

**UNITED STATES OF AMERICA  
BEFORE THE  
FEDERAL ENERGY REGULATORY COMMISSION**

PJM Interconnection, L.L.C.	)	
	)	Docket No. ER13-198-000
	)	

**COMMENTS OF THE INDEPENDENT MARKET MONITOR FOR PJM**

Pursuant to Rule 211 of the Commission’s Rules and Regulations,<sup>1</sup> Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor for PJM (“Market Monitor”),<sup>2</sup> submits these comments on the compliance proposal filed by PJM Interconnection, L.L.C. (“PJM”) on October 10, 2012 (“October 10<sup>th</sup> Proposal”) in order to comply with Order No. 1000 and on complaint.<sup>3</sup> The Market Monitor is concerned that the October 10<sup>th</sup> Proposal does not permit meaningful comparative evaluation of competing projects based on costs. The proposal adopts essentially that same process for evaluating competing nonincumbent and incumbent projects used in the *Primary Power* case.<sup>4</sup> That process failed to produce a transparent result, consistent with the objectives in Order No. 1000, and this proceeding presents an important opportunity to improve the process.

The process included in the October 10<sup>th</sup> Proposal does not provide for a transparent comparative evaluation of different projects competing to meet the same need. This process

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<sup>1</sup> 18 CFR § 385.211 (2012).

<sup>2</sup> Capitalized terms used herein and not otherwise defined have the meaning used in the PJM Open Access Transmission Tariff (“OATT”).

<sup>3</sup> See *Transmission Planning and Cost Allocation by Transmission Owning and Operating Public Utilities*, Order No. 1000, 139 FERC ¶ 61,051 (2011) (“Order No. 1000”), *order on reh’g and clarification*, Order No. 1000-A, 139 FERC ¶ 61,132 (2012) (“Order No. 1000-A”); 18 USC § 824d (2000).

<sup>4</sup> See *Primary Power v. PJM Interconnection, L.L.C.*, 140 FERC ¶ 61,054 (2012) (“*Primary Power*”), *reh’g pending*; FERC Docket No. EL12-69.

does not meaningfully account for cost differences, much less identify a lowest cost solution. Without a transparent process that entails real cost comparisons, there is little or no incentive for continued participation by nonincumbents, and little prospect for realizing the innovative and worthwhile policy objectives of Order No. 1000. Without significant improvement, the October 10<sup>th</sup> Proposal would institute a de facto right of first refusal for incumbents even as it is eliminated de jure.

The best way to improve the October 10<sup>th</sup> Proposal is to include provisions for competitive financing.

Order No. 1000 explicitly declined to “mandate a competitive bidding process for selecting project developers,” and that is not what the Market Monitor proposes here. PJM can continue to select the projects to develop through the RTEP process without establishing a process for competitive bidding, although cost considerations should be included as one key element of the decision. However, once PJM has selected and included a project in the RTEP, PJM should require that the developer select the lowest cost source of capital through competitive bidding. PJM can consider the question of who supplies capital for a project separately from who develops it.

Under this approach, a project developer would not file with the Commission to obtain a cost-based rate and would enjoy no presumptive right to provide the capital at a preestablished rate of return. PJM can then evaluate projects on the merits, reserving the question of who will assume the risks and benefits of the investment.

If the use of competition to provide capital is not required, then alternative improvements should be required to address deficiencies in the October 10<sup>th</sup> Proposal.

Allowing incumbents to hold out proposals until very late in the process, even after PJM approves a competing project, allows incumbents the opportunity to oppose a project in the RTEP and to offer a competing proposal only when it is clear that some project addressing a system issue will go forward. The timeframe for proposing and considering projects should be redesigned to discourage such stratagems. Otherwise, the rules not only remove the incentive for competitors to propose projects in locations where incumbents

have a conflicting interest in local generation supply resources, but actively discourage such potential competitors. The effect on competition is the same as that produced by a right of first refusal and is correspondingly antithetical to the goals of Order No. 1000.

