UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

PJM Interconnection, L.L.C. v. PJM Interconnection, L.L.C.	)	Docket No. EL19-8-000
PJM Interconnection, L.L.C.	)	Docket No. ER19-210-000 (not consolidated)

ANSWER AND MOTION FOR LEAVE TO ANSWER
OF THE INDEPENDENT MARKET MONITOR FOR PJM

Pursuant to Rules 212 and 213 of the Commission's Rules and Regulations,[1] Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor for PJM[2] ("Market Monitor"), submits this answer to the comments submitted on November 19, 2018, by Dominion Energy Services, Inc. ("Dominion") and jointly by the PJM Power Providers Group and the Electric Power Supply Association ("Power Providers"). Other contemporaneously filed responses merely repeat arguments raised by PJM that have already been refuted, and so are not addressed here. None of these comments provide a coherent or logical defense of PJM's proposal or otherwise have merit. Accordingly, PJM's proposed revisions should not be approved.

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1 18 CFR §§ 385.212 & 385.213 (2018).

2 Capitalized terms used herein and not otherwise defined have the meaning used in the PJM Open Access Transmission Tariff ("OATT") or the PJM Operating Agreement ("OA").

I. ANSWER

A. Dominion Misdefines a Competitive Energy Offer.

Dominion claims (at 3) that "the capacity market is an inefficient means to recover variable long-term maintenance costs that are dependent upon electricity production." Dominion ignores that fact that variable long-term costs are by definition not short run marginal costs, and, therefore, not part of a competitive energy market offer.[3] Dominion argues that the three year maintenance cost forecasts required in the capacity market are inaccurate. But historic maintenance costs are inaccurate forecasts of the future and will always be wrong by definition. The twenty year maintenance cost history for use in energy market offers, dictated by the PJM Manual 15 (Cost Development Guidelines) is a demonstrably bad predictor, in significant part because it reflects costs based on very different operating conditions, including some that predate markets. Unit owners are free to use the maintenance history if they can demonstrate that it is relevant so there is no downside to using forward looking costs. Blindly using an average over the 20 year history of maintenance costs as a guide to future costs is not a reasonable or rational option, especially given the significant changes in market conditions. If under new market conditions the unit runs more or less or cycles more or less compared to their historic operation, maintenance costs will increase or decrease and the maintenance adder included in the cost-based offer will be under or overstated. Actual market competitors do not calculate forward looking costs based on a simple, mechanical average of history. Competitors make informed decisions about expected costs.

In using the term cost recovery, Dominion reveals the confusion about the difference between markets and cost of service regulation. Markets are not designed to be efficient ways to recover costs. Cost recovery is a cost of service regulation concept. Under cost of

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3 *See Southwest Power Pool*, 152 FERC ¶ 61,226 at P 68 (2015); *PJM Interconnection, L.L.C.*, 110 FERC ¶ 61,053 at P 25 (2005).

service regulation, generation owners are allowed to recover their costs subject to regulatory approval of the costs and the rate of return on capital. Under markets, net revenues from energy markets, ancillary services markets and the capacity market are all sources of revenue that provide an opportunity to cover costs and earn a return. The opportunity to earn revenues in all the markets creates an incentive to enter the markets and also an incentive to exit the markets. But costs are not assigned to net revenues from specific markets. Units can and do cover all their costs and their target rate of return from inframarginal rents in the energy market only. Many units need a combination of net revenues from all markets to cover their costs.

In arguing that long-run variable costs should be included in energy market cost-based offers, Dominion ignores (at 3–4) the fact that the purpose of energy market cost-based offers is to prevent the exercise of market power by defining a competitive offer level. The competitive offer level is short run marginal cost. Costs that vary in the long run that do not vary in the short run are not short run marginal costs. Therefore the inclusion of major maintenance in energy market cost-based offers as a long-run variable cost is inconsistent with competitive market outcomes. If generation owners can include costs that are not short run marginal costs in cost-based offers, that would directly permit the exercise of market power when units have structural market power and their offers are mitigated. The goal of the PJM market design is to provide energy at rates consistent with competition. PJM's proposal to allow prices, or uplift payments, in excess of the competitive level is not just and reasonable.

