

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

PJM Interconnection, L.L.C.

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Docket No. ER13-1654-001

**ANSWER AND MOTION FOR LEAVE TO ANSWER
AND TO FILE COMMENTS OUT-OF-TIME
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 PJM² ("Market Monitor"), submits this answer and motion for leave to answer the answer filed by PJM Interconnection, L.L.C. ("PJM") on October 8, 2013, and the comments filed by the Financial Marketers Coalition³ ("Financial Marketers") on October 9, 2013, and moves for the Commission to accept comments filed by the Market Monitor on October 1, 2013 (October 1st Comments), four days out-of-time. This answer is necessary to respond to inaccurate and confusing assertions made in response to the Market Monitor's October 1st Comments and the Market Monitor's proposal to apply the FTR Forfeiture Rule to up to congestion transactions ("UTCs") in the same manner that the rule applies to other virtual transactions.

¹ 18 CFR § 385.212 & 385.213 (2012).

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

³ Financial Marketers state (at 1): "For purposes of this pleading, the Financial Marketers Coalition consists of XO Energy MA, LLC; Red Wolf Energy Trading, Monterey MA, LLC, Solios Power, LLC, and Great Bay Energy, LLC."

I. ANSWER

A. The Financial Marketers Argument That the FTR Forfeiture Rule Should Not Be Consistently Applied Across Virtual Products Should Be Rejected.

The Financial Marketers recognize (at 8) that the Market Monitor is correct that under PJM's proposal, "the FTR Forfeiture Rule is applied in a different manner for UTC transactions than it is applied for incs/decs." The Financial Marketers incorrectly assert (at 9) that the difference in treatment of UTC transactions, and INCs and DECS in PJM's proposal is justified because of differences between these virtual products. The Financial Marketer's defense of unequal and preferential treatment for UTC bids fails because it is based on the contract path fiction addressed by the Market Monitor's October 1st Comments.

The Financial Marketer's assert that because INCs and DECS involve single points and UTCs involve paired source and sink points, these virtual transactions should be treated differently under the FTR Forfeiture rule. This assertion is based on the false assumption that flows from INCs and DECS follow different rules than flows from UTCs. The Financial Marketers argue (at 8) that, in the case of UTCs, "all of the energy injected at the source will be withdrawn at the sink." As explained in the IMM's comments, this assertion simply and incorrectly assumes that UTC flows follow their contract path.⁴ While UTC transactions are paired, the power injected at the UTC source is not all withdrawn at the UTC sink. The power flows across the system based on the characteristics (impedances) of the transmission system and is withdrawn at multiple points.

For example, in a constrained system, if a UTC increases congestion on a constraint (by sourcing on the unconstrained side and sinking on the constrained side) the UTC will require the simultaneous increase in generation in the constrained area and decrease in generation in the unconstrained area to prevent the violation of the constraint. This is

⁴ October 1st Comments at 3.

because the binding constraint, by definition, prevents the UTC injection from actually flowing from the UTC source to the UTC sink. Once a constraint is binding, the distribution factor (dfax) of the UTC source and sink to the constraint indicates the portion of the UTC flow that affects the constraint and thereby contributes to the need to relieve the constraint to maintain system security. To maintain system security, the induced flow in excess of line limits (the relief required) must be offset by increases in net injections on the constrained side and/or decreases in net injections on the unconstrained side. This accommodation of the UTC flow increases congestion and therefore affects the value of the related FTR. The offsetting increases and/or decreases in net injections within the least cost security constrained dispatch contributes to the costs to relieve the constraint, which is reflected in the shadow price of the constraint (the marginal cost to relieve the constraint) and increased congestion.

UTC transactions, like INCs and DEC, can increase the flow on a constraint, contributing to the need for constraint relief, which affects congestion on the constraint and thereby affecting the value of a participant's FTR. The FTR Forfeiture Rule should therefore operate in exactly the same fundamental way for both UTCs and INCs and DEC.

The Market Monitor is proposing the equivalent treatment of UTC bids, based on whether the UTC is a net injection or withdrawal relative to a constraint. If the UTC is a net withdrawal relative to the constraint, it is treated as a DEC. If the UTC is a net injection relative to the constraint, it is treated as an INC.

As defined in the Tariff, the effect of a transaction on a constraint between an FTR source and sink point is the desired metric. The Financial Marketers (at 9–11) reiterate the Market Monitor's approach to UTC forfeitures. In their summaries of the presented examples they succinctly demonstrate how the Market Monitor's proposed FTR Forfeiture Rule for UTC transactions is similar to the existing INC and DEC FTR Forfeiture Rule, while accounting for paired transactions. The Market Monitor agrees that the amount of power injected at a UTC's source and withdrawn at a UTC's sink is the same, but the source of that power varies based on system topology. As the Financial Marketers point out (at 8), "due to

the basic laws of physics, the energy may not flow in exactly the same path to reach the sink from the source”, so this power must come from various other buses to fill the required transaction quantity. By only including the source and sink points in the forfeiture process, the proposed PJM approach does not account for the actual flows, while the Market Monitor’s approach measures the net impact of the UTC on the constraint, consistent with the basic laws of physics.