Furthermore, the rules should not permit project sponsors to recover costs in excess of the costs PJM used in selecting a project. In *Primary Power*, PJM cited lower costs as a basis for its selection but there was and could be no actual support for that position. There are no limits on the costs recovered by project sponsors, regardless of how they compare to the costs used to evaluate competing alternatives. Project sponsors should be required to honor their costs as submitted or within a narrowly defined band and not be able to raise costs that served as the basis for their selection. Otherwise, sponsors will have an incentive to engage in strategic behavior.

Presumably, because PJM recognizes that some elements of its proposal may be outside of the scope of compliance with Order No. 1000, PJM also filed pursuant to section 206 of the Federal Power Act.<sup>5</sup> Because PJM does not, and cannot consistent with its independence, have a financial or commercial interest in these rules, PJM presumably files this complaint against itself for public interest reasons. The Market Monitor agrees that the Commission's rules permit complaints for public interest reasons by entities with tariff-defined responsibilities. An explicit determination that such complaints are properly filed under the Commission's rules would remove any doubt.

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<sup>5</sup> 18 USC § 824d.

## I. COMMENTS

### **A. In Order to Meet the Policy Objectives of Order No. 1000, PJM's Proposal Should Be Modified to Include Provision for Competitive Financing.**

The Market Monitor agrees with the Commission's support, in Order No. 1000, to create a new competition-based approach to the development of transmission.<sup>6</sup> This approach holds special promise in the PJM region, and other RTO/ISO regions, where an established independent entity operates and plans the transmission system. Order No. 1000 requires the elimination of transmission owners' right of first refusal and the establishment of a transparent and non discriminatory process for selecting the projects included in the RTEP.<sup>7</sup> PJM's rules do not contain an explicit right of first refusal, but the results in *Primary Power* show that the current rules allow a de facto right of first refusal to apply. Unless PJM's proposal includes additional features to avoid this result, the opportunity to take correction action in this filing will be lost and the policy objectives of Order No. 1000 cannot be realized.

The optimal improvement, within the framework defined by Order No. 1000, is provision for competitive procurement of capital. Order No. 1000 explicitly declined to "mandate a competitive bidding process for selecting project developers." PJM can select the projects to develop through the RTEP process without establishing a process for competitive bidding. However, once PJM has selected among proposed projects, PJM should select the source of capital based on a competitive process rather than the traditional cost of service and/or incentive rate approach. There is no reason why the development of a project, in the sense of constructing and owning it, cannot be separated from its financing.

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<sup>6</sup> See, e.g., Order No. 1000 at P 285 ("federal rights of first refusal in favor of incumbent transmission providers deprive customers of the benefits of competition in transmission development, and associated potential savings").

<sup>7</sup> See Order No. 1000 at PP 293-340.

A competitive market can best determine the cost of capital required for a project. This is true for the same reasons that the Commission has introduced regulation through competition elsewhere.<sup>8</sup> Competitive procurement of capital could attract potential nonincumbent participation to provide capital for all projects developed and included in the RTEP. Meanwhile, PJM, with advice from stakeholders and the oversight of the PJM Board, could continue to independently evaluate and select, on the basis of the most transparent criteria possible, the projects that best promote the public interest in obtaining reliable power at least cost. PJM and its stakeholders should continue to look for ways to enhance PJM's independence, objectivity and transparency in making these determinations.

Competitive procurement of capital avoids the difficult but less important issue, from a cost perspective, of who holds title to a project and who constructs a project.

