UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Independent Market Monitor for PJM **v.** **PJM Interconnection, L.L.C.**	)))))	**Docket No. EL19-47-000**
Office of the People's Counsel for District of Columbia **Delaware Division of the Public Advocate** **Citizens Utility Board** **Indiana Office of Utility Consumer Counselor** **Maryland Office of People's Counsel** **Pennsylvania Office of Consumer Advocate** **West Virginia Consumer Advocate Division** **PJM Industrial Customer Coalition** **v.** **PJM Interconnection, LLC**	))))))))))))))	**Docket No. EL19-63-000** **(Not Consolidated)**

REQUEST FOR REHEARING

Pursuant to Section 313(a) of the Federal Power Act (the "FPA")[1] and Rule 713 of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission (the "Commission" or "FERC"),[2] Calpine Corporation ("Calpine"), LS Power Associates, L.P. ("LS Power"), and Talen Energy Marketing, LLC ("Talen," and together with Calpine and LS Power, the "Indicated Suppliers"), the Electric Power Supply Association ("EPSA"),[3] and the PJM Power

1 16 U.S.C. § 825*l*(a) (2018).

2 18 C.F.R. § 385.713 (2021).

3 EPSA is the national trade association representing competitive power suppliers in the U.S. EPSA members provide reliable and competitively priced electricity from environmentally responsible facilities using a diverse mix of fuels and technologies. EPSA seeks to bring the benefits of competition to all power

Providers Group ("P3,"[4] and together with the Indicated Suppliers and EPSA, the "Indicated Parties") respectfully request rehearing of the Commission's September 2, 2021 order[5] regarding the default Market Seller Offer Cap ("MSOC") under PJM's Open Access Transmission Tariff (the "Tariff"). As discussed in detail below, rehearing of the September 2 Order is required because the Commission failed to properly consider the alternatives set forth by the Indicated Suppliers and others, and instead adopted an MSOC that fails to properly reflect the risks and costs imposed on suppliers and is at odds with PJM's Capacity Performance structure.

I.

BACKGROUND

A. PJM's Capacity Performance Structure and the Default MSOC

In 2015, the Commission approved PJM's proposal to establish a new Capacity Performance construct "to ensure that PJM's capacity market provides adequate incentives for resource performance . . . ."[6] In support of its proposal, PJM explained that its then-existing "penalty structure is inadequate, given that it places most of the risk of resource under-performance on loads, not on resource owners or operators," and that "a seller can earn substantial revenues

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customers. This pleading represents the position of EPSA as an organization, but not necessarily the views of any particular member with respect to any issue.

4 P3 is a non-profit organization dedicated to advancing federal, state and regional policies that promote properly designed and well-functioning electricity markets in the PJM Interconnection, L.L.C. ("PJM") region. Combined, P3 members own over 67,000 MWs of generation assets and produce enough power to supply over 50 million homes in the PJM region covering 13 states and the District of Columbia. For more information on P3, visit www.p3powergroup.com. This pleading represents the position of P3 as an organization, but not necessarily the views of any particular member with respect to any issue.

5 *Independent Market Monitor for PJM v. PJM Interconnection, LLC*, 176 FERC ¶ 61,137 (2021) (the "September 2 Order").

6 *PJM Interconnection, L.L.C.*, 151 FERC ¶ 61,208 at P 1 (2015) (the "CP Initial Order"), *on reh'g*, 155 FERC ¶ 61,157 (2016) (the "CP Rehearing Order") (together, the "CP Orders"), *aff'd sub nom. Advance Energy Mgmt. Alliance v. FERC*, 860 F.3d 656 (D.C. Cir. 2017).

through PJM's capacity auctions by committing its resource as capacity, with little concern that it will lose much of that revenue even if it performs poorly."[7] Accordingly, a central tenet of the Capacity Performance proposal was the imposition of higher penalties, which the Commission recognized would "provide incentive to capacity sellers to invest in and maintain their resources by tying capacity revenues more closely with real-time delivery of energy and reserves during emergency system conditions."[8]

The formula for calculating penalties is set forth in Section 10A of Attachment DD to the Tariff, which states that, "[f]or each Performance Assessment Interval [("PAI")], the Office of the Interconnection shall determine whether, and the extent to which, the actual performance of each Capacity Resource and Locational UCAP has fallen short of the performance expected of such committed Capacity Resource, and the magnitude of any such shortfall . . . ."[9] A resource is assessed a Non-Performance Charge that is based on its Performance Shortfall and the Non-Performance Charge Rate (also referred to as the "Penalty Rate"). The Penalty Rate, in turn, is calculated based on "an estimate of 30 hours of Emergency Actions," which reflects "the historical Emergency Action hours experienced during the 2013-14 commitment period . . . ."[10] Accordingly, the Tariff currently provides that –

> For Capacity Performance Resources and Seasonal Capacity Performance Resources, the Non-Performance Charge Rate = (Net Cost of New Entry (stated in terms of installed capacity) for the LDA and Delivery Year for which such calculation is performed *

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[7] *Id.* at P 25 (citation omitted).

[8] *Id.* at P 158.

[9] Tariff, Attachment DD, § 10A(c). There are twelve PAIs in one Performance Assessment Hour ("PAH").

[10] CP Initial Order, 151 FERC ¶ 61,208 at P 163.

> (the number of days in the Delivery Year / 30) / (the number of Real-Time Settlement Intervals in an hour).[11]

In its Capacity Performance proposal, PJM explained that the 30 PAH used to calculate the Penalty Rate[12] is "a reasonable, forward-looking allowance for the number of hours that Emergency Actions could be in effect each year."[13] Although the Commission accepted PJM's 30 PAH estimate, it also recognized that "the [PAH] estimate affects core components of the Capacity Performance design, including the Non-Performance Charge rate and the default offer cap," and therefore required PJM to "mak[e] annual informational filings with the Commission to provide updates on the use of 30 hours for this parameter."[14]

Just as the Capacity Performance construct penalizes capacity resources for failing to perform as expected during a PAI/PAH, it also rewards resources that help maintain reliability during emergencies. Accordingly, any collected Non-Performance Charges are distributed among

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[11] Tariff, Attachment DD, § 10A(e). Attachment DD to the Tariff also sets forth a "stop-loss" provision that limits Non-Performance Charges as follows:

> The Non-Performance Charges for each Capacity Performance Resource (including locational UCAP from such a resource) and each PRD Provider for a Delivery Year shall not exceed a Non-Performance Charge Limit equal to 1.5 times the Net Cost of New Entry times the megawatts of Unforced Capacity committed by such resource or such PRD Provider times the number of days in the Delivery Year.

Id., § 10A(f).

[12] The amount of PAI/PAH used to calculate the Penalty Rate is sometimes referred to herein as the "Penalty PAI" or "Penalty PAH." *See also* September 2 Order, 176 FERC ¶ 61,137 at P 4.

[13] Reforms to the Reliability Pricing Market ("RPM") and Related Rules in the PJM Open Access Transmission Tariff ("Tariff") and Reliability Assurance Agreement Among Load Serving Entities ("RAA"), Transmittal Letter at 43, Docket No. ER15-623-000 (filed Dec. 12, 2014). *See also id.* at 43-44 (explaining that "there were 23 such hours in the 2013/2014 Delivery Year," and that "PJM is reasonably adding some additional hours to that value to reflect the possibility that there could be a higher number of emergency hours in any given Delivery Year in the future").