B. Forward Looking Estimates are Consistent with the Way Actual Markets Work.

Dominion argues (at 4) that the inclusion of maintenance costs in the capacity offer is "problematic because a fundamental change in the market, such as future fuel pricing volatility, that occurs between the time a capacity offer is developed and a resource's operation for a delivery year could limit the resource's ability to recover its true maintenance costs." Dominion argues that this issue is solved by allowing resources to include maintenance costs in the energy offer. Dominion is mistaken.

In the PJM Market includable costs do not mean recoverable costs. Recoverable is a cost of service concept. Markets include uncertainty and all market participants face uncertainty. Dominion argues that including maintenance costs in the capacity market offer limits the ability to recover such costs. Dominion did not make the assertion that any units in PJM cannot or have not covered their avoidable costs from all markets. In the case when that is true, the units are receiving a retirement signal from the market. That is an appropriate signal. Including maintenance costs in the capacity market offer does not guarantee cost recovery. Not including maintenance costs in the capacity market offer does not mean that those costs are not being recovered from inframarginal rents in the capacity and energy market.

C. PJM's Proposal Will Allow Double Recovery of Variable Long Term Maintenance Costs.

Dominion argues (at 5) that PJM's proposal prevents potential double recovery of variable long term maintenance costs by not allowing a resource to include these costs in both the energy market offer and the capacity market offer. Dominion and PJM confuse cost of service regulation with markets and recoverable with includable. Inframarginal resources in the PJM markets can recover all of their costs from one market or another. For example, some resources offer at zero dollars per MWh in the energy market and at zero dollars per MW-day in the capacity market and recover all of their costs. On the other hand, a resource could offer all of its costs in one market or another and recover none of its costs because the offers are too high to clear either market. Including a cost in an offer is not equivalent to cost recovery. The way to maximize revenues and profits and cost recovery is to offer competitively.

Power Providers' comments highlight this problem. Power Providers argue (at 3) that PJM's proposed language "recover maintenance costs through the capacity market" is overly broad and could be read to cover resources offering below their RPM offer cap or circumstances where a generator receives inframarginal rents in the capacity market. Power Providers are correct that a Market Seller can recover a resource's maintenance costs in the capacity market without explicitly including those costs in a resource's Avoidable Cost Rate. Power Providers seek to recover maintenance costs through the capacity market and also include maintenance costs in the energy market. This behavior will allow double recovery of maintenance costs, once through inframarginal rents in the capacity market and again when the resource is offer capped in the energy market and paid its cost-based offer, including maintenance costs.

II. MOTION FOR LEAVE TO ANSWER

The Commission's Rules of Practice and Procedure, 18 CFR § 385.213(a)(2), do not permit answers to answers or protests unless otherwise ordered by the decisional authority. The Commission has made exceptions, however, where an answer clarifies the issues or assists in creating a complete record.[4] In this answer, the Market Monitor provides the Commission with information useful to the Commission's decision-making process and which provides a more complete record. Accordingly, the Market Monitor respectfully requests that this answer be permitted.

III. CONCLUSION

The Market Monitor respectfully requests that the Commission afford due consideration to this answer as the Commission resolves the issues raised in this proceeding.

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4 *See, e.g., PJM Interconnection, L.L.C., 119 FERC ¶61,318 at P 36 (2007) (*accepted answer to answer that "provided information that assisted … decision-making process*"); California Independent System Operator Corporation*, 110 FERC ¶ 61,007 (2005) (answer to answer permitted to assist Commission in decision-making process); *New Power Company v. PJM Interconnection, L.L.C.*, 98 FERC ¶ 61,208 (2002) (answer accepted to provide new factual and legal material to assist the Commission in decision-making process); *N.Y. Independent System Operator, Inc.*, 121 FERC ¶61,112 at P 4 (2007) (answer to protest accepted because it provided information that assisted the Commission in its decision-making process).

Respectfully submitted,

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Dated: December 4, 2018

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Eagleville, Pennsylvania,
this 4th day of December, 2018.

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