair value of FTR assets and liabilities for which PJM Settlement is the counterparty for an instant are determined on a recurring basis based on Level 3 inputs within the fair value hierarchy. The valuation model used is based on a three-year weighted average of historical location marginal price by month by node. The model also calculates historical values for on-peak, off-peak and 24-hour FTRs. For reporting purposes, these positions net to zero in the Consolidated Statements of Financial Position and the Consolidated Statements of Income, Comprehensive Income and Paid-in Capital, Retained Earnings and Accumulated Other Comprehensive Income and are not presented in the table above.

8. Income Taxes

The income tax rate on PJM's operating activities differed from the federal statutory rate as follows:

	September 30, 2019	September 30, 2018
Income tax expense at the federal statutory rate	$ 558	$ 245
Increase (decrease) resulting from:		
Change in valuation allowance	(8)	(12)
Permanent differences	348	145
State income taxes, net of federal tax benefit	392	163
Other	145	134
Income tax expense	$ 1,435	$ 675

PJM and its subsidiaries file a U.S. consolidated federal income tax return and consolidated or separate company tax returns in various states, including of the state of Pennsylvania. The tax years subsequent to 2014 remain open to examination by the United States Internal Revenue Service and generally, the tax years subsequent to 2014 remain open to examination by various state taxing authorities. There are no ongoing audits at this time.

9. Benefit Plans

The schedules that follows shows the components of net periodic pension and postretirement health care costs for the three-month and nine-month periods ended September 30, 2019 and September 30, 2018.

	Pension Benefits				Other Postretirement	
Components of Net Periodic Benefit	**Qualified**		**SERP**		**Benefits**	
Cost, July 1 to September 30	**2019**	**2018**	**2019**	**2018**	**2019**	**2018**
Service cost	$ 2,389	$ 2,696	$ 87	$ 92	$ 375	$ 421
Interest cost	2,439	2,250	80	68	594	573
Expected return on assets	(3,331)	(3,718)	-	-	(181)	(167)
Prior service cost / (gain)	(4)	(5)	2	2	(322)	(322)
Actuarial loss / (gain)	628	542	71	91	(158)	(14)
Total net periodic benefit cost	$ 2,121	$ 1,765	$ 240	$ 253	$ 308	$ 491

	Pension Benefits				Other Postretirement	
Components of Net Periodic Benefit	**Qualified**		**SERP**		**Benefits**	
Cost, January 1 to September 30	**2019**	**2018**	**2019**	**2018**	**2019**	**2018**
Service cost	$ 7,187	$ 8,261	$ 260	$ 272	$ 1,118	$ 1,274
Interest cost	7,289	6,764	237	203	1,785	1,705
Expected return on assets	(10,002)	(11,162)	-	-	(544)	(500)
Prior service cost / (gain)	(14)	(14)	5	5	(965)	(965)
Actuarial loss / (gain)	1,831	1,663	200	257	(468)	(69)
Total net periodic benefit cost	$ 6,291	$ 5,512	$ 702	$ 737	$ 926	$ 1,445

For both of the three-month periods ended September 30, 2019 and September 30, 2018, $0.2 million of total pension and postretirement benefits expense were included in capitalized project costs, respectively.

For both of the nine-month periods ended September 30, 2019 and September 30, 2018, $0.5 million of total pension and postretirement benefits expense were included in capitalized project costs, respectively.

The following schedule shows the assumptions used to calculate the pension and postretirement benefit obligations for as of September 30, 2019 and September 30, 2018.