[14] CP Initial Order, 151 FERC ¶ 61,208 at P 163 (footnote omitted).

the resources that performed better than expected during the PAI/PAH.[15] In this respect, because an energy-only resource is not expected to perform during a PAI/PAH, its full output during an emergency would be considered over-performance that would entitle it to a performance bonus.[16]

This system of potential penalties or bonus payments also underlay the design of the default MSOC that was adopted as part of the initial Capacity Performance structure. In the Commission's words, the default MSOC was based on the understanding that a resource would "be willing to take on a capacity obligation as long as the amount it can earn for capacity (including both capacity auction revenues as well as net Performance Bonus Payments) exceeds the amount it could earn in Performance Bonus Payments by participating in the energy market only."[17] The default MSOC was therefore set at the Penalty Rate "times the Balancing Ratio (B) times the total number of PAI in a given delivery year (Expected PAI)."[18] The assumption was also that the expected PAI underlying the default MSOC would be the same as the Penalty PAI (*i.e.*, 30 PAH/360 PAI), meaning that the default MSOC was effectively Net CONE multiplied by B. This provision thereby assumed that a Capacity Performance Resource would perform at the Balancing Ratio

[15] *See* Tariff, Attachment DD, § 10A(g) ("Revenues collected from assessment of Non-Performance Charges for a Performance Assessment Interval shall be distributed to each Market Participant, whether or not such Market Participant committed a Capacity Resource or Locational UCAP for a Performance Assessment Interval, that provided energy or load reductions above the levels expected for such resource during such interval.").

[16] *See id.*

[17] CP Initial Order, 151 FERC ¶ 61,208 at P 336.

[18] September 2 Order, 176 FERC ¶ 61,137 at P 4 (footnotes omitted). *See also* Tariff, Attachment DD, § 6.4(a) (providing that the default MSOC would be "the product of (the Net Cost of New Entry [(the "Net CONE")] applicable for the Delivery Year and Locational Deliverability Area for which such Capacity Performance Resource is offered times the average of the Balancing Ratios [(sometimes referred to as "B")] in the three consecutive calendar years (during the [PAI] in such calendar years) that precede the Base Residual Auction [("BRA")] for such Delivery Year)"); *id.*, § 10A (defining the Balancing Ratio as "(All Actual Generation Performance, Storage Resource Performance, Net Energy Imports and Demand Response Bonus Performance) / (All Committed Generation and Storage Capacity) . . . .").

multiplied by its committed capacity, and would be foregoing potential bonus payments associated with such performance by taking on a capacity commitment. A critical part of the default MSOC was language in Section 6.4(a) of Attachment DD making clear that "the submission of a Sell Offer with an Offer Price at or below the revised Market Seller Offer Cap permitted under this proviso shall not, in and of itself, be deemed an exercise of market power in the [Reliability Pricing Model ("RPM")] market."[19] Alternatively, a supplier that wished to submit an offer above the default MSOC may seek a unit-specific MSOC based on its net Avoidable Cost Rate ("ACR"),[20] where the assumption was that the unit's ACR would exceed potential bonus revenues.[21]

B. Complaints in Docket Nos. EL19-47 and EL19-63

On February 21, 2019, the Independent Market Monitor for PJM (the "IMM") filed a complaint in Docket No. EL19-47 arguing that the 30 PAH/360 PAI assumption that PJM included in its Capacity Performance proposal was overstated.[22] The IMM Complaint argued that "[d]uring 2015, 2016 and 2017, there were zero emergency events that would have triggered a PAI in PJM,"[23] and that "[t]he continued level of PJM's excess reserve margins . . . reduces the likelihood of having emergency actions that could trigger PAIs."[24] In addition, the IMM Complaint stated that simulations conducted by PJM showed that "if the capacity market cleared at the target

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[19] Tariff, Attachment DD, § 6.4(a).

[20] *See id.*

[21] *See* CP Initial Order, 151 FERC ¶ 61,208 at P 339.

[22] Complaint of the Independent Market Monitor for PJM, Docket No. EL19-47-000 (filed Feb. 21, 2019) (the "IMM Complaint").

[23] *Id.* at 17.

[24] *Id.* at 14.

[Installed Reserve Margin ("IRM")], the expected number of PAH is 15, and if the capacity market cleared with actual observed IRM, the expected number of PAH is two."[25]

The IMM proposed to use an estimate of 5 PAH, which was "based on using the two hour estimate that PJM's resource adequacy study estimated for the number of PAH with the actual, observed IRM of 21.8 percent, and adding three hours to account for the possibility of additional emergency events that might occur during the winter period."[26] At the same time, while claiming that the formula underlying the default MSOC should therefore use "60 intervals (5 hours) as the estimate for H," the IMM also proposed to "keep[] the non-performance charge rate unchanged."[27] Effectively, this would have meant that the default MSOC would be set at "one-sixth of net CONE times B . . . ."[28]

On April 15, 2019, the Joint Consumer Advocates (the "JCA") filed a complaint against PJM in Docket No. EL19-63, which echoed many of the arguments in the IMM Complaint.[29] Like the IMM, the JCA argued that "PJM's current reliance on 360 PAI, or 30 hours per year, is far above what the market has actually borne and 'does not accurately reflect market participants' reasonable expectations.'"[30] The JCA Complaint requested that the MSOC be reduced "at least to

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[25] *Id.*

[26] *Id.* at 17.

[27] *Id.*

[28] *Id.* at 18.

[29] Complaint and Motion for Consolidation, Docket No. EL19-63-000 (filed Apr. 15, 2019) (the "JCA Complaint," and with the IMM Complaint, the "Complaints").

[30] *Id.* at 9 (footnote omitted).

the level of recent rolling average RTO clearing price,"[31] but like the IMM, argued that no changes should be made to the Penalty Rate.[32]

On March 18, 2021, the Commission issued an order granting the IMM and JCA Complaints, and ordering briefing on the appropriate remedy.[33] In granting the Complaints, the Commission found that:

> 360 is no longer a reasonable estimate of Expected PAI and therefore that the default offer cap resulting from 360 Expected PAI is also unjust and unreasonable. Based on the record demonstrating consistently low PAI each year, we find that 360 PAI exceeds market participants' reasonable, actual expectations of the number of PAI the system will experience in a given year. Therefore, we find that the default offer cap described in the Tariff is incorrectly calibrated such that it may unjustly and unreasonably prevent the appropriate review of offers, thereby allowing potential exercises of market power, and reducing the capacity market's overall competitiveness.[34]

The Commission ordered additional briefing on the appropriate remedy, explaining:

> The record assembled to date largely addresses whether the replacement rate should focus on a reduction in the number of Expected PAI used to calculate the default offer cap. Although revising the Expected PAI used to establish the default offer cap may ultimately represent the just and reasonable replacement rate, we find it is necessary to direct briefing that would enable the Commission to further consider the appropriate replacement rate, including alternative approaches to market power mitigation in the capacity market.[35]

The March 18 Order further directed as follows:

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[31] *Id.* at 3.

