UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

PJM Interconnection, L.L.C.	))))))	Docket No. ER09-412-006 Docket No. ER09-1673-000 (not consolidated)

COMMENTS OF THE INDEPENDENT MARKET MONITOR FOR PJM

Pursuant to Rule 211 of the Commission's Rules and Regulations, 18 CFR § 385.211 (2008), Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor for PJM ("Market Monitor"),[1] submits these comments concerning PJM's proposed revisions to the Reliability Pricing Model ("RPM"), which were filed both in compliance with the Commission's orders of March 26 and August 14, 2009,[2] and separately in conjunction with the ongoing work of the Capacity Market Evolution Committee. The Market Monitor has observations and concerns about certain provisions, and in some cases requests that the Commission provide clarification or corrections.

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1 PJM Interconnection, L.L.C. is a FERC-approved Regional Transmission Organization. Capitalized terms used herein and not otherwise defined have the meaning used in the PJM Open Access Transmission Tariff ("OATT").

2 *PJM Interconnection, L.L.C.*, 126 FERC ¶61,275 (2009), *order on reh'g*, 123 FERC ¶61,157 (2009).

I. COST OF NEW ENTRY

PJM proposes in Docket No. ER09-412 (at 6–15) a process for updating the Cost of New Entry that uses reasonably objective inputs to its analysis of whether an adjustment is needed. The Market Monitor finds this approach acceptable, as it allows for a reasonable balance between the need for objective standards and the need for flexibility to establish an accurate net CONE.

The annual automatic adjustment to net CONE would be based on the Handy-Whitman Index. A more complex process would occur every four years. In establishing net CONE initially, and in its two filings to update net CONE since then, PJM, with the support of the Market Monitor, relied upon a study conducted by a consultant to prepare an estimated CONE in each of three areas in the PJM Region.[3] The consultant's analysis went beyond general industry research to confirm with actual builders that they would move forward with a project on the basis of the estimated CONE. PJM now proposes to review CONE every fourth year on the basis of an analytical process that centers on an analysis of new entry offers, including offers that do not clear. The Market Monitor agrees that an average of recent bona fide competitive offers from developers is a reasonable basis for periodically evaluating CONE.

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[3] *See* PJM filings initiating Docket Nos. ER05-1410-000 et al., ER08-516-000 and, ER09-412, submitted respectively, on August 31, 2005, January 30, 2008 and December 12, 2008.

Nonetheless, there are problems with this approach that justify PJM's decision to refrain from exclusive reliance upon such an analysis, and to continue to provide an important role for in depth studies prepared by consultants familiar with investment in generation facilities. The pool of offers analyzed may be quite small. Use of offers from the four preceding Base Residual Auctions, although necessary to enlarge the data pool, necessarily includes cost information that could be stale. As we have seen since RPM was implemented on June 1, 2007, the costs of development can change rapidly. Had this revision been in place for the BRA this past May, it would have considered every new entry offer submitted in RPM's history.

Another problem created by the pool sample size, which particularly concerns the Market Monitor, is the potential effect of new entry offers intended to manipulate the level of net CONE. Even a single offer designed to alter net CONE, with no expectation that it would trigger an obligation to build, could influence net CONE, and by extension, RPM prices. The proposed revision provides that whether offers are competitive will be "determined in accordance with objective criteria and evidence."[4] Although this task seems to fall naturally within the scope of the Market Monitor's

[4] Proposed section OATT Attach DD § {5.14}(vii)(c)(1).

duties under Attachment M, it would be helpful for the Commission to clarify the Market Monitor's role.[5]

II. NEW ENERGY PRICING ADJUSTMENT

PJM's proposal in Docket No. ER09-1673 includes (at 3–5) welcome revisions to the New Entry Pricing Adjustment ("NEPA") that would allow NEPA to provide the assurance of three years of annual recovery on and of investment to parties willing to make significant capital investments. The current NEPA does not serve its intended purpose because it does not provide the intended three year assurance of annual investment recovery. The NEPA resource continues to receive a make-whole payment to assure recovery of its initial price for two years, but the market clears on the basis of contemporary market offers.

