UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

PJM Interconnection, L.L.C.	)	Docket No. EL21-91-000

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 ("Market Monitor") for PJM Interconnection, L.L.C. ("PJM"), submits this answer to the answer submitted on December 10, 2021, by PJM and by Vistra Corp. and Dynegy Marketing and Trade, LLC (together "Vistra").[2]

On September 9, 2021, PJM filed revisions in this proceeding to Schedule 6A of the OATT to make explicit the formula for calculating the Capital Recovery Factors ("CRF") used as a component in the formula rates for black start service include in Paragraph 18 ("September 9th Filing").[3]

This case is about a mistake and how best to correct the mistake. PJM failed to update the CRF in the tariff to account for the Tax Cuts and Jobs Act of 2017 (TCJA). Black start units that were in service on January 1, 2018, faced a different tax liability going forward than the one assumed in the calculation of the CRF. The mistake was then

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1 18 CFR §§ 385.212 & 385.213 (2021).

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

3 PJM Compliance Filing, ER21-1635-002 (September 9, 2021) ("September 9th Filing").

compounded by PJM awarding new black start service terms in 2019, 2020, and 2021, using the incorrect and outdated CRF. In their August 10th order, the Commission stated that the "CRF values currently on file with the Commission appear to be unjust, unreasonable, unduly discriminatory or preferential, or otherwise unlawful."[4] The Market Monitor provided analysis that shows how the failure to update the CRF for seven black start units with completed service terms resulted in $4.3 million of payments to black start unit owners in excess of the capital investment.[5] The Market Monitor's analysis also shows that a failure to update the CRF will result in $126 million of payments to black start unit owners in excess of the capital investment for existing black start service units.[6]

The Market Monitor's proposal to fix the mistake will update the CRF for existing resources to a level that covers the tax liability associated with the capital recovery revenue payments, pays a 12 percent return on equity and the return of the equity investment and repays the debt investment at 7 percent. These financial terms are identical to the financial assumptions used to calculate the pre TCJA CRF. The Market Monitor's proposal is not retroactive. The Market Monitor's approach first establishes the remaining capital investment for a black start unit on the effective date of the updated CRF, and then calculates a new CRF using the remaining capital investment and the black start unit's remaining term of service.

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4 *PJM Interconnection, L.L.C.*, 176 FERC ¶ 61,080 at P 47 (2021) ("August 10th Order").

5 *See* Comments of the Independent Market Monitor (Corrected), Docket EL21-91-000 (November 18, 2021) at 10–13.

6 *Id*. at 13–18.

I. ANSWER

A. The Market Monitor's Proposal Is Not Retroactive.

The Commission stated in the August 10th Order (at P 50) that retroactive settlement would not be considered. The Market Monitor's proposal is consistent with the Commission's determination. At this point there is no active black start unit with a fully recovered black start capital investment, and therefore no over recovery or excess payback has occurred.[7] But over recovery will occur if the CRF values are not updated. Vistra points to the Market Monitor's statement that the updated CRF "will reflect the return of capital already received by the existing black start units and eliminate the payback in excess of the capital investment" as evidence that the Market Monitor's proposal will "claw-back alleged prior over-recoveries."[8] Vistra appears to interpret "eliminate the payback" as a disgorgement or retroactive resettlement which is a misunderstanding. The full amount of the capital investment plus return and taxes will be paid to black start unit owners. The payment will not be less than full compensatory. The payment will not be more than full compensatory. The Market Monitor's proposal does not claw back or disgorge payments. The Market Monitor's proposal simply and accurately prevents the excess payback from occurring.

The Market Monitor's proposal is similar to restructuring a loan. For example when a mortgage is refinanced, the outstanding principal is determined and a new interest rate is used to calculate a new monthly payment. The present value of the newly determined monthly mortgage payments is equal to the outstanding principal.

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[7] Capital recovery in excess of the taxes, and the return on and return of the capital investment has occurred for black start units that have completed their service terms. *See* Comments of the Independent Market Monitor for PJM, Docket No. EL21-91-000 (November 11, 2021) at 13.

[8] Vistra at 5.