[32] *Id.* at 11.

[33] *Independent Market Monitor for PJM v. PJM Interconnection, LLC*, 174 FERC ¶ 61,212 (2021) (the "March 18 Order").

[34] *Id.* at P 65 (footnote omitted).

[35] *Id.* at P 71 (footnote omitted).

> Parties should address the appropriateness of using different values for Penalty PAI and Expected PAI in the default Capacity Performance market seller offer cap calculation and the appropriate method for setting each value, including for updating one or both over time. Parties also should address whether revisions to the default offer cap can be made without revision to the unit-specific offer cap review process outlined in section 6 of Attachment DD of the Tariff, including whether and how that process should account for the risk of Capacity Performance penalties.[36]

In response to the March 18 Order, the Indicated Suppliers filed initial and reply briefs, supported with testimony by Roy J. Shanker, Ph.D., and William Stokes, Senior Vice President – Power Trading of Calpine.[37] The Indicated Suppliers Briefs explained that it was inappropriate to use a limited historical period to determine the default MSOC, as suppliers need to be able to reflect the substantial risks associated with assuming capacity obligations in their offers.[38] The Indicated Suppliers further explained that recent events in California and Texas have demonstrated the difficulty of predicting when extreme conditions may occur, and that such conditions may persist for extended periods. The Indicated Suppliers therefore recommended that the default MSOC be calculated using an Expected PAI of 11.5 to 15 PAH, based on the General Electric Multi-Area Reliability Simulation Program simulations that the IMM itself relied on in the IMM

[36] *Id.* at P 72 (footnote omitted).

[37] Initial Brief of the Indicated Suppliers, Docket Nos. EL19-47-000, *et al.* (filed May 3, 2021) (the "Indicated Suppliers Initial Brief"); *id.*, Attachment A, Affidavit of Roy J. Shanker, Ph.D. (the "Shanker Initial Affidavit"); *id.*, Attachment B, Affidavit of William Stokes (the "Stokes Affidavit"); Reply Brief of the Indicated Suppliers, Docket Nos. EL19-47-000, *et al.* (filed June 9, 2021) (the "Indicated Suppliers Reply Brief," and together with the Indicated Suppliers Initial Brief, the "Indicated Suppliers Briefs"); *id.*, Attachment A, Reply Affidavit of Roy J. Shanker, Ph.D. (the "Shanker Reply Affidavit," and together with the Shanker Initial Affidavit, the "Shanker Affidavits").

[38] The Indicated Suppliers explained that suppliers with capacity obligations are not only exposed to the risk of incurring Non-Performance Charges, but are also obligated to submit offers into the Day-Ahead Energy Market and if scheduled, are required to pay for any energy that is not delivered at the applicable Real-time Price, which can be anticipated to be very high during a PAI/PAH. *See* Indicated Suppliers Initial Brief at 16-17.

Complaint. In addition, the Indicated Suppliers emphasized the need for the Expected PAI used to calculate the default MSOC to be the same as the Penalty PAI/Penalty PAH used to calculate the Penalty Rate in order to be consistent with the structure of the Capacity Performance construct. P3 and EPSA also submitted a reply brief making similar points and supporting the recommendations of the Indicated Suppliers and certain other suppliers.[39]

C. The September 2 Order

The September 2 Order replaced the existing default MSOC with the "Unit-Specific Net ACR Proposal" advanced by the IMM.[40] Under this proposal, offers will be "capped at the resource's unit-specific net ACR, meaning unit-specific gross ACR minus forward-looking net energy and ancillary service revenues, with the option to use the technology-specific default gross ACRs minus unit-specific forward-looking net energy and ancillary service revenues . . . ."[41] The Commission further found that "the Unit-Specific ACR Proposal is preferable to the other options presented in the paper hearing because it would best ensure the capacity market's overall competitiveness and enable the Market Monitor and PJM to sufficiently review and mitigate offers to prevent the exercise of market power."[42] In eliminating the default MSOC, the September 2 Order also deleted the language in Section 6.4(a) of Attachment DD providing that offers at or below the default MSOC would not be deemed an exercise of market power.[43]

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[39] *See* Reply Brief of the PJM Power Providers Group and Electric Power Supply Association, Docket Nos. EL19-47-000, *et al.* (filed June 9, 2021) (the "P3/EPSA Reply Brief").

[40] *See* September 2 Order, 176 FERC ¶ 61,137 at P 61.

[41] *Id.* at P 8 (footnotes omitted).

[42] *Id.* at P 61 (footnote omitted).

[43] *See id.*, Appendix A.

II.

STATEMENT OF ISSUES

In accordance with Rule 713(c)(2) of the Commission's Rules of Practice and Procedure,[44] the Indicated Parties hereby identify each issue on which they seek rehearing of the September 2 Order, and provide representative precedent in support of their position on each of those issues:

1. The September 2 Order is arbitrary and capricious and fails to reflect reasoned decision-making, in violation of the Administrative Procedure Act (the "APA"),[45] because the Commission erroneously suggests that suppliers will be able to reflect the risks associated with capacity obligations in their offers through unit-specific ACR determinations. In so doing, the September 2 Order ignores limitations on the types of risks that may be included under the existing ACR formula. *See Motor Vehicle Mfrs. Ass'n of the U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) ("*State Farm*").

2. The September 2 Order fails to properly respond to arguments by the Indicated Suppliers and Dr. Shanker explaining that a more flexible MSOC is required because the existing ACR formula does not account for different types of risks imposed on certain resources. *See, e.g., PPL Wallingford Energy LLC v. FERC*, 419 F.3d 1194, 1198 (D.C. Cir. 2005) ("*PPL Wallingford*"); *NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158, 1165 (D.C. Cir. 1998) ("*NorAm*").

3. The September 2 Order is arbitrary and capricious and contrary to law, because the Commission eliminated the flexibility provided by the default MSOC without making changes to either the ACR formula or to the must-offer requirements applicable to traditional resources, without addressing arguments that this would have an unduly discriminatory impact on traditional resources, in violation of the requirements of the FPA. *See* 16 U.S.C. § 824d(b) (2018); 16 U.S.C. § 824e(a) (2018); *PPL Wallingford*, 419 F.3d at 1198; *City of Vernon v. FERC*, 845 F.2d 1042, 1048 (D.C. Cir. 1988) ("*Vernon*").

4. Even with respect to the limited risks that may be reflected in the existing ACR formula, the Commission fails to address arguments regarding the need for flexibility in light of the difficulty of quantifying and supporting such risks. *See, e.g., PPL Wallingford*, 419 F.3d at 1198; *NorAm*, 148 F.3d at 1165. Moreover, the September 2 Order's suggestion that PJM and the

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[44] 18 C.F.R. § 385.713(c)(2) (2021).

[45] 5 U.S.C. §§ 551, *et seq.* (2018).

IMM are capable of accounting for such risks is illogical in light of PJM's own arguments. *See, e.g., Baltimore Gas & Elec. Co. v. Natural Res. Def. Council, Inc.*, 462 U.S. 87, 105 (1983) ("*Baltimore Gas*").