In *Primary Power*, a non incumbent received preliminary approval for a package of incentives and other elements of a future cost-of-service filing, subject to future cost-of-service rate filings and the project's inclusion in the PJM RTEP.<sup>9</sup> That incentive package reflected the Commission's assessment of the "the demonstrable risks or challenges faced by the applicant."<sup>10</sup> With some elements of its rate determined on a preliminary basis, the nonincumbent's task was to ensure that that its project was included in the RTEP with itself designated as the sponsor to finance, develop and own the project. In other words, the competition occurred between incumbent transmission owners, and nonincumbent

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<sup>8</sup> See *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, FERC Stats. & Regs. ¶ 31,036 (1996) ("Order No. 888"), *order on reh'g*, Order No. 888-A, FERC Stats. & Regs. ¶ 31,048, *order on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *aff'd sub nom. New York v. FERC*, 535 U.S. 1 (2002).

<sup>9</sup> See *Primary Power, LLC*, 131 FERC ¶ 61,015 (2010).

<sup>10</sup> *Id.* at P 151.

transmission owners seeking to stand in the shoes of incumbents. A competition for incumbent status falls short of the benefits a competitive transmission policy could achieve.

Competitive procurement of capital would provide the Commission a basis to establish lawful transmission pricing.<sup>11</sup> It employs essentially the same justification on which the Commission relies to authorize suppliers to charge market-based rates.<sup>12</sup>

If the policy promoting competitive transmission investment emphasized competition to provide capital, the problems related to project identity, upgrades versus new projects, control over physical assets and access to property could be reduced or avoided. Ownership of projects in the sense of title and property access could remain with incumbents even if a non incumbent financed the project. Competition to construct projects already occurs among the discrete group of firms capable of constructing of transmission projects. Competitive financing should have no impact on who actually constructs projects.

The competitive process should select as the project's source of capital the lowest cost supplier of capital. Suppliers of capital would determine their own required returns, and the Commission would avoid the need to make these determinations administratively.

The sponsorship model creates numerous issues that complicate selecting between incumbent and nonincumbent projects. Although this approach does promote the public interest in ameliorating vertical market power, it does not harness competition to ensure that transmission projects are built at least cost. Ultimately, under PJM's proposed sponsorship model, the Commission must still rely on the traditional cost of service

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<sup>11</sup> *Market-Based Rates for Wholesale Sales of Electric Energy, Capacity and Ancillary Services by Public Utilities*, Order No. 697, FERC Stats. & Regs. ¶ 31,252 (2007), *clarified*, 121 FERC ¶ 61,260 (2007), *order on reh'g and clarification*, Order No. 697-A, FERC Stats. & Regs. ¶ 31,268, *clarified*, 124 FERC ¶ 61,055, *order on reh'g and clarification*, Order No. 697-B, FERC Stats. & Regs. ¶ 31,285 (2008), *order on reh'g and clarification*, Order No. 697-C, FERC Stats. & Regs. ¶ 31,291 (2009), *order on reh'g and clarification*, Order No. 697-D, FERC Stats. & Regs. ¶ 31,305 (2010), *order on clarification*, 131 FERC ¶ 61,021, *reh'g denied*, 134 FERC ¶ 61,046 (2010), *reh'g pending*.

<sup>12</sup> *See, e.g., Id.* at PP 943–955.

approach that the Commission has found inadequate for regulating supply.<sup>13</sup> This compliance proceeding presents an opportunity for the Commission to direct PJM to develop a process for pricing transmission projects consistent with competition.

A key cost driver for transmission projects is the cost of capital. Competition among suppliers of capital willing to bear investment risks at least cost would allow the Commission to facilitate the robust transmission system that it has determined the nation needs, at substantially lower cost than would otherwise be possible.<sup>14</sup> Having already authorized PJM and other RTOs as independent system operators and planners, there is no reason not to take this additional step to realize the full potential of these organizations and extend the application of the Commission's pro competition regulatory principles to the transmission sector.