	Pension Benefits		Postretirement Benefits	
	2019	**2018**	**2019**	**2018**
Discount rate	4.30%	3.70%	4.30%	3.70%
Expected return on plan assets	6.40%	6.60%	6.40%	6.60%
Rate of compensation increase	4.50%	4.50%	N/A	N/A
Medical care cost trend rate				
Current (Pre-65)			5.92%	6.17%
Current (Post-65)			6.48%	6.93%
Ultimate (Pre-65)			4.46%	4.46%
Ultimate (Post-65)			4.45%	4.45%
Years to ultimate			19	20

10. Commitments and Contingencies

Other Items

Marginal Line Loss Surplus Payment Reallocation

Between July 17, 2012, and July 20, 2012, fourteen companies defaulted on payment obligations totaling $28 million, net of collateral held by PJM. These obligations resulted from reallocations for previously ordered, and provided, refunds made to certain market participants for billing adjustments related to the marginal line loss payment surplus allocation methodology under the Amended and Restated Operating Agreement of PJM (Operating Agreement) and the Tariff, which was ordered by FERC in an order issued in Docket No. EL08-14 on July 21, 2011. PJM Settlement filed 2 complaints in civil action alleging breach of contract in the state of Delaware against former members. The first complaint, filed on November 7, 2012, naming City Power Marketing, LLC, Energy Endeavors, LLC, Energy Endeavors, LP and Crane Energy, LP, seeks the recovery of approximately $23 million owed to PJM Settlement. The second complaint, filed on December 6, 2012, naming Round Rock Energy, LLC; Round Rock Energy, LP; Huntrise Energy Fund, LLC; and certain named principals individually, seeks the recovery of approximately $4 million.

Several parties affected by FERC's underlying ruling in this matter sought judicial review of FERC's decision in the United States Court of Appeals for the District of Columbia Circuit and, in the ruling issued in August 2013, the court of appeals directed FERC to provide additional support for its determination to recoup the previously ordered refunds. On or about November 7, 2016, FERC filed an unopposed motion and requested the court of appeals to remand the recoupment order. Accordingly, the court granted FERC's motion and remanded the recoupment order on November 9, 2016, to FERC. On June 20, 2019, FERC issued an Order on Voluntary Remand and Granting Rehearing ("June 20 Remand Order") finding that previously-ordered refunds were appropriate and reversing its prior determinations to the contrary. As a result, PJM is directed to pay additional refunds of misallocated marginal line loss over-collection amounts to those Financial Marketers that engaged in Up-To-Congestion transactions. On July 22, 2019, American Municipal Power, Inc. ("AMP") filed a request for rehearing on FERC's June 20 Remand Order requesting that FERC reinstate the determinations made in its prior orders. On October 28, 2019, FERC issued an order denying AMP's rehearing request. PJM Settlement, Inc. has started its determination of the amounts of refunds and plans to notify market participants of the additional funds to be collected and credits which will be provided during first quarter 2020.

The collection actions referenced above remain stayed in the Delaware courts until such time as a final order is received on any appeals of FERC's orders in this matter. The outcome of these additional refunds is not anticipated to have a material adverse effect on PJM's financial position, results of operations or cash flow.

TranSource Matter

On June 23, 2015, TranSource, LLC (TranSource) filed a complaint (Complaint) against PJM with FERC. In the Complaint, TranSource asked FERC to order PJM to provide work papers used to determine the cost estimates for each individual system upgrade specified in System Impact Studies and to suspend all Tariff deadlines otherwise applicable to its Incremental Auction Revenue Rights (IARR) request, pending receipt of the demanded information. On September 24, 2015, FERC issued an order setting the Complaint for a trial-type evidentiary hearing. On February 10, 2016, TranSource filed an amendment to the Complaint (the Amended Complaint). In the Amended Complaint, TranSource claims it incurred $72 million in lost profit opportunities from monthly IARRs during calendar year 2015 plus continuing losses of approximately $6 million per month going forward.

On January 19, 2018, the Administrative Law Judge issued an initial decision finding that PJM's practices used to process TranSource's Upgrade Requests during the System Impact Study phase were nontransparent; and the impact of the system impact study phase, as applicable to TranSource, was discriminatory under the

Federal Power Act and therefore unjust and unreasonable. TranSource was granted limited relief, ordering PJM to restore TranSource's original queue position and refund the $0.15 million paid by TranSource for the study of its upgrade request. All other requests for relief were denied. PJM filed a brief on exceptions on February 20, 2018. A final decision will be issued by the Commission after considering all exception briefs filed.