5. Rehearing of the September 2 Order is required because the Commission's finding that "concerns that the [IMM] will not entertain alternative expectations of risk [are] speculative," September 2 Order, 176 FERC ¶ 61,137 at P 69, is illogical on its face and is contrary to the record evidence as well as other statements made by the IMM. *See, e.g.*, 5 U.S.C. § 706(2)(E) (2018); *Allentown Mack Sales & Serv., Inc. v. NLRB*, 522 U.S. 359, 374 (1998) ("*Allentown*"); *Illinois Commerce Comm'n v. FERC*, 576 F.3d 470, 477 (7th Cir. 2009) ("*ICC*"); *Pacific Gas & Elec. Co. v. FERC*, 373 F.3d 1315, 1319 (D.C. Cir. 2004) ("*PG&E*").

6. The September 2 Order is arbitrary and capricious because the adoption of MSOCs that do not account for the risks and opportunity costs associated with capacity commitments represents an unacknowledged and unexplained departure from the Commission's CP Orders. *See FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009) ("*Fox*"); *West Deptford Energy, LLC v. FERC*, 766 F.3d 10, 20 (D.C. Cir. 2014) ("*West Deptford*").

7. The September 2 Order fails to reflect reasoned decision-making because it does not respond meaningfully to arguments by the Indicated Suppliers and others raising concerns with respect to the IMM's Unit-Specific Net ACR Proposal. *See, e.g., Public Utils. Comm'n of Cal. v. FERC*, 462 F.3d 1027, 1051 (9th Cir. 2006) ("*CPUC*"); *PPL Wallingford*, 419 F.3d at 1198; *NorAm*, 148 F.3d at 1165.

8. The September 2 Order does not reflect reasoned decision-making because it fails to address the Indicated Suppliers' and Dr. Shanker's explanations that adjusting the PAI/PAH used to calculate both the default MSOC and the Penalty Rate would address market power concerns by resulting in a default MSOC that properly accounts for the risks and opportunity costs associated with capacity obligations. *See, e.g., PPL Wallingford*, 419 F.3d at 1198; *NorAm*, 148 F.3d at 1165. At the same time, the Commission did not provide any rationale for departing from its findings in the CP Orders that such an offer would be competitive. *See, e.g., West Deptford*, 766 F.3d at 20.

9. Rather than seriously considering and responding to intervenors' proposals and arguments, the September 2 Order erroneously suggests that the March 18 Order found that an MSOC is only effective as a mitigation measure to the extent that it is likely to result in review of the marginal offer, and further mischaracterized the findings in the March 18 Order. *See* September 2 Order, 176 FERC ¶ 61,137 at PP 64-65. *See also* 5 U.S.C. § 706(2)(E) (2018); *Code v. McCarthy*, 959 F.3d 406, 409 (D.C. Cir. 2020) (*"Code*");

Natural Res. Def. Council v. U.S. Forest Serv., 421 F.3d 797, 816 (*"NRDC*").

10. The September 2 Order is arbitrary and capricious because, by replacing the default MSOC with the IMM's Unit-Specific Net ACR Proposal while keeping the Penalty Rate and Penalty PAI unchanged, the September 2 Order illogically results in mismatched offer caps and potential penalties. *See, e.g., ANR Storage Co. v. FERC*, 904 F.3d 1020, 1028 (D.C. Cir. 2018) ("*ANR*"); *GameFly, Inc. v. Postal Regulatory Comm'n*, 704 F.3d 145, 148 (D.C. Cir. 2013) ("*GameFly*").

11. The September 2 Order fails to reflect reasoned decision-making because the Commission's failure to adjust the Penalty Rate and Penalty PAI is at odds with its recognition in the CP Orders that penalties must be sufficiently high to ensure that suppliers have incentives to perform. *See*, *e.g.*, *Good Samaritan Medical Ctr. v. NLRB*, 858 F.3d 617, 629 (1st Cir. 2017) ("*Good Samaritan*"); *Williams Gas Processing-Gulf Coast Co., L.P. v. FERC*, 475 F.3d 319, 322 (D.C. Cir. 2006) ("*Williams*").

III.

REQUEST FOR REHEARING

The September 2 Order fails to reflect reasoned decision-making. The Commission not only neglected its obligation to respond meaningfully to arguments and evidence presented by the Indicated Suppliers and others, but also completely failed to explain how an MSOC set at the Unit-Specific Net ACR will reflect the risks and costs that suppliers must assume in taking on capacity commitments in PJM or is consistent with the structure of PJM's Capacity Performance construct.

A. Rehearing of the September 2 Order is Required Because It Results in an MSOC That Does Not Permit Suppliers to Reflect the Risks and Opportunity Costs Associated with Assuming Capacity Obligations in PJM and That is Unduly Discriminatory

Under the September 2 Order, the new MSOC will be "a given resource's applicable default gross ACR value less the resource's unit-specific EAS Offset calculated by the Market Monitor . . . ."[46] The default gross ACR values were developed by PJM and the Brattle Group

[46] September 2 Order, 176 FERC ¶ 61,137 at P 63 (footnote omitted).

("Brattle") and accepted by the Commission in the context of proceedings involving the Minimum Offer Price Rule ("MOPR").[47] Nothing in that default gross ACR accounts for the risks associated with incurring Non-Performance Charges or other costs, or the opportunity costs of foregoing potential bonus payments.[48]

The September 2 Order nonetheless states that suppliers will be able to reflect their risks through the Capacity Performance Quantifiable Risk ("CPQR") component of the ACR formula.[49] But the Commission "entirely fail[s] to consider an important aspect of the problem . . . ."[50] While suppliers may "include expected non-performance penalties in CPQR,"[51] the Commission took no steps to ensure that the ACR formula properly reflects all of the risks that are associated with a capacity obligation. In particular, the September 2 Order rejected arguments that the ACR formula should be modified to reflect the risks associated with "volatile energy market revenues, liquidated damages, and unanticipated outages,"[52] claiming that "the Commission already rejected such requests in the Capacity Performance proceeding."[53] This ignores the fact that these types of risks were precisely why a default MSOC was necessary, because it "afford[ed] market sellers flexibility

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[47] *See id.* (citing *Calpine Corp. v. PJM Interconnection, L.L.C.*, 173 FERC ¶ 61,061 at P 201 (2020) ("EL16-49 October 2020 Order")).

[48] *See* Compliance Filing Concerning the Minimum Offer Price Rule, Request for Waiver of RPM Auction Deadlines, and Request for Extended Comment Period of at Least 35 Days, Attachment D, Affidavit of Samuel A. Newell, John M. Hagerty and Sang H. Gang on behalf of PJM Interconnection, L.L.C., Exhibit 2, Gross Avoidable Cost Rates for Existing Generation and Net Cost of New Entry for New Energy Efficiency Docket No. ER18-1314-003 (filed Mar. 18, 2020) (describing development of gross ACRs for various existing generation resource types). *See also* EL16-49 October 2020 Order, 173 FERC ¶ 61,061 at P 201 (accepting same).

[49] September 2 Order, 176 FERC ¶ 61,137 at PP 69, 71.

[50] *State Farm*, 463 U.S. at 43.

[51] September 2 Order, 176 FERC ¶ 61,137 at P 75.

[52] *Id.* at P 72.

