UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

PJM Interconnection, L.L.C.	))))	Docket Nos. ER11-2875-000, -001 and -002, EL11-20-000 and -001

MOTION FOR CLARIFICATION OF THE INDEPENDENT MARKET MONITOR FOR PJM

Pursuant to Rule 212 of the Commission's Rules and Regulations,[1] Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor for PJM ("Market Monitor"), moves for clarification of the Commission's orders of April 12, 2011 ("April 12th Order") and November 17, 2011 ("November 17th Order"). In those orders, the Commission approved a revised Minimum Offer Price Rule ("MOPR"), consisting of a "benchmark" or "reference" value by unit class against which to determine whether or not an offer raised buyer-side market power issues.[2] The Commission also approved a unit specific review process to allow sellers the opportunity to obtain a lower unit specific value based on the particular facts and circumstances of its unit. In order to ensure that the nature and purpose of the unit specific review process is understood, the Market Monitor requests that the Commission grant clarification that the MOPR reference value and the method by which it is calculated constitute the core MOPR standard. In order to obtain approval of a unit specific value lower than that reference value, the burden is on the seller to demonstrate

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[1] 18 CFR § 385.212 (2011).

[2] *PJM Interconnection, L.L.C., et al.*, 135 FERC ¶61,022 (April 12, 2011) ("April 12th Order"); *order on compliance and reh'g*, 137 FERC ¶ 61,145 (November 17, 2011) ("November 17th Order").

that its actual costs result in a lower value. This review is case specific. Unit specific review is not an invitation to reopen an inquiry about whether the method used to calculate the reference value is an appropriate method, or whether alternative methods are available that can produce lower values.

Clearly, different methods than those employed to establish the reference value can produce a result lower than the reference value. But a seller should not be able to pass the MOPR screen simply by applying a different set of methodological assumptions to the MOPR calculation rather than demonstrating that actual project costs are lower than for the MOPR reference unit. To do so would be to permit the MOPR screen to be passed by assumption and would make the MOPR rule virtually meaningless.

The Market Monitor requests that the Commission clarify that the approach to calculating the objective reference value is not within the Market Monitor's or PJM's discretion to change, and that unit specific review means a review based on the specific facts and circumstances of a particular project, using exactly the same modeling assumptions used to calculate the MOPR screen value. Unit specific review does not imply an opportunity to change the modeling approach in a way that would establish a lower reference value. In addition, it must be clear that this review of facts and circumstances does not permit incorporating the impact of non-market revenues including subsidies or revenue guarantees in the project cost.

I. MOTION

The Commission has reviewed the MOPR reference value developed by PJM and approved it, subject to certain modifications, as just and reasonable and not unduly discriminatory.[3] The approved reference value is reasonable and sufficient to protect PJM markets from buyer-side market power.

In approving the MOPR reference value, the Commission also considered and approved the specific assumptions used to establish that reference value:

> We find that PJM's proposal as accepted in the April 12 Order establishes a just and reasonable administrative method for calculating the MOPR reference values consistent with the existing VRR Curve guidelines. These reference values establish a reasonable estimate of the average annualized cost (net of expected energy and ancillary service revenues) that a new entrant would incur to enter the market. In contrast with the view of the Maryland Commission, we conclude that a competitive capacity market would provide annual revenues over time that, on average, would approximate Net CONE. If annual revenues were significantly lower, prospective developers of new capacity would not enter the market, because they would not expect to recover the costs of their investments over time. Consequently, expecting that a typical supplier acting competitively would not likely offer to provide new capacity at a price significantly below its net entry cost is reasonable. Thus, a reasonable offer floor would be near Net CONE.[4]

The reference value sets an objective standard that should apply except in specific cases where the objective facts and circumstances of a particular project support a value lower than the reference value. As the Commission explained:

> Offers above the MOPR reference values, based on Net CONE, are not mitigated. Offers below these MOPR values, however, are not automatically mitigated, as a mitigation determination is subject to the seller availing itself of the unit-specific review process.[5]

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3 April 12th Order at P 43.

