UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Price Formation in Energy and Ancillary Services	)	
Markets Operated by Regional Transmission	)	**Docket No. AD14-14-000**
Organizations and Independent System Operators	)	

COMMENTS
OF THE PJM POWER PROVIDERS GROUP

Pursuant to the Notice dated January 16, 2015, issued in the above-captioned proceedings by the Federal Energy Regulatory Commission (the “Commission” or “FERC”), the PJM Power Providers Group ("P3")[1] submits these comments on issues raised during the technical workshops on September 8, 2014, October 28, 2014, and December 9, 2014, regarding price formation in the energy and ancillary services markets operated by Regional Transmission Organizations (“RTOs”) and Independent System Operators ("ISOs").

I. COMMENTS

While P3 has not been an active participant in this docket to date, the organization applauds the Commission’s leadership in tackling the tough issues associated with energy price formation. P3 is pleased with the discussions to date and hopes that they lead to appropriate tariff revisions.

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[1] P3 is a nonprofit corporation dedicated to promoting policies that will allow the PJM region to fulfill the promise of its competitive wholesale electricity markets. The comments contained in this filing represent the position of P3 as an organization, but not necessarily the views of any particular member with respect to any issue. For more information on P3, visit www.p3powergroup.com

As the Commission knows and has articulated, appropriate energy market price formation is essential to maximizing the value of organized markets. Without the market price of electricity accurately reflecting actual market conditions, the market will incent the wrong behaviors from both buyers and sellers and ultimately lead to irrational results. Fortunately, the Commission has identified several areas that are appropriate for examination and reform.

For purposes of these comments, P3 will focus on the energy market offer cap and uplift challenge as the two most important issues facing PJM's energy markets. While other areas identified by the Commission are important and merit Commission attention in PJM and other markets, these comments will focus only on the two issues and as they relate to PJM. P3 reserves the right to address at a later date the other issues raised by the Commission in the notice.

A. PJM's Energy Market Offer Cap

Reforming the outdated energy market cap has been a peculiarly circuitous journey in PJM. Despite broad agreement on the current market cap's inadequacies,[2] a permanent solution in PJM has been elusive. In fact, the Commission has approved three separate "temporary" solutions to the unjust and unreasonable $1,000/MWh offer cap in PJM. The most recent "temporary" solution will expire on March 31, 2015, and PJM's tariff will revert to provisions that proved unworkable in the winters of 2014 and 2015.

PJM first realized the numerous problems associated with the $1,000/MWh offer cap in the winter of 2014. Faced with extreme cold weather and gas prices that were at levels that did not allow generators to reflect their fuel costs in bids below the offer cap, the Commission approved two waivers. The first waiver allowed generators to submit cost-based offers over $1,000/MWh (ER14-44) and the second allowed cost based offers over $1,000/MWh to set the

[2] See generally, EL15-31.

energy price (ER14-45). However, both of these waivers expired on March 31, 2014, leaving the $1,000/MWh cap in place going into the winter of 2015.

Citing of lack of stakeholder consensus, PJM filed on December 15, 2014, for Commission approval of a proposed "temporary" tariff change that would allow cost-based offers up to $1,800/MWh to set the energy market clearing price. The Commission approved this temporary change on January 16, 2015. At the time, the Commission recognized that the revised cap would be in effective only until April 1, 2015, and that consideration of an offer cap beyond this winter would be more "'appropriately addressed" in this docket.

At the technical workshop on October 28, 2014, the Commission heard that the offer cap was never intended to artificially suppress prices, as it did in the winter of 2014. Adam Keech, Director of Market Operations at PJM, stated, "[w]e had resources that were limited by the $1,000 offer cap. And as a result, couldn't offer in their true cost into the market. And as a result of those market rules, we couldn't set prices—had we dispatched those resources, we couldn't set prices that were commensurate with the controlling actions we were taking."[3] Dr. Joseph Bowring, the Independent Market Monitor ("IMM") for PJM similarly acknowledged that, at the inception of the offer cap, "it was a number that people thought could never be reached."[4]

Given the realty of two straight winters in which cost-based offers over $1,000/MWh were submitted to PJM, it is incredible that the $1,000/MWh energy offer cap will be in place on April 1, 2015. A permanent solution is needed and Commission leadership appears to be required in order for a durable solution to be enacted.

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[3] FERC October 28, 2014 Price Formation Technical Conference Transcript, AD14-14-000 ("FERC Price Formation Transcript"), citing Adam Keech from PJM at p. 208.

[4] FERC Price Formation Transcript citing Dr. Joseph Bowring, the Independent Market Monitor for PJM at p. 209.