B. The Financial Marketers’ Interpretation and Analysis of the Market Monitor’s Examples Is Incorrect.

The Financial Marketers claim (at 9–11) that the examples that the Market Monitor included in its October 1st Comments are flawed. However, the Financial Marketers are mistaken in their analysis of the examples, specifically in their interpretation of the dfax, and dfax triggers, as used in FTR Forfeiture Rule. The Financial Marketers oppose the Market Monitor’s approach which compares the net dfax of the UTC to the largest impact injection or withdrawal on the opposite side of the constraint. The Financial Marketers claim that the dfax metrics misrepresent flows on the constraint and note that some dfax differences are greater than 100 percent.

The Financial Marketers object to the FTR Forfeiture Rule under the guise of disagreeing with its application to UTCs. Under the INC/DEC FTR Forfeiture Rule, the difference between the dfax of an INC or DEC and the dfax of the largest impact withdrawal or injection can be greater than 100 percent, due to the combined effect of the injection and withdrawal. For example, if an INC offer is placed at a bus with a dfax of 1.0, and the largest impact withdrawal has a dfax of -0.5, the existing FTR Forfeiture Rule would assign this a value of 1.5, over the 0.75 threshold, and flag it for forfeiture. In theory, the maximum difference is 2.0. While an individual bid or transaction cannot impact a constraint more than 100 percent, the dfax difference calculation shows the relative impact of a bid or offer, in combination with another bid or offer, on the constraint. Therefore a high dfax injection in combination with a high dfax withdrawal on the other side of a

constraint appropriately triggers the rule when the difference is greater than .75. The dfax comparison metric is the metric used to detect this combined impact on the constraint.

C. PJM Incorrectly Asserts That the Existing FTR Forfeiture Rule Is Only Applied to INCs and DECs with Positive Dfax Values.

PJM asserts (at 4) that “[t]he inclusion of only positive net dfax values is consistent with the existing application of the FTR Forfeiture Rule to INCs and DECs which only includes positive dfax values.” PJM’s assertion that the existing FTR Forfeiture Rule for INCs and DECs only includes positive dfax values is not correct. PJM relies on the IMM to apply the FTR Forfeiture Rule and all associated calculations. The IMM performs the FTR Forfeiture analysis and calculates the FTR forfeiture amounts, which are then communicated to and applied by PJM in its settlement process. The IMM’s FTR Forfeiture Rule analysis includes the examination of INCs and DECs with positive and negative dfax values. In the IMM’s FTR Forfeiture Rule analysis the only time the sign of the dfax value, positive or negative, is considered is to exclude INCs on the constrained or DECs on the unconstrained side of a constraint, since in both cases such bids help rather than hurt the constraint and therefore cannot make the associated FTR more valuable.

In the case of INCs and DECs, if only positive dfax values were considered then all DECs on the constrained side would pass the forfeiture test, even though they hurt the constraint. This is not the way the rule is currently applied to INCs and DECs.

PJM is not proposing to change the application of the FTR Forfeiture Rule to INCs and DECs. The application of the FTR Forfeiture Rule as applied to INCs and DECs is beyond the scope of this proceeding. However, due to PJM’s apparent misunderstanding of the FTR Forfeiture Rule as applied to INCs and DECs, PJM is proposing that the FTR Forfeiture Rule, as applied to UTCs, only consider UTCs with the positive net dfax values.

The problem with PJM's proposal to keep only the positive net dfax values is demonstrated in the Market Monitor's previous filing in Figure I-5.⁵ In this example, a UTC has a negative net dfax, creating additional flows on a constraint and thus increasing congestion, yet the PJM proposal would ignore the UTC for purposes of the rule. In the reverse case, a UTC has a positive net dfax, reducing net flows on the constraint and thus reducing congestion, the PJM proposal would treat the UTC as failing the rule. Both results under the PJM rule are clearly illogical.