[53] *Id.* (footnote omitted).

to evaluate the additional costs and risks they face from offering into the revised capacity market, consistent with the principle that market sellers bear responsibility for resource performance."[54] Similarly, the Indicated Suppliers explained that, "[u]nder the existing construct where the default MSOC and the Non-Performance Charge Rate are both based on a reasonable estimate of the PAI that can be expected in a particular Delivery Year, sufficient flexibility is provided to the traditional resource owner to reflect the full risks that it faces."[55] It therefore makes no sense for the September 2 Order to remove that flexibility while also refusing to make other modifications to permit suppliers to account for their risks in their offers.

The need for a default MSOC that provides flexibility is particularly acute for traditional resources because, as the Indicated Suppliers explained, Intermittent Resources and Capacity Storage Resources are not subject to the same energy must-offer obligation as traditional resources and thus have greater flexibility to reduce their exposure to the risk of having to pay for replacement energy at the Real-time Price.[56] The Indicated Suppliers further explained that, in the event that the Commission chose to adopt the IMM's proposal but did not modify the ACR formula to permit consideration of additional risks and costs, it would also need to revisit the must-offer rules in order to give traditional resources the same optionality as Intermittent Resources and

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54 CP Rehearing Order, 155 FERC ¶ 61,157 at P 187.

55 Indicated Suppliers Reply Brief at 20.

56 *See* Indicated Suppliers Initial Brief at 16-19. As explained in the Indicated Suppliers Initial Brief, capacity resources are "subject to a must-offer requirement and are required to submit offers into the Day-Ahead Energy Market." Indicated Suppliers Initial Brief at 16 (citing Tariff, Attachment K – Appendix, § 1.10(d)). Moreover, if scheduled in the Day-Ahead Energy Market, the capacity resource is then obligated to "replace the energy not delivered with energy from the Real-time Energy Market and shall pay for such energy at the applicable Real-time Price." *Id.* (citing Tariff, Attachment K – Appendix, § 1.10.4(a)).

Capacity Storage Resources.[57] As the Indicated Suppliers explained, because Intermittent Resources and Capacity Resources are subject to less onerous must-offer rules than traditional resources,

> Intermittent Resources and Capacity Storage Resources have ways to manage their risks that are not available to traditional resources. For example, an Intermittent Resource or Capacity Storage Resource that is concerned regarding potential PAI that are not recognized by the IMM in its net ACR review could simply not offer all of its capacity (or its energy), and hold such capacity in reserve so that it is available in the event of an emergency, without the risk of losing its CIRs. The Intermittent Resource or Capacity Storage Resource is therefore not dependent on a correctly-calculated MSOC to protect itself against potential risks and associated costs, because it can rely on its own output to cover potential penalties and provide replacement energy, without any risk to its CIRs.[58]

But the Commission failed to properly address the Indicated Suppliers' arguments in violation of its obligations under the APA.[59] While the Indicated Parties understand that the capacity and energy must-offer requirements "are not at issue in this proceeding,"[60] the September 2 Order erroneously found that no modifications to the must-offer requirements were necessary despite the elimination of the default MSOC. The September 2 Order held that modifications of

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[57] *See* Indicated Suppliers Reply Brief at 18-21. In addition, the Indicated Suppliers Reply Brief further explained that traditional resources may lose their Capacity Interconnection Rights ("CIRs") if they do not offer their capacity into the RPM auctions, while such limitations do not apply to Intermittent Resources, Capacity Storage Resources, Demand Resources, and Energy Efficiency Resources. *See id.* at 18-19.

[58] *Id.* at 19-20.

[59] *See, e.g.*, *PPL Wallingford*, 419 F.3d at 1198 (requiring the Commission to "respond meaningfully" to concerns raised by parties); *NorAm*, 148 F.3d at 1165 (reversing order in which the Commission "not only failed to provide an adequate response to [petitioner's] argument, it failed to take seriously its responsibility to respond at all"); *K N Energy, Inc. v. FERC*, 968 F.2d 1295, 1303 (D.C. Cir. 1992) (stating that an agency must "engage the arguments raised before it – that it conduct a process of *reasoned* decisionmaking" (emphasis in original)).

[60] September 2 Order, 176 FERC ¶ 61,137 at P 74.

the must-offer requirement would adversely affect reliability and raise market power concerns,[61] without responding to the crux of the Indicated Suppliers' arguments.[62] Nowhere did the Commission address the issue of how the elimination of the default MSOC would result in greater harm to traditional resources because of the uneven must-offer requirements imposed on different types of resources.[63] Instead, the September 2 Order simply eliminated the default MSOC and the flexibility thereunder without any acknowledgement that this would impose greater hardship and have an unduly discriminatory impact on traditional resources in violation of the FPA.[64]

Even aside from the limited scope of costs that may be included under the ACR formula, the Commission's suggestion that suppliers will be able to reflect their risks in the CPQR fails to properly consider the requirements of the Tariff, which states as follows:

> CPQR (Capacity Performance Quantifiable Risk) consists of the ***quantifiable and reasonably-supported costs*** of mitigating the risks of non-performance associated with submission of a Capacity Performance Resource offer (or of a Base Capacity Resource offer for the 2018/19 or 2019/20 Delivery Years), such as insurance expenses associated with resource non-performance risks. CPQR shall be considered reasonably supported if it is based on actuarial practices generally used by the industry to model or value risk and if it is based on actuarial practices used by the Capacity Market Seller to model or value risk in other aspects of the Capacity Market

61 *See id.*

62 *See, e.g., Vernon*, 845 F.2d at 1048 (explaining that "an agency is not entitled under the APA to respond with a non sequitur" (citations omitted)); *Tennessee Gas Pipeline Co. v. FERC*, 824 F.2d 78, 84 (D.C. Cir. 1987) (finding decision to be arbitrary and capricious where the Commission's finding was a "complete *non sequitur*").

63 The September 2 Order simply stated, without elaboration, that "no party has demonstrated that the elimination of the default offer cap renders [the must-offer rules] unjust and unreasonable." September 2 Order, 176 FERC ¶ 61,137 at P 74. This type of "conclusory and unexplained statement is not the 'reasoned' explanation required by the APA." *Environmental Health Trust v. FCC*, 9 F.4th 893, 909 (D.C. Cir. 2021).

64 *See* 16 U.S.C. § 824d(b) (2018); 16 U.S.C. § 824e(a) (2018). *See also Ala. Elec. Coop., Inc. v. FERC*, 684 F.2d 20, 254 (D.C. Cir. 1982) (explaining that charging the same rate to customers that are not similarly situated "may be considered discrimination," just as charging "different rates to customer classes which are similarly situated" may be unduly discriminatory).