#### **B. The Proposed Selection Is Not Complete Without Transparent Selection Criteria.**

Adding provision for competitive sources of capital would best improve the October 10<sup>th</sup> Proposal. Adopting the competitive financing approach means significantly modifying the sponsorship model used in *Primary Power*, but the two could coexist if competitive financing were required of all sponsors. If the need for significant modification is not

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<sup>13</sup> See, e.g., Order No. 888 mimeo at 48–49 (“The many changes discussed above have converged to create a situation in which new generating capacity can be built and operated at prices substantially lower than many utilities embedded costs of generation. As discussed above, new generation facilities can produce power on the grid at a cost of less than 3 cents per kWh to 5 cents per kWh, yet the costs for large plants constructed and installed over the last decade were typically in the range of 4 to 7 cents per kWh for coal plants and 9 to 15 cents for nuclear plants. Non-traditional generators are taking advantage of this opportunity to compete. Indeed, the non-traditional generators' share of total U.S. electricity generation increased from 4 percent in 1985 to 10 percent in 1993. Much of this increased share of generation is the result of competitive bidding for new generation resources that has occurred in 37 states.” [footnotes omitted].).

<sup>14</sup> See, e.g., U.S. Department of Energy, National Electric Transmission Congestion Study (December 2009), which can be accessed at: <[http://www.congestion09.anl.gov/documents/docs/Congestion\\_Study\\_2009.pdf](http://www.congestion09.anl.gov/documents/docs/Congestion_Study_2009.pdf)>; FERC Staff, National Action Plan on Demand Response (June 17, 2010), which can be accessed at: <<http://www.ferc.gov/legal/staff-reports/06-17-10-demand-response.pdf>>.

accepted, then the *Primary Power* sponsorship model still requires substantial improvement. The October 10<sup>th</sup> Proposal fails to provide it.

In *Primary Power*, the issue of whether PJM's existing procedures under Schedule 6 constituted a sponsorship model of procurement was contested.<sup>15</sup> The October 10<sup>th</sup> Proposal resolves that issue in favor of a sponsorship model.<sup>16</sup> The proposal does little else. Most significantly, it fails to address issues manifest in *Primary Power* relating to transparency and incentives. Those issues pose an obstacle to future participation by nonincumbents.

A key objective of Order No. 1000 is removal of the right of first refusal from RTO tariffs.<sup>17</sup> Removal of such a preference for incumbents should encourage participation in the RTEP by nonincumbents. A de facto right of first refusal will prevent achievement of that objective just as effectively as one that is de jure.

In *Primary Power*, incumbents proposed projects that displaced a nonincumbent's project very late in the process.<sup>18</sup> Allowing incumbents to hold out proposals until very late in the process, even after PJM approves a competing project, allows incumbents the opportunity to oppose a project in the RTEP and to offer a competing proposal only when it is clear that some project addressing a system issue will go forward.<sup>19</sup> The timeframe for

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<sup>15</sup> See 140 FERC ¶ 61,054 at P 49.

<sup>16</sup> October 10<sup>th</sup> Proposal at 13 (“This proposed process is a sponsorship model whereby both incumbent transmission owners and nonincumbent transmission developers may propose transmission projects for inclusion in the RTEP.”).

<sup>17</sup> Order No. 1000 at P 284 (“[G]ranting incumbent transmission providers a federal right of first refusal with respect to transmission facilities selected in a regional transmission plan for purposes of cost allocation effectively restricts the universe of transmission developers offering potential solutions for consideration in the regional transmission planning process. This is unjust and unreasonable because it may result in the failure to consider more efficient or cost-effective solutions to regional needs and, in turn, the inclusion of higher-cost solutions in the regional transmission plan.”).

<sup>18</sup> 140 FERC ¶ 61,054 at PP 8–12.

<sup>19</sup> See *Id.* at P 11.



proposing and considering projects should be redesigned to discourage such stratagems. Otherwise, the rules not only remove the incentive for competitors to propose projects in locations where incumbents have a conflicting interest in local generation supply resources, but actively discourage such potential competitors. The effect on competition is the same as that produced by a right of first refusal and is correspondingly antithetical to the goals of Order No. 1000. The rules should encourage sponsors to propose all projects intended to address the same need early in the process.

