UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Panda Hummel Station LLC	)	Docket Nos. ER19-391-003
Hummel Station, LLC	)	ER19-391-005

To: The Honorable Patricia M. French
Presiding Administrative Law
Judge

BRIEF OF THE
INDEPENDENT MARKET MONITOR FOR PJM

Pursuant to Order No. 1, issued in this proceeding August 25, 2022, Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor ("Market Monitor") for PJM Interconnection, L.L.C. ("PJM"),[1] submits this brief. The Market Monitor believes that issues of fact exist in this case only to the extent that the company asserts the existence of specific costs that are not recovered or recoverable in PJM markets. The Market Monitor's position is that no such specific costs exist. The Market Monitor's position is that a purely legal basis for a revenue requirement of $2,199 per MW-Year under Schedule 2 does exist. The Market Monitor does not advocate any further action by the Presiding Judge while this matter is pending before the Commission.

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[1] 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").

I. ARGUMENT

A. Whether the determination and establishment of a cost of service for a particularized generating unit's reactive power is a question of fact that is determined on a case-by-case basis.

Schedule 2 allows individual resources to file revenue requirements. Preliminary to any consideration of a proposed revenue requirement, resources must meet the eligibility requirements in Schedule 2.[2] The Commission makes determinations on eligibility directly.[3] Resources must also identify costs appropriately included in a proposed revenue requirement, including costs not already recovered or recoverable in PJM markets. The Commission must directly determine whether costs appropriate for inclusion in a revenue requirement under Schedule 2 have been identified.

The Market Monitor disputes whether it is just and reasonable to develop and file a cost of service rate under Schedule 2 to the OATT ("Schedule 2") as a matter of law and fact. The Market Monitor disputes whether the *AEP* Method is a cost of service method, and, whatever it is, disputes whether the *AEP* Method is appropriate for calculating a revenue requirement under Schedule 2.[4] In a separate

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[2] *See* OATT Schedule 2; *see also Whitetail Solar 3, LLC, et al.*, Initial Decision, 180 FERC ¶ 63,009 (2022).

[3] *Id*.

[4] *See American Electric Power Service Corporation*, Opinion No. 440, 88 FERC ¶ 61,141 (1999), *withdrawal of reh'g granted*, 92 FERC ¶ 61,001 (2000) ("*AEP*"). In *AEP*, the company proposed a method to allocate the costs of its generation fleet between a cost of service generation account and a cost of service transmission account such that duplicative recovery of the same costs was avoided. *See AEP* at 61,456 ("AEP explained that since generator/exciters and an allocated portion of accessory electric equipment produce active and reactive power, "it was necessary to arrive at an allocation factor to segregate the reactive (VAr) production function from the active power (Watt) production function."); *see also Fern Solar LLC*, Order Denying

pending rulemaking proceeding, the Commission is evaluating whether the use of the *AEP* Method is appropriate.[5] Because the issue concerns the appropriate implementation of Schedule 2, there is no reason why the issue should not be addressed in a proceeding that is about implementing Schedule 2.

No prior case explains how the *AEP* Method properly applies to rates for reactive supply capability to be used within the framework of the PJM market rules, including a capacity market, or the rules applicable to any organized

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Motion for Partial Summary Disposition and Motion to Strike, 180 FERC ¶ 63,024 at P 15 (2022) ("The AEP method came into being because one of its creators, AEP's Bernard Pasternack, needed to allocate costs between two cost-based services, generation and transmission. AEP's utility subsidiaries were unbundling regulated transmission service from regulated generation service, making each service available for sale separately. Since each of these regulated services would need its own cost-of-service rate, Mr. Pasternack faced a classic cost allocation problem—how to determine which pieces of equipment serve a transmission function and which serve a generation function; and where some pieces of equipment served both functions, how to allocate their costs between the two functions. But because the price-basis for both services was traditional cost of service set by the same regulatory jurisdiction, there was no possibility of duplicative recovery."); *see also* NOI at P 9 ("In Opinion No. 440,[footnote omitted] the Commission approved a method presented by [AEP], a vertically integrated utility, for allocating the costs of generator equipment between real power capability and reactive power capability, as well as the related operations and maintenance costs.").