> Seller's business. Such reasonable support shall also include an officer certification that the modeling and valuation of the CPQR was developed in accord with such practices. Provision of such reasonable support shall be sufficient to establish the CPQR. A Capacity Market Seller may use other methods or forms of support for its proposed CPQR that shows the CPQR is limited to risks the seller faces from committing a Capacity Resource hereunder, that ***quantifies*** the costs of mitigating such risks, and that includes supporting documentation (which may include an officer certification) for the identification of such risks and ***quantification*** of such costs. Such showing shall establish the proposed CPQR upon acceptance by the Office of the Interconnection.[65]

This Tariff language is unduly restrictive, because it will be exceedingly difficult for suppliers to "quantify" and "support" their predictions of the risks associated with potential emergency conditions. In fact, PJM's filing proposing its Capacity Performance construct argued that a default MSOC was needed because "costs and risks may be difficult to quantify, especially on a three-year forward basis."[66] As explained in detail in the Indicated Suppliers Initial Brief and Shanker Initial Affidavit, this is particularly true with respect to low probability/high impact events such as the Polar Vortex that led to the adoption of the Capacity Performance construct, as well as extreme conditions seen in California and Texas in 2020 and 2021, which are very difficult to model and document as required under the Tariff.[67] The Indicated Suppliers therefore urged the Commission to "adopt a PAI/PAH that properly accounts for the possibility of the types of low probability/high impact events discussed in the Shanker [Initial] Affidavit."[68] The Commission, however, failed to properly respond to the arguments put forward by the Indicated Suppliers regarding the need for the MSOC to be flexible in light of the difficulty of predicting and

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65 Tariff, Attachment DD, § 6.8 (emphases added).

66 CP Initial Order, 151 FERC ¶ 61,208 at P 297.

67 *See* Indicated Suppliers Initial Brief at 8-11.

68 *Id.* at 12.

documenting the risks and potential costs associated with assuming a capacity obligation.[69] The Commission asserted that the "currently effective Tariff already requires PJM and the [IMM] to make determinations regarding CPQR . . . ."[70] But this finding fails to reflect reasoned decision-making and is plainly illogical,[71] given that the September 2 Order simultaneously acknowledges that PJM itself has taken the position that "unit-specific review is unworkable because of the complexity of calculating and quantifying risk under the Capacity Performance construct."[72]

Finally, the Commission cavalierly brushed aside concerns raised by the Indicated Suppliers and others that the IMM will reject their proposed CPQRs, claiming that "concerns that the [IMM] will not entertain alternative expectations of risk [are] speculative."[73] This finding is "unsupported by substantial evidence" in violation of the APA[74] and the FPA.[75] As the Indicated Suppliers explained,[76] the IMM made clear that CPQR should be calculated "based on unit specific values for A, B and H,"[77] where H is "the expected number of PAI during the delivery year . . . ."[78] But as noted in the March 18 Order, this proceeding stemmed from the IMM's assertion that "a

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[69] *See, e.g.*, *PPL Wallingford*, 419 F.3d at 1198; *NorAm*, 148 F.3d at 1165.

[70] September 2 Order, 176 FERC ¶ 61,137 at P 69.

[71] *See Baltimore Gas*, 462 U.S. at 105 (agency must "consider[] the relevant factors and articulate[] a rational connection between the facts found and the choice made" (citations omitted)).

[72] September 2 Order, 176 FERC ¶ 61,137 at P 69.

[73] *Id.*

[74] 5 U.S.C. § 706(2)(E) (2018).

[75] 16 U.S.C. § 825*l*(b) (2018). *See also ICC*, 576 F.3d at 477 (explaining that a reviewing court cannot "uphold a regulatory decision that is not supported by substantial evidence on the record as a whole"); *PG&E*, 373 F.3d at 1319 (the Commission's orders must be "based upon substantial evidence in the record" (quoting *Northern States Power Co. v. FERC*, 30 F.3d 177, 180 (D.C. Cir. 1994)).

[76] *See* Indicated Suppliers Reply Brief at 9-10.

[77] Brief of the Independent Market Monitor for PJM at 5, Docket Nos. EL19-47-000, *et al.* (filed Apr. 28, 2021) (the "IMM Initial Brief").

[78] *Id.* at 4.

reasonable Expected PAI is close to zero . . . ."[79] More recently, the IMM again asserted in this proceeding that suppliers' "real expectations [are] close to zero PAH."[80] In fact, the IMM rationalized its Unit-Specific Net ACR Proposal based on "the low historical and low expected number of PAI . . . ."[81] It is thus plainly wrong for the Commission to take the position that the IMM will accept suppliers' views of risk, when the entirety of the IMM's position in this proceeding has been based on the IMM's stated belief that the expected PAI should be at or close to zero.[82] Moreover, even in claiming that it is willing to entertain different views of risks, the IMM also asserted that any such differences should be "consistent with the locational distribution of emergency actions in PJM," and that it intends to "analyze[] the assumptions used in calculating these risks to ensure that CPQR reasonably reflects ***actual risks*** . . . ."[83] The IMM's own statements in this proceeding have therefore made clear that it has an exceedingly narrow view of the differences between resources that may be validly taken into account, and of the PAI that may be used in a CPQR calculation. The Commission, however, ignored all of this, choosing instead to focus solely on the IMM's statement that "it recognizes that different market sellers have different expectations."[84] Rehearing is therefore required, because the Commission cannot simply

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79 March 18 Order, 174 FERC ¶ 61,212 at P 7.

80 Answer and Motion for Leave to Answer of the Independent Market Monitor for PJM at 2, Docket Nos. EL19-47-000, *et al.* (filed June 25, 2021) (the "IMM Answer"). *See also id.* at 3 ("The current complaint exists because that open discussion on estimating PAI failed to recognize and update the estimated PAI to a value that reflects reality.").

81 IMM Initial Brief at 4.

82 *See, e.g., Allentown*, 522 U.S. at 374 (the process by which an agency arrives at a particular "result must be logical and rational"); *Baltimore Gas*, 462 U.S. at 105 (agency must "consider[] the relevant factors and articulate[] a rational connection between the facts found and the choice made" (citations omitted)).

83 IMM Answer at 4 (emphasis added).

84 September 2 Order, 176 FERC ¶ 61,137 at P 69.

"confine its attention to evidence that support[s] its conclusion and . . . ignore[] any contrary evidence."[85]

Critically, the IMM has also taken positions outside these proceedings that make it even more unlikely that suppliers will attempt, much less be allowed, to cover their risks and costs through the unit-specific review process. In stakeholder proceedings, the IMM has indicated that, for a resource with a low forced outage rate, the "competitive offer is ***less than*** its Net ACR."[86] Even more problematically, the IMM has also notified suppliers that, "[i]f the Capacity Market Seller ***indicates disagreement*** with the [IMM's] MSOC values, . . . or determinations, the [IMM] will evaluate whether it must bring the matter to the attention of the Federal Energy Regulatory Commission."[87] Given the costs associated with responding to an investigation by the Commission's Office of Enforcement, it is foreseeable that this threat of referral alone will deter

85 *International Union, United Auto., Aerospace & Agr. Implement Workers of Am. v. NLRB*, 802 F.2d 969, 975 (7th Cir. 1986). *See also Genuine Parts Co. v. EPA*, 890 F.3d 304, 311 (D.C. Cir. 2018) (making clear that "an agency cannot ignore evidence that undercuts its judgment . . . [or] minimize such evidence without adequate explanation"); *Tenneco Gas v. FERC*, 969 F2d 1187, 1214 (D.C. Cir. 1992) (finding that "a FERC order neglectful of pertinent facts on the record must crumble for want of substantial evidence"); *Lakeland Bus Lines, Inc. v. NLRB*, 347 F.3d 955, 963 (D.C. Cir. 2003) (holding that the agency may not rely on a "clipped view of the record" to support its conclusion); *Schurz Commc'ns, Inc. v. FCC*, 982 F.2d 1043, 1050 (7th Cir. 1992) (finding decision to be arbitrary and capricious where the agency in "ostrich fashion, did not discuss the most substantial objections to its approach, though the objections were argued vigorously to it").