4 November 17th Order at P 25.

5 *Id*. at P 26.

A unit specific review means a review of the facts and circumstances of a particular project. Performance of such a review necessarily requires the existence of an actual specific project to evaluate. The particular aspect(s) of the project supporting special treatment, such as the location, technology choice, design, equipment contracts and construction contracts must be in place or near final. The MOPR reference value is based on a specific analytical, or modeling, approach using specific assumptions. If a seller wants to challenge those assumptions, then the appropriate recourse is to file a complaint with the Commission or to convince PJM to file a rule change. Limiting unit specific review under MOPR to a generating unit's specific facts and circumstances and the specific MOPR modeling approach is consistent with unit specific reviews in other aspects of PJM's mitigation program. The PJM market rules set forth common methods for calculating unit specific offer caps in the energy markets and in RPM. There is no reason to apply a different standard to unit specific offer reviews under MOPR.

The Market Monitor should not have the discretion to change the MOPR reference value by adopting a different set of assumptions than those used to calculate the reference value. Market sellers should not have the discretion to support an exception to the MOPR reference value by adopting a different set of assumptions than those used to calculate the reference value.

Any seller could generate a lower first year project cost by changing the assumptions used to calculate the reference value, holding everything else constant. The Market Monitor includes an Attachment that shows that changing the assumption about unit life and the assumption about the levelization method can dramatically change the project cost in the first year. The table shows gross CONE values for the MOPR combined cycle (CC) technology under a range of assumptions. The table shows that the first year cost can be reduced from $421.05 per MW-day under the MOPR assumptions to $359.93 by changing the assumed method from nominal levelization to real levelization, with a 2.5 percent annual escalation in revenues. The table shows that the first year cost can be reduced from $421.05 per MW-day under the MOPR assumptions to $396.12 by changing the assumed life of the unit from 20 to 30 years. (This is identical to assuming a residual value for the project.) The table shows, in the most extreme case, that the first year cost can be reduced from $421.05 per MW-day under the MOPR assumptions to $152.90 per MW-day by changing the assumed life of the unit from 20 to 30 years and using real levelization with a 10.0 percent annual escalation in revenues.

Any seller seeking to establish a lower value could claim a longer expected life or a different levelization method or a different expected escalation rate. These are all modeling assumptions and not based on the facts and circumstances of actual projects. In order to apply the MOPR test and in order to not discriminate among potential projects, the modeling assumptions must be the same for all projects. Projects should be able to demonstrate that their costs are lower because they have a competitive advantage and not because they select the most advantageous modeling assumptions.

Units with a subsidized revenue stream have a strong incentive to pick advantageous modeling assumptions because passing the MOPR test with a low offer which also clears in an RPM auction means that they are guaranteed that subsidized revenue stream.[6] The guaranteed subsidized price can exceed their offer into the RPM

[6] For example, both the New Jersey LCAPP and the Maryland RFP process require units to pass MOPR and clear in an RPM auction in order to receive the guaranteed contract price.

auction and exceed the RPM clearing price. The subsidized price can also exceed the unit's MOPR exception value and exceed the MOPR screen value.

Selective use of favorable modeling assumptions also creates the potential to distort market outcomes because it can make a more expensive project appear to be cheaper. The result could be that the more expensive project clears in the RPM auction while the less expensive project does not clear. This would be a non-competitive outcome.

Selective use of favorable modeling assumptions also creates the potential to distort the MOPR exception review process. If there are two sellers with identical projects and identical costs, seller A can make their project costs appear lower through modeling assumptions. If the MMU rejects that approach and seller A appeals to the Commission, this creates a risk for seller B. If seller A's approach is upheld, seller A will have an advantage in the RPM auction. This, in turn, creates an incentive for all participants to make aggressive modeling assumptions in order to gain an advantage. But these assumptions have nothing to do with actual costs or actual competition.

