

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

PJM Interconnection, L.L.C.)	Docket No. EL16-6-002 & ER16-121-001
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**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 for PJM² (“Market Monitor”), submits this answer to the Answer to Requests for Rehearing of J. Aron & Company submitted on November 9, 2016 (“J. Aron”), and the Answer of PJM Interconnection, L.L.C, submitted on November 23, 2016 (“PJM”), responding to the Market Monitor’s request for rehearing submitted on October 14, 2016.

I. ANSWER

A. PJM’s Discretionary Reduction in ARRs Does Not Constitute a Change in Circumstances.

The Commission’s order in this proceeding issued September 15, 2016 (“September 15th Order”), relies on an asserted “change of circumstances” between the *FirstEnergy* orders and the September 15th Order as the rationale for allocating balancing congestion to real-

¹ 18 CFR §§ 385.212 & 385.213 (2016).

² Capitalized terms used herein and not otherwise defined have the meaning used in the PJM Open Access Transmission Tariff (“OATT”) or the PJM Operating Agreement (“OA”).

time load and exports.³ J. Aron contends (at 2) that this change of circumstance was the “clear cost shift between various Load Serving Entities that were subjected to a reduction in allocation of Auction Revenue Rights as a result of persistent underfunding.”

This reduction in ARR was a result of PJM’s decision to reduce the allocation of Stage 1B ARRs by arbitrarily increasing the outages reflected in the FTR model in order to improve the payout ratio.⁴ J. Aron and PJM assert that PJM’s actions resulted in a change in circumstances. A more direct and effective way to deal with the results of PJM’s reduction in ARR allocations would be to simply reverse PJM’s reduction in ARR allocations. A change in circumstances implies that something fundamental changed in the markets. But that did not occur. A reduction in ARR allocations by PJM led to a reduction in ARR allocations. This does not qualify as a change in circumstances. To the extent that the rationale for PJM’s actions was a low payout ratio, that was explicitly reviewed in the *FirstEnergy* orders and therefore cannot be a changed circumstance since those orders.

The Commission’s decision to assign balancing congestion to ARR holders does not address or resolve the results of PJM’s changed ARR allocation. PJM’s change in allocation made load worse off. The Commission’s actions make load even worse off by assigning balancing congestion to load.

B. The Impact of PJM’s Reduction of ARR Allocations to Load Are Not Addressed by Assigning Balancing Congestion to ARR Holders.

PJM states (at 4) that in response to FTR target allocations exceeding total congestion revenue, PJM began reducing the allocation of Stage 1B ARRs to load and this “more conservative ARR allocation resulted in inappropriate costs shifts between ARR holders and FTR holders.” PJM notes (at 6) “that reducing the number of ARRs allocated to

³ *PJM Interconnection, L.L.C.*, 156 FERC ¶61,180(2016); *FirstEnergy Solutions Corp. v. PJM*, 143 FERC ¶ 61,209 (2013) (*FirstEnergy*), *reh’g denied*, 151 FERC ¶ 61,205 (*FirstEnergy II*).

⁴ *Id.*

transmission service customers was an imperfect solution to the FTR underfunding problem.”

As PJM apparently agrees, PJM did not need to, but rather chose to, reduce ARR allocations to improve FTR funding. PJM’s efforts to guarantee FTR funding at the expense of ARR holders through reduced ARR allocations was deemed to be unjust and unreasonable by the Commission.⁵

The Commission previously decided that FTR target allocations are not a guarantee of payment and there is no obligation by PJM or the ARR holders to guarantee payment of the target allocations.⁶ Therefore, PJM should not have applied its FTR market model discretion to guarantee revenue adequacy within the FTR market by reducing the allocation of ARRs at the expense of load. This effectively did require load to guarantee payment of the target allocations.

PJM failed to take a series of identified steps to improve FTR funding and instead directly reduced the allocation of ARRs to load. That allocation resulted in cost shifting to ARRs. That cost shifting led the Commission to conclude that balancing congestion should be assigned directly to load in order to prevent the cost shifting to load. Assigning balancing congestion to load has been PJM’s objective for many years. The solution to cost shifting to load was cost shifting to load. PJM should be directed instead to take the necessary steps to address FTR funding directly to the extent that PJM believes that funding levels are an issue.