D. PJM's Proposal Continues To Be Unclear On Essential Details.

PJM indicates (at 4) that they have "struggle[d] to understand the need for, and even the nature of, the further refinements and detail the IMM believes constitute improvements to PJM's proposed application of the FTR Forfeiture Rule to UTC Transactions." The method proposed by the Market Monitor is more sophisticated than the one proposed by PJM because such complexity produces a result that is significantly more accurate and fair to market participants. The Market Monitor's method requires no more computational power than the PJM proposed method, or than the existing method for INCs and DECs. It is somewhat ironic that PJM defends its incomplete and inaccurate method as being less complex, given the complex nature of the underlying problem and the corresponding complexity that necessarily pervades PJM rules. When the PJM method was proposed to stakeholders, the details of the implementation were not discussed. Even in PJM's Answer, details such as keeping only positive dfax values are not explicitly defined. Stakeholders and the Market Monitor were not provided the necessary details about PJM's proposed implementation prior to the proposed implementation date and still have not been provided such details.

⁵ October 1st Comments at 15.

The lack of transparency and the flawed logic in PJM's method presented to stakeholders is illustrated in the Financial Marketers Answer. The Financial Marketers reference (at 9–10) Figure I-5 from the Market Monitor's October 1st Comments, in which a UTC transaction crosses a constraint, increasing flows on the constraint. The Financial Marketers and the Market Monitor agree that it is clear that a UTC in the direction of a constraint increases flow on that constraint, and should therefore be eligible for forfeiture if it meets the given threshold. However, under PJM's flawed proposed implementation method, the UTC being reference would not be subject to forfeiture, because the net dfax (-.75) has a negative sign.

E. PJM's Approach Is Not Adequate to Protect the Markets, Is Inconsistent with the Longstanding Application of the FTR Forfeiture Rule to Other Virtual Transactions, and Is Not Just and Reasonable.

PJM asserts (at 4) that the IMM's proposal constitutes "confusing additional complexities" which "the IMM feels would make the FTR Forfeiture Rule more 'just and reasonable'." PJM argues that "the standard the Commission must apply here is not whether the IMM proposal is better or more rigorous...[r]ather, the Commission must evaluate whether the filing of the public utility—here PJM's proposal—is just and reasonable standing alone."⁸

PJM's proposal is not just and reasonable. PJM's proposal would not protect the market from manipulation in the way that the current FTR Forfeiture Rule does.⁶ PJM's proposal would penalize market participants that should not be penalized, and would not penalize market participants that should be penalized. PJM's proposal would not provide consistent treatment across virtual bid products. PJM's proposal would provide

⁶ It is essential that rules limit manipulation where possible in order to avoid lengthy, individual prosecutions of market participants and in order to ensure that all violations are detected and immediately addressed in a non-discriminatory manner. *See Deutsche Bank Energy Trading, LLC*, 142 FERC ¶ 61,056 (2013) as an example of what happens when a rule does not address such behavior.

unsupported preferential treatment to UTC bids relative to PJM's treatment of INC and DEC bids under the FTR Forfeiture Rule. Given that UTC transactions have displaced INCs and DECs as the predominant form of virtual transactions, it is essential that the FTR Forfeiture Rule not be applied in a discriminatory manner so as to provide an arbitrary incentive to use UTC transactions in place of INCs and DECs. Given this displacement, such a discriminatory application of the rule would mean the effective replacement of the FTR Forfeiture Rule with a much weaker rule and create a risk of market manipulation.

II. MOTION FOR LEAVE TO ANSWER

The Commission's Rule 213 does not permit answers to answers or protests unless otherwise ordered by the decisional authority.⁷ The Commission has made exceptions, however, where an answer clarifies the issues or assists in creating a complete record.⁸ 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. MOTION FOR LEAVE TO FILE COMMENTS

Pursuant to the Commission's Rule 212, the Market Monitor respectfully requests that the Commission grant this motion to file its comments submitted on October 1, 2013, four days out-of-time.⁹ The Market Monitor's October 1st Comments address important

⁷ 18 CFR § 385.213(a)(2).

⁸ See, e.g., *N.Y. Indep. Sys. 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); *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).

⁹ 18 CFR § 385.212 (2012).

issues related to the application of the FTR Forfeiture Rule to up-to-congestion transactions. Submission of the comments after the filing deadline resulted from the Market Monitor's determination that additional review was necessary to ensure that accurate information was provided. The Commission has frequently exercised its discretion to accept comments out-of-time where good cause exists.¹⁰ The Market Monitor's comments at this early state of the proceeding may be useful to the Commission as it engages in the decision-making process, and acceptance of the comments will not cause any disruption or delay to the Commission's consideration of the application. Additionally, because no other party chose to submit comments, the Commission's acceptance of the Market Monitor's comments will not adversely affect or prejudice any party. Accordingly, the Market Monitor's October 1st Comments should be accepted and considered.