It is essential that all projects use the same basic modeling assumptions and that the standard of review uses the same basic modeling assumptions. That is the only way to ensure that projects compete on the basis of actual costs rather than on the basis of modeling assumptions.

The Commission approved the process for unit specific review despite objections that such a process would accord undue discretion to the Market Monitor. The Commission explained:

> PJM notes that the Commission rejected a proposal to replace the current MOPR with a provision that would have given responsibility to the IMM to determine whether a seller's new entry offer was an exercise of market power.[citation omitted] The Commission did not, however, object to the IMM participating in

> the process of making this determination. Instead, the Commission objected to a proposal that would have given the IMM "unfettered discretion" to make such determinations unilaterally through a process that would have lacked the certainty for market participants that more objective MOPR tariff standards could provide.[citation omitted] The procedure proposed by the IMM and accepted here does not give the IMM the discretion to unilaterally decide whether a resource gets mitigated. We therefore find that the IMM's proposal is consistent with our precedent.[7]

If, in the unit specific review process, the Market Monitor can accept a change in the assumptions used to calculate the MOPR reference value in order to calculate a unit specific value, then, all else constant, it would have "the discretion to unilaterally decide whether a resource gets mitigated." The Market Monitor does not want or need such discretion. The better approach is to establish the assumptions that will be used to determine both the reference values and unit specific values. Unit specific reviews should be limited to the facts and circumstances of a specific project.

In the April 12th Order the Commission approved a single objective standard.[8] Despite its initial concerns about excess discretion, PJM submitted a unit specific process for review that weakened the objective standards and introduced subjective aspects to the process for unit specific review. PJM also requested rehearing on the Commissions' directive in the April 12th Order that unit specific review should include the same nominal levelization method used in calculating the MOPR reference values. The Commission

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7 April 12th Order at P 120.

8 April 12th Order at P 43.

accepted PJM's compliance standard, including granting rehearing on the levelization issue in the November 17th Order.

The Commission explained:

> After reviewing the public comments and upon further reflection, we conclude that the April 12 Order's implication that it would always be irrational for a new entrant to offer at a price based on the real levelized method was not justified. We agree with PJM that, while the nominal cost recovery method is appropriate for the MOPR screen, requiring that cost recovery method during the unit-specific review process is unnecessary. In making a case to the IMM, PJM, or the Commission, parties should have the opportunity to present a reasonable business case based on their individualized facts and circumstances, including the use of a different depreciation model. The case-by-case nature of the unit-specific exemption process allows for the IMM, PJM, and the Commission to consider more carefully the different circumstances of individual sellers. Thus, we grant rehearing of the April 12 Order's requirement that the standard of review applicable to the unit-specific review process reflect the use of the nominal levelized methodology, without exception. Accordingly, we direct PJM to submit a compliance filing revising its Tariff to eliminate the requirement that parties must use the nominal levelized methodology in a unit-specific review.[9]

Consequently, the Market Monitor now has discretion to accept costs calculated on a real levelized basis rather than on a nominal levelized basis. Other things held equal, any seller can demonstrate a lower value than the reference value for a project that is identical to the reference project simply by using real levelization. Real levelization is not based on a different depreciation method than nominal levelization. All projects use the most advantageous depreciation method. Real levelization is simply a modeling assumption. At the same time, the Commission also made clear that unit specific review means an

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[9] November 17th Order at P 75.

opportunity for the seller "to present a reasonable business case based on their individualized facts and circumstances." This implies that the Commission would not accept a simple preference for using a particular levelization approach in order to obtain a lower value. The intent, as the Market Monitor understands it, is not to revisit the Commission-approved assumptions reflected in the MOPR reference value.