Fortunately, the correct solution for the market is grounded on two simple propositions: generators should be able to submit their cost-based energy offers and those offers should be able to set the Locational Marginal Price ("LMP"). The PJM IMM actively endorsed this solution at the October 28 technical workshop. As the IMM told the Commission, "[S]o if costs imply energy offers greater than $1,000, you have to allow them. That's the point. I mean, I talk about short-run marginal costs before and what doesn't belong, but one thing that very much does belong is the cost of gas. That's part of the short-run marginal costs. And if the cost of gas implies your offer is $1,500, that's what it should be. It should set LMP. It should not be an uplift; it should set LMP."[5]

This approach is also entirely consistent with Commission precedent on the matter. In fact, any departure from this standard will be a departure from "longstanding Commission precedent." As the Commission stated:

> "*By limiting legitimate, cost-based bids to no more than $1,000/MWh, the market produces artificially suppressed market prices and inefficient resource selection. By paying an uplift, PJM is in effect paying one price for energy dispatched through the market (e.g. $1,000), and a second higher price (e.g. $1,200) for the resource dispatched out-of-merit (while treating the latter in the dispatch stack as if it had a bid of $1,000). This would not be consistent with longstanding Commission precedent on the issue.*"[6]

PJM and the Commission need to end the search for a compromise that is based on finding "the right number." As the IMM stated on October 28, "the cost-based offer cap has to be as high as necessary to allow the recovery of actual costs."[7] That should be standard and not some artificial number that will have to be revisited in 5, 10 or 20 years at a time when the grid is likely to be stressed and producers are wondering whether they can produce power without

[5] FERC Price Formation Transcript at p. 214.

[6] 146 FERC ¶ 61,078 (2014) at p. 14, P40.

[7] FERC Price Formation Transcript at p. 215.

losing money on account of an artificial price cap. While the temporary tariff change approved for the winter of 2015 includes an effective $1,800/MWh cap based on last year's experience, there will no doubt come a time when that number is obsolete. At one point, the $1,000/MWh was considered "…the highest number anybody could think of at the time and then multiplied by five…" It is only a matter of time before $1,800/MWh is considered in the same light.

Implementing an offer cap along the lines suggested by the PJM IMM would be a relatively straight forward proposition. As the entity that oversees all energy market bids, the IMM has the ability to review and approve costs based offers over a certain level to insure that those energy market bids are reflective of actual costs and an appropriate benchmark for the setting of LMP. As in the current market construct, the IMM has the authority to take action against bids that are not consistent with PJM's market monitoring protocols and to refer any matters to FERC if appropriate.

P3 respectfully suggests that the current "band aid policy" approach to the energy market offer cap in PJM needs to come to an end and an enduring solution be put in place no later than December 1, 2015. Given the inability of PJM and PJM stakeholders to develop a permanent tariff change, the Commission should provide clear direction to PJM that energy market bids should be able to reflect actual costs and those bids, if cleared, should set the market price. P3 would urge the Commission to provide that direction consistent with its own precedent and the comments above.

P3 would also respectfully submit that this offer cap standard would be appropriate in all markets - not just PJM's. P3 shares the Commission's concern about different energy market offer caps in neighboring regions, creating potential inefficient market outcomes and more troubling reliability issues. If electricity prices driven by higher fuel prices allow a generator to recover its costs in a neighboring market and not in a generator's "home" market, it is only natural that the generator will want to export that energy so it can be appropriately compensated for serving the load. If that energy is needed for reliability in its home market, this outcome is far from desirable. By adopting the IMM's offer cap standard in all organized markets, this problem can be eliminated.

B. Uplift

Related, but distinct, from the offer cap issue is uplift and the issues associated with it. As the Commission Staff appropriately observed,

> "[R]egardless of the underlying causes of uplift, a failure to make the causes transparent and to price them into the energy and ancillary services markets can undermine the effectiveness of price signals and efficient system utilization, and mute investment signals. Volatile uplift charges may also create financial uncertainty for customers, depress liquidity and reduce market efficiency."[8]

The Commission has properly identified the drivers are uplift and, in doing so, astutely realized that uplift is better thought of as a symptom rather than a problem. Indeed, in PJM in January of 2014, as the result of extreme weather conditions, uplift charges spiked to over $500 million. The impact on market caused by such a spike was significant and lead to several parties filing for requests for tariff waivers.

P3 urges to the Commission to remain focused on the uplift challenge. It is important to note that PJM's currently pending capacity performance filing[9] could materially impact uplift dynamics in PJM as generators will be required to operate differently in order to avoid penalties. As part of this investigation, the Commission should certainly consider whether any approved tariff revisions in the capacity performance filing will help to reduce uplift in PJM.

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8 *Federal Energy Commission Staff Analysis of Uplift in RTO and ISO Markets*, August 2014, p. 2. http://www.ferc.gov/legal/staff-reports/2014/08-13-14-uplift.pdf

9 *PJM Interconnection, L.L.C.,* Docket No. ER15-623-000, December 12, 2014.

II. CONCLUSION

For the foregoing reasons, P3 respectfully requests that the Commission consider these comments in deciding issues regarding price formation in PJM's energy and ancillary services markets.

Respectfully submitted,

On behalf of the PJM Power Providers Group

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Dated: March 6, 2015

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 Washington, D.C., this 6th day of March, 2015.

On behalf of the PJM Power Providers Group

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