86 Monitoring Analytics, *Market Seller Offer Cap (MSOC)*, at 12 (presentation to the MIC Special Session, Sept. 17, 2021) ("IMM MIC Presentation") (emphasis added), https://pjm.com/-/media/committees-groups/committees/mic/2021/20210917-special/20210917-item-03-market-seller-offer-cap-msoc.ashx.

87 Monitoring Analytics, IMM Determinations Posted for the PJM 2023/2024 RPM Base Residual Auction, at 1 (Sept. 2, 2021) (emphasis added), https://www.monitoringanalytics.com/reports/Market_Messages/RPM_Material/IMM_Determinations_on_RPM_Requests_2023-2024_Base_Residual_Auction_20210902.pdf. *See also* IMM MIC Presentation at 6 ("If the Capacity Market Seller indicates disagreement with the [IMM's] MSOC values, the [IMM] will evaluate whether it must bring the matter to the attention of the Federal Energy Regulatory Commission.").

suppliers from attempting to challenge the IMM's determinations.[88] Moreover, it makes little sense for the September 2 Order to assert that suppliers can turn to the Commission to the extent that they disagree with the IMM's or PJM's MSOC determinations,[89] when the IMM has taken the position that even voicing disagreement with the IMM's calculations will expose a supplier to a potential enforcement action. There is therefore no rational basis or support for the Commission's claim that suppliers will have leeway to reflect their own risk expectations in their offers.[90]

B. The Commission Ignored Arguments by the Indicated Parties and Others, and Mischaracterized Its Prior Orders, in Attempting to Justify Its Decision to Adopt the IMM's Proposal

In accepting the existing default MSOC, the Commission recognized that "[u]nder PJM's Capacity Performance market rules, market sellers take on new obligations and risks and obtain additional sources of revenue through Performance Bonus Payments, all of which must be considered in fashioning appropriate mitigation rules."[91] The Commission therefore accepted the default MSOC as properly "afford[ing] market sellers flexibility to evaluate the additional costs and risks they face from offering into the revised capacity market, consistent with the principle that market sellers bear responsibility for resource performance."[92]

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88 *Cf. NRG Power Mktg., LLC*, 174 FERC ¶ 61,016 (2021) (discussing enforcement investigation that resulted from a referral by a market monitor).

89 *See* September 2 Order, 176 FERC ¶ 61,137 at P 69.

90 *See, e.g.*, *Allentown*, 522 U.S. at 374 (the process by which an agency arrives at a particular "result must be logical and rational"); *ICC*, 576 F.3d at 477 (reviewing court cannot "uphold a regulatory decision that is not supported by substantial evidence on the record as a whole").

91 CP Rehearing Order, 155 FERC ¶ 61,157 at P 187.

92 *Id. See also id.* at P 183 (finding that "[m]itigation does not, and should not, protect consumers from actual capacity cost increases that are attributable to necessary investments that allow a capacity resource to participate in the capacity market, including relevant opportunity costs faced by said resource, or risks associated with that resource's participation").

By contrast, as explained above, the September 2 Order will result in MSOCs that are based on default gross ACRs that assume that there is zero risk of a PAI and, correspondingly, minimal risks or opportunity costs associated with assuming a capacity obligation in PJM. Moreover, even under the unit-specific process, it will be exceedingly difficult, if not impossible, for suppliers to include a risk component that reflects their expectations. Nowhere in the September 2 Order does the Commission reconcile this approach with its prior recognition of the risks and costs assumed by suppliers under the Capacity Performance construct,[93] nor does the Commission identify any evidence demonstrating that there is little or minimal risk to suppliers so as to justify this change.[94]

As explained in detail in the Indicated Suppliers Initial Brief, the limited PAI that have occurred in the short amount of time since the implementation of the Capacity Performance construct do not provide a reasonable indication of the risks associated with taking on a capacity obligation in PJM.[95] Both Dr. Shanker and Mr. Stokes of Calpine emphasized that low probability/high impact events, such as the Polar Vortex of 2014, as well as more recent events in California and Texas, demonstrate that emergency events can and do occur at unanticipated times and are very difficult to model.[96] As indicated above, the Indicated Suppliers and Mr. Stokes further explained that suppliers face enormous exposure to penalties, not just from Non-

93 *See, e.g.*, *Fox*, 556 U.S. at 515 (stating that an agency departing from its own precedent must "display awareness that it is changing position" and "show that there are good reasons for the new policy"); *West Deptford*, 766 F.3d at 20 ("It is textbook administrative law that an agency must 'provide[] a reasoned explanation for departing from precedent or treating similar situations differently,' . . . and Commission cases are no exception . . . ." (quoting *ANR Pipeline Co. v. FERC*, 71 F.3d 897, 901 (D.C. Cir. 1995))); *Panhandle E. Pipe Line Co. v. FERC*, 196 F.3d 1273, 1275 (D.C. Cir. 1999) ("As we have repeatedly reminded FERC, if it wishes to depart from its prior policies, it must explain the reasons for its departure." (citations omitted)).

94 *See* 5 U.S.C. § 706(2)(E) (2018); 16 U.S.C. § 825l(b) (2018); *ICC*, 576 F.3d at 477; *PG&E*, 373 F.3d at 1319.

95 *See, e.g.*, Indicated Suppliers Initial Brief at 8-12; P3/EPSA Reply Brief at 4.

96 *See generally* Shanker Initial Affidavit; Stokes Affidavit.

Performance Charges, but also from the obligation to offer into the energy market and pay for replacement energy at potentially very high prices.[97]

In contravention of the Commission's obligations under the APA, the September 2 Order does not provide any response to the Indicated Parties' arguments regarding the need for MSOCs that fully reflect the risks and opportunity costs associated with capacity obligations. Similarly, the Commission utterly failed to respond to concerns raised by another supplier, Exelon Corporation ("Exelon"), that it is inappropriate to "apply the MOPR default gross ACR values to the capacity market offer cap context," and that "the offer floor should reflect the minimum amount a market participant might reasonably need to justify continued operation, while an offer cap reflects the maximum amount."[98] And, the Commission also ignored arguments by the Indicated Suppliers that the IMM's Unit-Specific Net ACR Proposal would, as discussed above, require a determination of the appropriate number of PAI, and that "conducting the type of individualized review of suppliers' PAI expectations as proposed by the IMM raises concerns regarding potentially discriminatory or inconsistent determinations that could create an uneven playing field for suppliers."[99] The Indicated Suppliers further stated that, in contrast, their proposal would ensure more even-handed treatment, as it "provides a transparent and consistent measure of risk that can be easily applied to all suppliers . . . ."[100]

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97 *See supra* note 56.