Separate from the Complaint pending before FERC, TranSource commenced a civil action against PJM and four PJM transmission owners in the Montgomery County Pennsylvania Court of Common Pleas. This action has been removed to federal district court and all proceedings in the civil action are stayed pending the conclusion of the proceedings before the FERC, including the conclusion of any appeals and the expiration of the period for filing any appeals.

PJM does not believe that these matters will have a material adverse effect on its financial position, results of operations or cash flow.

Credit Matter

On June 21, 2018, GreenHat Energy, LLC defaulted on its obligations related to its FTR portfolio, which includes positions applicable to the current planning year as well as the 2019–2020 and 2020–2021 planning years. The default allocation assessments to the non-defaulting members for the period June 2018 through September 2019 were $130.6 million and may change to liquidated costs. On January 30, 2019, FERC denied PJM's waiver requesting to only offer the August 2018 defaulted FTRs for liquidation in the FTR auction conducted in July 2018. PJM has requested FERC to stay implementation of that denial and has requested rehearing and clarification of FERC's denial of PJM's waiver request. In June 2019, FERC issued an order on clarification and set the matter for a paper hearing and settlement judge procedures. The parties submitted a settlement with FERC on October 9, 2019 that resolves all issues in this proceeding and would avoid the recalculation and rebilling on past default charges. PJM and the settling parties are awaiting FERC action on the settlement. PJM cannot predict the future default allocation assessments resulting from this default. The aggregate payment default of this member, net of collateral held, will be billed to the non-defaulting members in accordance with the default allocation assessment formula in the Operating Agreement. PJM has implemented significant FTR credit policy enhancements in both 2018 and 2019. The outcome of the default is not anticipated to have a material adverse effect on PJM's financial position, results of operations or cash flow.

Legal

PJM is routinely involved in legal actions. In the opinion of management, none of these matters will have a material adverse effect, if any, on the financial position, results of operations or liquidity of PJM.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPEARTIONS

Forward-Looking Statements

In addition to the historical information presented throughout this report, there are forward-looking statements that reflect management's expectations for the future. Sometimes the words "estimate," "plan," "expect," "believe," or similar expressions will be used to identify such forward-looking statements. These forward-looking statements are based on current expectations. These statements are not guarantees of future performance and are subject to certain risks and uncertainties.

Many factors could cause actual results to differ materially from these statements. These factors include, but are not limited to, the results of regulatory proceedings, the conditions of the capital markets, interest rates, actuarial assumptions, availability of credit, liquidity and general economic conditions; changes in accounting principles and practices; acts of terrorists; the actions of adjacent control areas and other Regional Transmission Organizations (RTOs); and other operational conditions that could arise on the power system. For a description of these and other factors that may cause actual results to differ, reference is made hereby to PJM Interconnection L.L.C.'s (PJM or the Company) Consolidated Financial Statements, Notes thereto and other documents filed by the Company from time to time with the Federal Energy Regulatory Commission (FERC).

These forward-looking statements represent PJM's estimates and assumptions only as of the date of this report, and PJM assumes no responsibility to update these forward-looking statements.

Results of Operations

Revenues and Expenses

PJM's service fees increased $3.6 million, or 4 percent, to $86.8 million for the three-month period ended September 30, 2019 as compared with the three-month period ended September 30, 2018; and increased $9.1 million, or 4 percent, to $243.2 million for the nine-month period ended September 30, 2019 as compared with the nine-month period ended September 30, 2018. The variance in service fees is principally due to a 2.5 percent increase in the composite stated-rate on January 1, 2019 and increased bidding activity under the various PJM auctions. Transmission volumes for the three-month and nine-month periods ended September 30, 2019 were 228 terawatt hours (TWhs) and 628 TWhs as compared with 228 TWhs and 635 TWhs for the three-month and nine-month periods ended September 30, 2018.