C. Balancing Congestion Is a Component of Total Congestion and Is Not The Cause of FTR Target Allocations Exceeding FTR Funding.

PJM argues (at 6) that “balancing congestion does not represent congestion.” Balancing congestion is, by definition, a component of total congestion, which is the

⁵ September 15th Order at P 96.

⁶ *FirstEnergy II* at PP 40–41.

revenue available to fund FTRs. PJM's newly provided figure (at 5) demonstrates only that the removal of a large negative number from total congestion makes total congestion higher. There is no analytical or factual support for the assertion that balancing congestion is not congestion. The history and logic of the PJM markets make it clear that balancing congestion is part of total congestion.

The Market Monitor agrees with PJM that balancing congestion is not the same as real-time congestion. The fact that balancing congestion can be defined as "...a monetization of nodal energy injections and extractions between day-ahead and real-time weighted by the real-time LMPs" does not mean that balancing congestion is not part of total congestion.⁷ It could also be stated that day-ahead congestion is the monetization of nodal energy injections and extractions weighted by day-ahead LMPs. This does not mean that day-ahead congestion is not part of total congestion.

Balancing congestion is calculated as difference between the real-time and day-ahead MWh multiplied by the real-time congestion LMP, not the total LMP. Balancing congestion is calculated to settle differences in congestion paid by participants between the real-time and day-ahead markets. Balancing congestion reconciles the amount of congestion paid by participants between the two markets. The balancing congestion reconciliation ensures that participants are paying the right level of total congestion based on actual energy usage.

D. Fully Funding FTRs by Assigning Balancing Congestion to ARR Holders Will Not Provide a Net Benefit to Load.

PJM argues (at 8) that "But, in removing a major source for the underfunding, market participants will have more confidence in FTRs." PJM concludes that the result ultimately benefits load. PJM's argument is demonstrably false. PJM's argument is that if load pays more, it may cause FTR holders to pay more for FTRs, which will increase ARR

⁷ See PJM at 7.

funding. If PJM wants to increase FTR funding, there is a series of identified steps to improve FTR funding that PJM could take. There is also a much simpler way to address these issues and that is to assign the rights to all congestion revenues to load.

There is no market evidence that there is a lack of confidence in FTRs. When payout ratios declined, market participants purchased more FTRs at lower prices. The market adapted. There was no problem that required resolution.

PJM argues that fully funded FTRs, generated by shifting costs to ARR holders, will provide a net benefit to ARR holders through increased ARR rents. No evidence is provided to support this argument. Instead, the evidence that is available runs counter to this assertion. The objective and result of reducing Stage 1B and Stage 2 ARR allocation, for example, was the full funding of FTRs. By PJM's own admission, fully funded FTRs achieved through reduced Stage 1B and Stage 2 ARR allocation came at the expense of ARR holders.

There is no basis for the assertion that the full funding of FTRs supported by the shifting of balancing congestion to ARR holders will provide a net benefit to ARR holders.

E. Assigning Balancing Congestion Creates Undue Discrimination Between Financial Participant FTR Holders and Load FTR Holders

PJM argues (at 7) that "there is no need to include balancing congestion in the funding definition of FTRs to maintain the financial hedge." PJM states (*id.*) that, in fact, "doing so unjustly and unreasonably undermines the effectiveness of that hedge." PJM's assertions are incorrect.

Allocating balancing congestion to load significantly undermines the effectiveness of ARRs as an offset to congestion. Under the current rules load exchanges its rights to variable congestion rents for fixed ARR payments.

The Commission states "...FTR holders do not cause and cannot predict the level of balancing congestion."⁸ The same is true for ARR holders.

But financial participant FTR holders voluntarily take on FTR risk in hope of a profit based on their analysis of expected congestion. FTR holders can change their bid prices to reflect their expectations.

ARR holders and load are not voluntary participants. If load wishes to receive at least part of the congestion revenue they pay, they must accept some or all of the ARRs allocated to them by PJM. Under the existing FTR rules, load receives a fixed ARR payment based on FTR clearing prices. Or, under the existing rules, if load chooses to self schedule the ARRs as FTRs, load may receive actual congestion revenues like financial FTR holders.