The Market Monitor believes that PJM's proposed tariff language should require that a cleared NEPA resource submit an offer in the two subsequent BRAs at a price no greater than its original offer, as that is the assured minimum price that the NEPA resource would receive.[6] In the new approach, where the NEPA resource is guaranteed to clear, it does not make sense to allow for a riskless opportunity for the NEPA resource to receive a higher price.

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5 Such clarification could occur in this proceeding or in the proceeding concern PJM's compliance with Order No. 719, Docket No. ER09-1063.

6 *See* OATT Attach DD § 5.14(c) para. c.

III. DEMAND RESPONSE PARTICIPATION

PJM proposes (at 5–7) in Docket No. ER09-1673 to permit offers from demand side resources to set the clearing price, to eliminate such offers from market power mitigation provisions and to exclude such offers from the supply used in applying the market structure test.

The Market Monitor agrees that, under current market conditions, it is reasonable to eliminate demand side resources from market power mitigation provisions. The supply from generation resources limits the auction clearing price, except where there is a shortage, and therefore the participation of demand side resources can only decrease the clearing prices. Given this reliance on supply from generation resources, it is logical to exclude demand side resources in applying the market power test of market structure to generation resources.

However, competition among demand side resources will result in lower prices than the absence of competition among demand side resources. The Market Monitor remains concerned about the competitiveness of demand side resources. Should the Commission adopt PJM's proposal, the Market Monitor intends to closely follow the behavior of demand side resources and their impact on auction results. The Market Monitor requests that the Commission leave room for PJM to include demand resources under the mitigation rules if subsequent review and analysis show that this is needed.

PJM's proposal includes a proviso in its proposed section 6.3(c) of Attachment DD to the OATT concerning the "Determination of Incremental Supply" as it relates to demand response. Despite the differences concerning the respective roles of the PJM staff and the Market Monitor expressed in Docket No. ER09-1063, concerning compliance with Order No. 719, it is undisputed that the Office of the Interconnection and not the Market Monitor applies the market structure test and that the Market Monitor's role is to monitor its application. Consequently, the proviso should identify the Office of the Interconnection and not the Market Monitor as the party that "shall consider only such supply available from Generation Capacity Resources".[7] PJM can confirm its intent here, if necessary, but this appears to be merely an oversight. Accordingly, the Commission should condition its approval on this correction.

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[7] Specifically, the following correction is needed to OATT Sheet No. 606:

> (c) Determination of Incremental Supply
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> In applying the market structure test, the *Office of the Interconnection* shall consider all incremental supply up to and including all such supply (provided, however, that the ~~Market Monitoring Unit~~ Office of the Interconnection shall consider only such supply available from Generation Capacity Resources) available at an effective cost less than or equal to 150% of the cost-based clearing price calculated using the incremental megawatts of supply available to solve the constraint and the need for megawatts to solve the constraint giving rise to a Locational Price Adder.

IV. DEFAULT AVOIDABLE COST RATES APPLICABLE TO INCREMENTAL AUCTIONS

PJM proposes in Docket No. ER09-1673 (at 11–13) to revise the default Avoided Cost Rates ("ACR") in section 6.7(c) of Attachment DD to the OATT substantially in the manner urged by the Market Monitor in its letter filed in Docket No. ER05-1410-000, dated April 29, 2009. PJM has requested an effective data of November 1, 2009, but it would be very helpful to the Market Monitor to have an order confirming at least this aspect of PJM's proposal no later than October 29, 2009, in order to facilitate the orderly application of these changes.[8] On November 2, 2009, the ACR system opens for data entry in advance of the Incremental Auction scheduled January 2010.

8 The Market Monitor notes that the specific language proposed by PJM does not reflect the Market Monitor's position on matters currently contested in Docket No. ER09-1063.

V. CONCLUSION

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

Respectfully submitted,

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Dated: September 22, 2009

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 22nd day of September, 2009.

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