The Market Monitor applies the same logic to update the CRF to account for the tax impacts of the TCJA. The outstanding capital investment is determined as of a specified date. Then an updated CRF and associated revenue requirement are calculated so that the present value of the after tax cash flow associated with the newly determined revenue payments is equal to the outstanding capital investment.

B. Criticisms of the Market Monitor's Analysis Are Misplaced.

Vistra stated that the Market Monitor's analysis and estimate of the $126 million payback in excess of the capital investment "should be viewed as an exercise in false precision and afforded no weight."[9] Vistra contends that the Market Monitor's "cash flow summaries would be instructive if - and only if - the cash flows associated with every single Black Start investment made by a variety of companies across the PJM footprint over the course of their cost-recovery periods were identical and remained static but for the" federal tax rate.[10] Vistra misunderstands the cash flow summaries. The Market Monitor's cash flow summaries that illustrate the payback in excess of the capital investment are from the perspective of the PJM customer and represent the costs that PJM customers are required to pay. The Market Monitor's analysis shows that payments by PJM customers will exceed the amount required by the tariff. It is not relevant to the PJM customer whether Vistra's effective federal tax rate for 2018, due in part to a deferred tax credit of $54 million, may have been 44.6 percent (see Table 1). The PJM tariff requires that the black start customer pay the black start owner's tax liability associated with the capital recovery revenue, and the return on and return of the capital investment. The terms of the capital investment from the PJM customer's perspective is a 1:1 debt to equity ratio, 12.0 percent return on equity and 7.0 percent debt interest rate. Knowledge of whether or not the black start owner is

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9 *Id*. at 7.

10 *Id*. at 6.

deferring taxes or knowledge of the actual financial terms for each black start owner is not necessary. The customers pay this amount regardless of the other aspects of the unit owners' financial situation.

Vistra's income tax table actually illustrates the Market Monitor's point (see Table 1). Vistra's black start service revenue for 2017 and 2018 would have been included in the first line of Table 1 (income before income taxes), and lines 2 and 3 clearly show the impact of the TCJA. Vistra's black service revenue from 2017 was taxed at 35 percent and Vistra's black start service revenue from 2018 was taxed at 21 percent.

Table 1 Income Tax Expense (Benefit) Table from Vistra Energy Corp. Form 10-K[11]

	Year Ended December 31,	
	2018	2017
Income (loss) before income taxes	$ (101)	$ 250
US federal statutory rate	21%	35%
Income taxes at the U.S. federal statutory rate	(20)	88
Nondeductible TRA accretion	8	(80)
State tax, net of federal benefit	22	13
Impacts of tax reform legislation on deferred taxes	—	451
Return to provision adjustment	(12)	19
Remeasurement of historical Vistra Energy deferred taxes for expanded state footprint	(54)	—
Effect of refundable minimum tax credits no longer subject to sequestration	(15)	—
Nondeductible compensation	8	—
Nondeductible transaction costs	3	—
Equity awards	(3)	—
Nondeductible debt restructuring costs	—	—
Nondeductible interest expense	—	—
Nontaxable gain on extinguishment of LSTC	—	—
Valuation allowance on state NOLs	20	—
Other	(2)	13
Income tax expense (benefit)	$ (45)	$ 504
Effective tax rate	44.6%	201.6%

The material below line 3 in Table 1 has absolutely no relevance to the PJM black start service customer and should be given zero consideration in any analysis of PJM black start capital cost recovery.

C. Vistra's Arguments For Not Changing the CRF Are Self Serving and Disingenuous.

Vistra (at 7) accuses the IMM of ignoring "the steep public consequences of disregarding the compensation established" for black start investments. Had the corporate

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[11] *Form 10-K for the Fiscal Year Ended December 31, 2018, Vistra Energy Corp.*, Note 9, p 119 <https://filecache.investorroom.com/mr5ir_vistracorp_ir/130/vistra-q42018-10K.pdf>.

tax rate increased most assuredly Vistra would be seeking a change to the CRF.[12] Vistra seeks to maintain the current black start revenue payments that assume a 36 percent federal tax rate. Vistra ignores the "steep public consequences" of forcing PJM customers to reimburse black start providers for taxes that are not being levied and eventually under the PJM proposal, to pay returns for investments that have already been paid back.

