Defaulting FTR Positions

Problem / Opportunity Statement

Effective December 1, 2018, PJM implemented changes to Tarff, Attachment K-Appendix, sections 7.3.1 and 7.3.9, and the identical provisions of Operating Agreement, Schedule 1, sections 7.3.1 and 7.3.9, ending the practice of liquidating a defaulting FTR Participant's ongoing Financial Transmission Right (FTR) positions. This change represented an overwhelming consensus of the PJM stakeholder community seeking to address, on a going forward basis, how they wished to manage the disposition of a defaulting Member's FTR portfolio. This change resulted in allowing a defaulted FTR Participant's FTR positions to go to settlement, rather than being liquidated. The change was also initiated in response to a specific default and the very prescriptive nature of the manner in which PJM was required to liquidate that defaulting FTR portfolio pursuant to the referenced Tariff and Operating Agreement provisions. If PJM had the flexibility to offer, for example, smaller subsets of the portfolio position based on factors such as, but not limited to, the size of the specific portfolio, the FTR market's ability to absorb the positions, and with a focus on minimizing costs to the Members, PJM would have been able to align with best practices that have been established in the financial industry that are focused on unwinding a defaulted position in a prudent and orderly manner.

In the *Report of the Independent Consultants on the GreenHat Default* (March 26, 2019), the consultants noted weaknesses in PJM's policies and processes related to advancing credit risk management best practices into the Tariff. While the report did not specifically address the ability to liquidate an FTR portfolio, it is industry best practice to neutralize or reduce large one directional risk as soon as reasonably practical. PJM opines that re-establishing the ability to liquidate and close out a defaulted FTR portfolio in a manner that is reasonable and allows for flexibility in managing a defaulted portfolio through a variety of methods that minimizes costs to Members and allows for closing out the positions in a prudent and orderly manner.

In order to minimize costs to Members and allows for closing out of defaulted positions in a prudent and orderly manner, PJM needs to have the flexibility to liquidate and close out defaulting FTR positions in a manner that allows PJM to hedge and/or offer for auction the positions (with a goal to minimize costs to Members), limit significant price disruptions to the market, and manage and/or close out the defaulting FTR Participant's positions, while also holding onto any applicable collateral. PJM needs to have the flexibility to consider the size of the defaulted portfolio, the liquidity of the market, and other factors that PJM deems appropriate.