Clarity is also needed to establish which facts and circumstances are relevant to a MOPR analysis and which are not. The point of MOPR is to ensure competitive offers. Competitive offers are offers based on actual costs, without non-market revenues, which will succeed or fail in the market based on its offer. When a seller's facts and circumstances include non-market revenues and/or subsidies, then the impact of those facts and circumstances must be removed from the proposed offer. For example, if a unit has a subsidized revenue stream that is guaranteed if it passes MOPR, that is a fact and circumstance that should not be permitted to affect the offer. The MOPR rule is designed to address precisely such subsidies and their impacts on offers and to prevent them from affecting offers.

The Market Monitor is likely to address two classes of project sponsor in unit specific reviews. One class of sponsor will rely entirely on market revenues to support its project. Another class of sponsor will have access to revenues or guarantee of revenues that will insulate it from having to rely entirely on market revenues to support its project. The first class of sponsor, "market sponsors," has an incentive to be competitive based on actual project costs because such sponsors make money only if their project costs are competitive. Market sponsors do not make money if their offer is below their costs and they clear RPM at that level.

The second class of sponsor, "non-market sponsors," has an incentive to make the lowest possible offer so as to pass the MOPR screen and to clear in the RPM auction because these are the requirements for receiving the subsidized revenue stream. Non-market sponsors make money if their offer is below their costs and they clear RPM at that level.

The most relevant facts and circumstances of such non-market sponsors create a need for MOPR review. In this case, the object of MOPR review is to determine the offer that a non-market sponsor would offer if they were making a competitive offer. Any particular facts about the specific project that could justify a lower offer, like a low cost site or a low cost EPC contract, should be reflected in the offer. However, non-market sponsors should not be permitted to reduce their offers based on modeling assumptions rather than actual lower costs. The MOPR standard is designed to incorporate the assumptions used in competitive, market-based offers. It follows that a non-market sponsor should be required to use those assumptions. If those assumptions are not correct, then the solution is to change the MOPR standard for all participants rather than to create an exception for one participant. Such an exception would create the incentives for all such participants to take the same approach. Such an exception would result in non-market sponsors being taken ahead of market sponsors. That would be a non-competitive result and a result inconsistent with the basic purpose of MOPR.

Clarity on this point could avert considerable confusion and would avoid bringing multiple disputes about MOPR issues to the Commission in the near future.

As an example, one area of likely dispute will be the levelization method. If the opportunity to justify use of a real levelized method is preserved, it should only be available to market sponsors. It would not undermine the MOPR to allow market sponsors the opportunity to argue for use of real levelized approach based on a demonstrated willingness to use this approach in making competitive market-based investment decisions. The same logic should apply to other modeling assumptions.

Non-market sponsors should not be permitted to use a real levelized method. As the examples provided in the Attachment demonstrate, projects that are identical to the MOPR reference unit can be demonstrated to be lower cost than the MOPR reference unit solely on the basis of modeling assumptions. The same logic should apply to other modeling assumptions.

Clarification from the Commission is needed to ensure that the focus of unit specific review remains an inquiry about the actual costs of particular projects and does not permit those sellers with an incentive to offer at below cost to defeat the intent of the MOPR rule by using modeling assumptions to artificially reduce their first year project costs. The unit specific review process should preserve the ability to apply objective standards, and to discourage relitigation of the analytical assumptions used to develop the generally applicable MOPR standard.

II. CONCLUSION

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

Respectfully submitted,

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Dated: February 17, 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 17th day of February, 2012.

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Attachment

Table 1 Impact of modeling assumptions on first year cost of MOPR reference unit (CC)

Project Evaluation Life (Years)	20 Years	20 Years	30 Years	30 Years	20 Years	30 Years
Case Number	1 (Base)	2	3	4	5	6
Levelization Type	Nominal	Real Year 2015	Nominal	Real Year 2015	Real Year 2015	Real Year 2015
Revenue Requirements ($/MW-Day)	$421.05	$359.93	$396.12	$325.98	$207.92	$152.90
Revenue Escalation (%)	0.0%	2.5%	0.0%	2.5%	10.0%	10.0%