5 *See Reactive Power Capability Compensation*, Notice of Inquiry, 177 FERC ¶ 61,118 at PP 18, 26, 27, 28(j) and 28(s) (2021) ("NOI") (summarizing the IMM's arguments and asking "Is the existing AEP Methodology appropriate to allocate the costs associated with reactive power revenue requirements of non-synchronous resources? If not, why and can changes be made to the existing AEP Methodology to establish just and reasonable reactive power revenue requirements for non-synchronous resources?" and "Do resources in PJM that receive reactive power capability compensation above $2,199/MW-year effectively receive double-recovery as alleged by the PJM Market Monitor?").

wholesale electric market. Unexplained, rote application of the *AEP* Method does not create issue preclusion.[6] Arguments against the use of the *AEP* Method in Schedule 2 proceedings are valid unless and until the issue is both actually litigated and actually decided.[7]

Because the *AEP* Method was developed and filed years before Order No. 888 was issued and the implementation of competitive markets in PJM, there is no rational presumption for using the *AEP* Method in the context of PJM competitive markets.[8] The *AEP* Method does not define the specific costs actually associated with producing reactive power, if there are any, or whether those same costs are recoverable in PJM markets.

Market participants invest in resources in PJM in order to compete in PJM's markets. Whether costs recoverable in PJM markets are eligible for inclusion in a revenue requirement in Schedule 2 is a question of law. Over recovery of costs is

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6 *See, e.g.*, Texas Employers' Ins. Asso. v. Jackson, 862 F.2d 491, 500 (5th Cir. 1988) ("Collateral estoppel, or "issue preclusion," requires, among other things, that the allegedly precluded issue have been "actually litigated and determined" in the prior action."); citing, *e.g.*, Lawlor v. National Screen Service Corp., 349 U.S. 322 (1955) ("collateral estoppel . . . precludes relitigation of issues actually litigated and determined in the prior suit"); Montana v. United States, 440 U.S. 147 (1979); Liona Corp. v. PCH Assocs. (In re PCH Assocs.), 949 F.2d 585, 593 (2nd Cir. 1991) ("With respect to issue preclusion, it must be remembered that for the doctrine to be properly invoked the particular issue currently in dispute must have been "both actually litigated and actually decided.").

7 *Id*.

8 AEP proposed the *AEP* Method in its filing dated April 2, 1993, in Docket No. ER93-540; *see also* NOI at P 2 ("Since the issuance of AEP, the electric markets and the generation resource mix have undergone significant change.").

not permitted as matter of law.[9] In a separate pending rulemaking proceeding, the Commission is evaluating whether the use of cost of service rates in Schedule 2 may result in over recovery.[10] The maximum level of revenue requirement permitted under Schedule 2 is not a settled issue. Because the issue concerns the appropriate implementation of Schedule 2, there is no reason why the issue should not be addressed in a proceeding that is about implementing Schedule 2.

Whether a resource can identify specific costs that are not recoverable in PJM markets in order to include them in a revenue requirement is a question of fact. No specific costs that are not recoverable in PJM markets have been identified in this proceeding. Whether any such costs exist is a question of fact. The Market Monitor takes the position that no such costs exist.

The Market Monitor takes the position that the only valid case for a revenue requirement concerns a legal argument. The PJM market design excludes from the capacity market design parameters costs anticipated for recovery under Schedule 2.[11] The costs removed from the PJM market design have a specific value in the current rules: $2,199 per MW-Year (the "Offset"). A resource could argue that, as

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9 *See, e.g.*, United Airlines, Inc. v. FERC, 827 F.3d 122, 134 (D.C. Cir. 2016) ("[B]ecause FERC failed to demonstrate that there is no double-recovery . . . we hold that FERC acted arbitrarily or capriciously.").