Allocating balancing congestion to load undermines the value of ARRs as a means for load to offset their exposure to congestion risk. It shifts risk from the voluntary FTR holder to the ARR holder, with no offsetting benefit. Under the September 15th Order, if load chooses ARRs, the value is no longer fixed because load must also pay balancing congestion. Even if load self schedules the ARRs as FTRs, load must still pay balancing congestion. Under the September 15th Order, there is no way for load to offset its exposure to balancing congestion.

The September 15th Order would, if implemented, create two classes of FTR holders. Financial participants holding FTRs would be paid day-ahead only congestion. Load holding FTRs would be paid day-ahead only congestion minus total balancing congestion (when negative). The payments to load are comparable to the prior definition of total congestion, day-ahead congestion minus balancing congestion, except that it is worse because load now must pay all of the balancing congestion rather than just the balancing congestion associated with its positions. This result is unduly discriminatory because load holding FTRs are substantially worse off than financial participants holding the same FTRs.

⁸ September 15th Order at P 95.

Allocating balancing congestion to load completely eliminates any mechanism load had to create a predictable congestion offset. Balancing congestion can vary significantly from month to month. For example, in the 2015 calendar year, monthly balancing congestion charges varied from 7.9 percent to 79.2 percent of all participants' ARR target allocations. The discriminatory treatment of load holding FTRs combined with the uncertainty associated with monthly balancing congestion makes the Commission's FTR/ARR design a very significant negative for load.

The assertion that load will be better off because load is required to subsidize financial participants holding FTRs is unsupported by any analysis and is unsupportable. Such speculative benefits should not be the basis for such a dramatic change in the definition of FTRs and the creation of discriminatory treatment of FTR holders.

F. FTRs Are Not A Day-Ahead Only Product.

PJM argues (at 3) that "it is well accepted that by design, FTR is a day-ahead product." There is no basis for this statement. The PJM FTR product predates the PJM day-ahead market and therefore could not have been conceived of as a day ahead product. FTRs were introduced on April 1, 1999, along with the PJM real-time market. At that time, PJM did not have a day-ahead market and FTRs returned total congestion to load. At that time, total congestion equaled real-time congestion and all positions were settled at real-time market prices. FTR target allocations (based on real-time CLMP and FTR MW) could still vary from total congestion collected, but FTRs were only due the total congestion collected. FTRs are not now and never have been a product based solely on the day-ahead market.

The PJM day-ahead market was not introduced until June 1, 2000. The introduction of the day-ahead market transformed PJM's energy market into a two settlement system, with day-ahead and balancing settlement. In a two settlement system, balancing settlement is based on differences between a participant's day-ahead and real-time positions. Under a two settlement system congestion equals the sum of day-ahead and balancing congestion. When the day-ahead market was introduced, FTRs were directly allocated to load and paid

total congestion, now including day-ahead and balancing congestion, to load. FTR target allocations (based on day-ahead CLMPs and FTR MW) still varied from total congestion collected, but FTRs were paid total congestion.

Effective June 1, 2003, PJM replaced the direct allocation of FTRs to load with an allocation of Auction Revenue Rights (ARRs). The load still owns the rights to congestion collected under this system, but with ARRs load can either claim the associated FTRs directly (through a process called self scheduling), or can keep the ARRs which entitle the holder to a fixed amount of revenue based on the auction prices of FTRs. With ARRs, total FTR auction revenues for associated FTRs belong to load and total congestion revenues belong to those that purchase or self schedule the FTRs.

The introduction of ARRs did not change the definition of FTRs and did not change the FTR product into a day-ahead only product.

In a two settlement market there is no such thing as a day-ahead only position or a day-ahead only product. All cleared positions are evaluated on the basis of the day-ahead market results and any associated balancing settlements. Total congestion under a two settlement system is the result of all cleared day-ahead positions and any associated balancing settlements.

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.⁹ In this answer, the Market Monitor provides the

⁹ 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 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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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).

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 2nd day of December, 2016.



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