Total expenses, excluding FERC fees, study and interconnection services, interest expense, and income taxes, decreased $3.0 million, or 4 percent, to $69.9 million for the three-month period ended September 30, 2019 as compared with the three-month period ended September 30, 2018. Total expenses, excluding FERC fees, study and interconnection services, interest expense, and income taxes, increased $2.8 million, or 1 percent, to $220.6 million for the nine-month period ended September 30, 2019 as compared with the nine-month period ended September 30, 2018. The decrease in expenses in third quarter 2019 resulted primarily from a decrease in depreciation and amortization primarily due to a lower fixed asset balance period over period. The decrease in expense was offset by incremental costs associated with employee retirements that are one time in nature along with increased outside services.

Liquidity and Capital Resources

PJM has a revolving credit agreement with PNC Bank for $150 million, which expires on January 31, 2020 and can be extended automatically through February 28, 2021. The facility is unsecured and is available to fund short-term cash obligations. At September 30, 2019, $13.3 million was outstanding under the revolving credit agreement.

On June 28, 2018, FERC approved PJM's application to refinance the Company's existing bank loan with PNC with a new term loan at Bank of America (BoA). On July 20, 2018, PJM entered into a $20.2 million loan agreement with BoA. The BoA term loan has a seven-year term and is unsecured. At September 30, 2019, the outstanding borrowings under the term loan were $17.3 million.

Risks and Uncertainties

PJM does not provide forecasts of future financial performance. While PJM management is optimistic about the Company's long-term prospects, the following issues and uncertainties, among others, should be considered in evaluating its outlook.

Credit Risks

PJM bills and collects its operating expenses monthly from its members. Payment of all operating expense bills is due from PJM's members three business days after the month-end bill is issued by PJM, generally within the first two weeks of each month. For the nine-month period ended September 30, 2019, approximately 55 percent of PJM's operating expenses were billed to 19 of its members, each of which either has an investment-grade credit rating according to at least one of the three major rating services or has provided a guaranty from an affiliate with an investment-grade rating. In the event of default of any PJM members, PJM has the right to bill the remaining PJM members a ratable portion of the operating expenses previously billed to the defaulting member.

In accordance with PJM's credit policy, PJM obtains collateral from certain members in order to secure their credit positions. The collateral can be in the form of a cash deposit or letter of credit. Corporate guaranties are also accepted from creditworthy affiliates to fulfill certain credit requirements.

Marginal Line Loss Surplus Payment Reallocation

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Several parties affected by FERC's underlying ruling in this matter sought judicial review of FERC's decision in the United States Court of Appeals for the District of Columbia Circuit and, in the ruling issued in August 2013, the court of appeals directed FERC to provide additional support for its determination to recoup the previously ordered refunds. On or about November 7, 2016, FERC filed an unopposed motion and requested the court of appeals to remand the recoupment order. Accordingly, the court granted FERC's motion and remanded the recoupment order on November 9, 2016, to FERC. On June 20, 2019, FERC issued an Order on Voluntary Remand and Granting Rehearing ("June 20 Remand Order") finding that previously-ordered refunds were appropriate and reversing its prior determinations to the contrary. As a result, PJM is directed to pay additional refunds of misallocated marginal line loss over-collection amounts to those Financial Marketers that engaged in Up-To-Congestion transactions. On July 22, 2019, American Municipal Power, Inc. ("AMP") filed a request for rehearing on FERC's June 20 Remand Order requesting that FERC reinstate the determinations made in its prior orders. On October 28, 2019, FERC issued an order denying AMP's rehearing request. PJM Settlement, Inc. has started its determination of the amounts of refunds and plans to notify market participants of the additional funds to be collected and credits which will be provided during first quarter 2020.

PJM is working to implement the FERC's order and will be making additional refunds to Financial Marketers. The collection actions referenced above remain stayed in the Delaware courts until such time as a final order is received on any appeals of FERC's orders in this matter. The outcome of these additional refunds is not anticipated to have a material adverse effect on PJM's financial position, results of operations or cash flow.

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