Vistra argues (at 8) that "Black Start service presents providers with unique risks" and that these "risks are not reflected in the IMM's calculations." PJM made a similar argument in its response to the show cause order.[13] Arguments concerning risk and return should be framed in terms of rate of return. Equity investors and lenders would require higher rates of return if the risks of providing black start service have increased. If Vistra or any other entity genuinely believes the 12 percent return on equity and 7 percent interest on debt are not adequate, then they should make an argument for these rates to be increased. PJM undercuts their contentions regarding risk and return by filing for exactly the same return on equity (12 percent) in their April 7th filing and again in their September 9th Filing.[14] The Market Monitor is not aware of any filings in the black start CRF docket (ER21-1635-000) that sought a higher return on equity than 12.0 percent. Vistra's arguments are also undercut by the fact their black start investments were made prior to the TCJA. Following Vistra's logic (at 7), Vistra (or their predecessor) undertook "complex risk assessments" prior "to committing to make the Black Start investments" and concluded that 12 percent return on equity and debt at 7 percent adequately reflected the risk of providing black start

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12 Media reports in recent months indicate that Congress was just one or two votes shy of increasing the corporate federal income tax rate.

13 PJM, Response to Commission's Show Cause Order at 3, Docket EL21-91 (October 12, 2021).

14 *Cf*. PJM Filing, ER21-1635-000 (April 7, 2021), Attachment C (Redlines); September 9th Filing, Attachment C (Redlines).

service. Now Vistra argues that it is necessary to the keep the current CRF in place in order for Vistra to capture returns in excess of the 12 percent return on equity.

D. The CRF is Not a Stated Rate.

Vistra continues to argue (at 2–5) that CRF values calculated under the formula that is now explicit in the tariff cannot be applied retroactively. Vistra apparently means to suggest that the CRF values included in the tables in Paragraph 18 of OATT Schedule 6A prior to PJM's September 9th Filing ("CRF Tables") are stated rates. Vistra never actually claims that the CRF Tables are stated rates. Vistra stops at the legally meaningless observation that the CRF Tables are "stated."

The CRF Tables standing alone are not rates at all, stated or formula. The CRF Tables are components of the formula rate set forth in Paragraph 18. Paragraph 18 explicitly describes the rates set forth in that paragraph as "formula rates." The CRF values are components of formula rates.

That Paragraph 18 included the CRF Tables in Paragraph 18 does not change their fundamental nature as components of formula rates. The September 9th Filing explicitly includes a formula, and the previous approach of including the CRF Tables did not explicitly include a formula. Vistra suggests (at 3) that that the CRF Tables have no basis because PJM failed to fully explain their basis when it filed them. Information on the basis of the calculated values represented in the CRF Tables has always been available.

Vistra concedes the critical point about formula rate components at issue here when it states: "Retroactive rate changes are only permissible in two narrow circumstances, as the D.C. Circuit recently underscored: (1) when a filed rate takes the form of a formula that varies as the incorporated factors change over time and (2) "when a court invalidates a filed rate as unlawful."[15] Vistra is wrong to characterize such circumstances as "retroactive rate

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[15] *See* Vistra at 4 & n.9, citing Okla. Gas & Elec. Co. v. FERC, 11 F.4th 821, 830–31 (D.C. Cir. 2021) (citing Old Dominion Elec. Coop. v. FERC, 892 F.3d 1223, 1227 (D.C. Cir. 2018)).

changes." The correct characterization is that use of accurate components is necessary to implement the filed formula rate.

The Market Monitor's proposal corrects the overpayment issue and does not require rebilling.

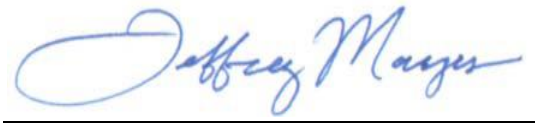
II. MOTION FOR LEAVE TO ANSWER

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.[16] 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.

Respectfully submitted,



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[16] *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).

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Dated: December 20, 2021

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 20th day of December, 2021.

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