Furthermore, the rules should not permit project sponsors to recover costs in excess of the costs PJM used in selecting a project. In *Primary Power*, PJM cited lower costs as a basis for its selection but there was and could be no actual support for that position.<sup>20</sup> There are no limits on the costs recovered by project sponsors, regardless of how they compare to the costs used to evaluate competing alternatives. Project sponsors should be required to honor their costs as submitted or within a narrowly defined band and not be able to raise costs that served as the basis for their selection. Otherwise, sponsors will have an incentive to engage in strategic behavior.

Nonincumbents will not continue to participate in RTEP and propose projects if they have no prospect to obtain a benefit, or worse, are more likely to be stuck with unrecoverable costs.<sup>21</sup> The rules should provide some assurance to sponsors that they will not be unfairly undercut.

The sponsorship model used in *Primary Power* left too many concepts undefined. They remain undefined in the October 10<sup>th</sup> Proposal. The October 10<sup>th</sup> Proposal does not explain how to differentiate one sponsor's project from another's when both projects address approximately the same problem, using approximately the same technology, in

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<sup>20</sup> 140 FERC ¶ 61,054 at PP 36, 75.

<sup>21</sup> See Request for Clarification, or in the Alternative, Rehearing of Primary Power, LLC, filed in Docket No. EL12-69-001 (Aug. 20, 2012).

approximately the same location. This was an issue in *Primary Power*.<sup>22</sup> The October 10<sup>th</sup> Proposal does not define what constitutes a discrete project. The rules should define what changes to a project are material to its remaining the same project or its becoming a different project. The factors relied upon by the Commission in *Primary Power* would be a good starting place.<sup>23</sup>

The October 10<sup>th</sup> Proposal does not define types of the projects that, under Order No. 1000, nonincumbents may not sponsor, including upgrades and projects located on an incumbent's property or in its rights of way.<sup>24</sup> These exceptions are significant, and the rules that apply Order No. 1000's concepts must define those concepts with greater precision.

PJM also needs to explain its decisions so that they are better understood and accepted. If PJM does not want to decide between projects on the basis of an objective evaluation of costs alone, then it needs to outline in more detail how it evaluates costs relative to other factors. PJM acknowledged that these criteria are lacking in *Primary Power*, but still failed to develop and include any criteria in the October 10<sup>th</sup> Proposal.<sup>25</sup>

### **C. PJM Has Standing to File a Complaint Against Itself, Even Though It Has No Financial Interest in This Proceeding.**

Presumably, because PJM recognizes that some elements of its proposal may be outside of the scope of compliance with Order No. 1000, PJM also submitted its proposal pursuant to section 206 of the Federal Power Act.<sup>26</sup> Because PJM does not, and cannot,

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<sup>22</sup> 140 FERC ¶ 61,054 at PP 78–79.

<sup>23</sup> *Id.* (Citing to “the design and operation of the facilities, the point of interconnection, the voltage ratings used, differences in operational flexibility, simpler construction, the use of existing infrastructure, and coordination with other available resources.”).

<sup>24</sup> Order No. 1000 at P 319.

<sup>25</sup> Motion to Intervene and Comments of PJM Interconnection, L.L.C., filed in Docket Nos. ER10-253, EL10-14 (December 11, 2009) at 6.

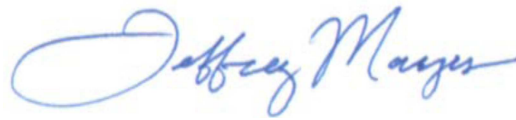
<sup>26</sup> 18 USC § 824d.

consistent with its independence, have a financial or commercial interest in these rules, PJM presumably files this complaint against itself for public interest reasons. The Market Monitor agrees that the Commission's rules permit complaints for public interest reasons by entities with tariff-defined responsibilities. An explicit determination that such complaints are properly filed under the Commission's rules would remove any doubt.

## II. CONCLUSION

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

Respectfully submitted,



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Dated: December 10, 2012

**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 10<sup>th</sup> day of December, 2012.



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