IV. ANSWER TO MOTION TO STRIKE

The Financial Marketers move to strike the Market Monitor's October 1st Comments, alleging that the comments impermissibly exceed the scope of the proceeding by setting forth independent recommendations that differ from PJM's proposal.¹¹ In the Commission's order on compliance, issued August 19, 2013, the Commission stated:

It is unclear from the filing how PJM intends to apply the 'at any other bus' requirement in Section 5.2.1(c) to UTC

¹⁰ See, e.g., *PJM Interconnection, L.L.C.*, 125 FERC ¶61,231 at P 13 (2008) (accepting out-of-time comments for good cause shown); *Midwest Independent Transmission System Operator, Inc. and Ameren Transmission Company of Illinois*, 138 FERC ¶61,147 at P 8 (2012) (permitting comments out of time); *ISO New England Inc.*, 123 FERC ¶61, 266 at P 22 (2008) (granting NEPOOL's motion for leave to file comments out-of-time, given the early stage of the proceedings); *Duke Energy Ohio, Inc. and Duke Energy Kentucky, Inc.*, 133 FERC ¶61,058 at P 17 (2010) (accepting out-of-time comments given the filing parties' interest in the proceeding, the early stage of the proceeding, and the absence of undue prejudice or delay); *California Independent System Operator Corp.*, 115 FERC ¶61,329 (2006) (accepting comments filed out-of-time, given the early stage of the proceeding and the absence of any undue prejudice or delay).

¹¹ Motion to Strike, or in the Alternative, For Leave to Answer and Answer of Financial Marketers Coalition, Docket No. ER13-1654-001 (October 9, 2013) at 2.

transactions.[fn18: The Financial Marketers suggest in their comments that PJM’s application of Section 5.2.1 (c) to UTC transactions will differ from the method currently applied to INCs/DECs. Financial Marketers Comments at 3.] Therefore, our acceptance of PJM’s proposal is conditioned on PJM including in its compliance filing an explanation of how PJM intends to apply Section 5.2.1 (b) and (c) to UTC transactions, including the ‘at any other bus’ clause of Section 5.2.1(c). In addition, PJM must explain whether and how the calculations for UTC transactions would differ from the calculations for INCs and DEC’s, and, if so, explain the different approach for UTC transactions.¹²

PJM is required to support its proposal in the first instance, and the Commission found that PJM had not provided the necessary support.¹³ It was comments of the Financial Marketers that alerted the Commission to this deficiency in PJM’s explanation and support for its proposal.¹⁴ The Commission has not yet reviewed and evaluated PJM’s explanation of how PJM’s proposal would actually apply the FTR Forfeiture Rule to up to congestion transactions, and it is illogical to argue that, under these circumstances, the Commission could or would have accepted PJM’s proposal before the Commission has completed that review and evaluation. In its September 9th compliance filing, PJM explains for the first time how it intends to apply the FTR Forfeiture Rule to up to congestion transactions, revealing that its proposal would apply the rule in a different and significantly less effective manner to up to congestion transactions than this rule has applied for over ten years to INCs/DECs. Specifically, PJM does not propose to apply the FTR Forfeiture Rule based on the “any other bus” standard in the current rule, as the Commission’s question assumes (at P 27), when the

¹² See *Order Conditionally Accepting Tariff Provisions and Directing an Informational Filing*, 144 FERC ¶ 61,121 at P 27 (August 19, 2013) (“August 19th Order”).

¹³ See *Id.*; see also, e.g., *New York Independent System Operator, Inc.*, 117 FERC ¶61,266 at P 22 (2006) (“[T]he Commission rejects the claim that it shifted the burden of proof to EPIC when it found that “EPIC has not made a convincing case” that NYISO’s compliance filings were inadequate... The burden of proof in this proceeding was on NYISO.”).

¹⁴ *Id.* at P 27 n18.

rule is applied to a UTC transaction rather than an INC/DEC. In its October 1st Comments and this answer, the Market Monitor explains why PJM's proposal is inadequate and how the current FTR Forfeiture Rule can and should be applied consistent with longstanding PJM practice. Thus, the Market Monitor's comments pertain directly to PJM's September 9th compliance filing and respond directly to the Commission's inquiry, which is directed precisely at this core flaw in PJM's proposal. If PJM's proposal is accepted as filed, PJM markets will be exposed to increased and unprecedented risk of manipulation of FTR positions through virtual transactions.¹⁵ Because the Market Monitor's comments are the only comments that explain the flaws in PJM's proposal, they may assist the Commission's inquiry into this issue. The Financial Marketers motion to strike should be denied, and the Market Monitor's October 1st Comments should be accepted in the record.

V. CONCLUSION

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

Respectfully submitted,



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¹⁵ See *Deutsche Bank Energy Trading, LLC*, 142 FERC ¶ 61,056 (2013) (Civil penalty of \$1,500,000 assessed and \$172,654, plus interest, profits disgorged to settle investigation concerning manipulation of FTR-equivalent instruments using virtual trades where no equivalent to the FTR Forfeiture Rule applied.)

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Dated: October 25, 2013

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 25th day of October, 2012.



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