10 *See* NOI at PP 27, 28 (section d., question r & s).

11 *See* OATT Attachment DD § 5.10(a)(v)(A). The rules that account for recovery of reactive revenues are built into the auction parameters, specifically, the VRR Curve. The PJM market rules explicitly account for recovery of reactive revenues of $2,199 per MW-year through inclusion in the Net CONE parameter of the capacity market demand (VRR) curve. The Net CONE parameter directly affects clearing prices by affecting both the maximum capacity price and the location of the downward sloping part of the VRR curve. In addition, market sellers, when submitting offers based on net avoidable costs must account for revenues received through cost of service reactive capability rates in the calculation.

a matter of law, the Offset is not recoverable in PJM markets and is therefore recoverable in a revenue requirement under Schedule 2. The argument for a recovery of the Offset is based solely on the existence of the Offset. The issue does not depend on an individual unit's identification of any particular cost.

B. Whether the determination of the existence of or likelihood of a double collection in rates is a question of fact, in this instance as between recoveries in the market versus recoveries under a cost-based rate.

This issue of over recovery is a question of fact only to the extent that specific incremental costs are identified and asserted as necessary for reactive supply and are not required as a condition to receive interconnection service and are not required to generate real power. The Offset provides a legal basis for arguing that there is no over recovery for a revenue requirement under Schedule 2 at or below the value of the Offset: $2,199 per MW-Year.

C. Whether the agreed-upon resolution of any matter under a "black box" removes the question of whether it is a factual issue, and whether the fact that the resolution agreed-upon is not unanimous among all participants is of consequence.

Resolution of a matter on a black box basis indicates only an agreement of the parties or participants who accept the black box result. The only fact established by a black box agreement is the existence of an agreement. If material issues raised by a non settling party can be severed and litigated, then the remaining black box portion of resolution of the matter remains viable.[12]

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[12] The four approaches for approving a settlement under *Trailblazer Pipeline Company* include: (i) addressing the contentions of the contesting party on the merits when there is any adequate record; (ii) approving a contested settlement as a package on the ground that the overall result of the settlement is just and reasonable; (iii) determining that the contesting party's interest is sufficiently attenuated such that the settlement can be analyzed under the fair

Otherwise, one way or another, the resolution of the matter would need to be defended on the merits and would no longer be black box.[13] Thus, the significance of a contested black box settlement is that (i) the contested material issue must be defended on its merits, or (ii) the overall settlement must be defended on the merits.

In this case, the Market Monitor raises core issues on how Schedule 2 is properly interpreted and applied. Severance of the issues raised by the Market Monitor is not possible. Defense of the offer of settlement against the Market Monitor's position requires either a showing of costs that are not recovered or recoverable in PJM markets (fact based), or a reasoned explanation for why this showing is not required as matter of law (law based).

D. What happens procedurally if there remains a genuine issue of material fact AND a settlement that is not unanimous? Does the presiding judge report the matter to the Commission recommending rejection before the presiding judge recommences hearings? Or does the presiding judge suspend the settlement in order to gather sufficient evidence to build a record that might elucidate the reasonableness of the settlement? Or some other process?

In this proceeding, a contested offer of settlement is pending before the Commission.[14] The Market Monitor does not advocate any further action by the Presiding Judge until the Commission acts on the contested offer of settlement.

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and reasonable standard applicable to uncontested settlements when the settlement benefits the directly affected settling parties; or (iv) preserving the settlement for the consenting parties while allowing contesting parties to obtain a litigated result on the merits. *See Trailblazer Pipeline Company*, 85 FERC ¶ 61,345 (1998).

13 *Id.*

14 18 CFR § 385.602(h).

II. CONCLUSION

The Market Monitor respectfully requests that the Presiding afford due consideration to the arguments on brief as it resolves the issues raised in this proceeding.

Respectfully submitted,

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Dated: September 9, 2022

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 9th day of September, 2022.

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