98 September 2 Order, 176 FERC ¶ 61,137 at P 16 (footnote omitted).

99 Indicated Suppliers Reply Brief at 10 (footnote omitted). *See also* Shanker Reply Affidavit at ¶¶ 10-11.

100 Indicated Suppliers Reply Brief at 7. *See also* Shanker Reply Affidavit at ¶ 11 (explaining that "given the need for an Expected PAI/PAH value in all proposals," the Indicated Suppliers' proposal "is preferable due to the open and transparent discussion and analyses leading to whatever PAI/PAH value is ultimately used").

Instead of providing a "reasoned response" to the arguments above,[101] the Commission responded to the Indicated Suppliers' and Exelon's arguments "with a non sequitur,"[102] claiming that "the Unit-Specific ACR Proposal is preferable to the other options presented in the paper hearing because it would best ensure the capacity market's overall competitiveness and enable the Market Monitor and PJM to sufficiently review and mitigate offers to prevent the exercise of market power."[103] While it is undeniable that the IMM's Unit-Specific ACR Proposal will result in the review of a larger number of offers by the IMM and PJM, the September 2 Order acknowledges that the Commission previously found that "***one way*** to measure the effectiveness of seller-side market power mitigation is whether the marginal offer is reviewed."[104] There is no basis for the September 2 Order to then turn around and claim that any proposed MSOC that does not result in the marginal offer being reviewed does not provide adequate market power mitigation.[105] Moreover, to be clear, the CP Orders did not suggest that the Commission's acceptance of the default MSOC hinged on the IMM's review of the marginal offer.[106] Instead, the CP Rehearing Order explained as follows:

> [T]he Commission accepted PJM's proposed Capacity Performance default offer cap on the grounds that it is based on a reasonable estimate of a low-end competitive offer, after accounting for all marginal costs, opportunity costs, and risks associated with

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101 *CPUC*, 462 F.3d at 1051. *See also, e.g.*, *PPL Wallingford*, 419 F.3d at 1198; *NorAm*, 148 F.3d at 1165.

102 *Vernon*, 845 F.2d at 1048.

103 September 2 Order, 176 FERC ¶ 61,137 at P 61 (footnote omitted).

104 *Id.* at P 62 (emphasis added).

105 *See id.* at P 64 ("We find that the unit-specific review approach included in the Unit-Specific ACR Proposal addresses supplier market power by reviewing the marginal offer while the proposals made by PJM and other parties may not.").

106 *See, e.g.*, 5 U.S.C. § 706(2)(E) (2018); *Code*, 959 F.3d at 409 (reversing where "a basic mistake of fact render[ed] the [agency]'s decision arbitrary and capricious"); *NRDC*, 421 F.3d at 816 (finding decision to be "arbitrary and capricious in violation of the APA" where there was "an important mistake in fact").

> assuming a Capacity Performance commitment. The Commission therefore reasoned that "[a]ny Capacity Performance offer below the default offer cap can properly be deemed competitive[.]" We affirm that finding.[107]

The Commission also emphasized that "consideration of opportunity cost in deriving a default offer cap and in reviewing sell offers above the default offer cap is just and reasonable because it is a legitimate consideration in formulating a competitive offer within the Capacity Performance design."[108] Consistent with these findings, Dr. Shanker explained in detail in his affidavit responding to the IMM Complaint[109] that market power concerns are fully addressed by the Indicated Suppliers' proposal to lower the PAI/PAH used in ***both*** the default MSOC and the Penalty Rate, because this ensures that the default MSOC will properly reflect the risks and opportunity cost of taking on a capacity obligation:

> In the context of the IMM's complaint, the potential market monitoring/market power implications of having either too low a performance penalty or too high an MSOC are also straightforward. Both alternatives create a gap between the correct competitive offer that should reflect the seller's indifference point and the allowed safe harbor of the "old" MSOC and its associated penalty.
>
> From a market monitoring perspective, if the expected number of PAH is less than 30 and the MSOC were not adjusted down, sellers are free to make unmitigated offers in the gap between an indifference point reflecting too low a penalty rate and a higher one reflecting a penalty rate based on the lower PAH. Thus, the IMM proposes to lower the default MSOC. However, if the reality is that if the appropriate PAH is 5 hours, an equivalent action to set the "right" MSOC would be to increase the non-performance charge rate by (in this case) a factor of six to keep the indifference calculations and thus the MSOC the same at B x Net CONE. Indeed, this later approach is superior in my judgment as explained below, and is consistent with the expectation that the PAH would be

107 CP Rehearing Order, 155 FERC ¶ 61,157 at P 184 (footnotes omitted).

108 *Id.* at P 185.

109 *See* Shanker Initial Affidavit, Attachment RJS-2.

> periodically reviewed and that the non-performance charge rate would be adjusted accordingly.[110]

Rather than tackling Dr. Shanker's arguments head on[111] or providing any rationale for departing from the Commission's prior findings in the CP Orders that competitive offers will reflect the risks and opportunity costs associated with capacity obligations,[112] the September 2 Order claimed that "the Commission found in the [March 18] Order that the default offer cap in PJM was too high and that 'Net CONE times B has not been lower than the competitive offer estimate for a resource with a high avoidable cost rate' and was therefore 'inappropriate.'"[113] Respectfully, these are mischaracterizations of the March 18 Order.[114] Rather than finding the default MSOC to be "too high," the March 18 Order in fact found that "360 is no longer a reasonable estimate of Expected PAI and therefore that the default offer cap resulting from 360 Expected PAI is also unjust and unreasonable," and that "360 PAI exceeds market participants' reasonable, actual expectations of the number of PAI the system will experience in a given year."[115] Indeed, the Commission invited comments on "the appropriateness of using different values for

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[110] *Id.* at ¶¶ 25-26 (footnote omitted). *See also, e.g.*, Indicated Suppliers Reply Brief at 6 (explaining that the Indicated Suppliers' proposal to use 11.5 to 15 hours for both the default MSOC and Penalty PAI/Penalty PAH "reasonably reflects supplier expectations regarding potential emergency events and the costs associated therewith" and "therefore addresses the market power concerns raised by the Commission in its March 18, 2021 order").

[111] *See, e.g.*, *PPL Wallingford*, 419 F.3d at 1198; *NorAm*, 148 F.3d at 1165.

[112] *See, e.g.*, *Fox*, 556 U.S. at 515; *West Deptford*, 766 F.3d at 20.

[113] September 2 Order, 176 FERC ¶ 61,137 at P 71 (citing March 18 Order, 174 FERC ¶ 61,212 at PP 65-66).

[114] *See, e.g., State Farm*, 463 U.S. at 43 (holding that an "agency must examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made'); *Alcoa Inc. v. FERC*, 564 F.3d 1342, 1347 (D.C. Cir. 2009) (same).

[115] March 18 Order, 174 FERC ¶ 61,212 at P 65 (footnote omitted). *See also* P3/EPSA Reply Brief at 3 (explaining that the March 18 Order "simply found that one component of the Capacity Performance ("CP") market design was flawed, that of the default MSOC based on the current value of the PAIs").

Penalty PAI and Expected PAI in the default Capacity Performance market seller offer cap calculation and the appropriate method for setting each value, including for updating one or both over time."[116] The Indicated Suppliers' proposal to lower the expected PAI used in the default MSOC would therefore have addressed the Commission's concerns in this respect. In addition, and as noted in the CP Initial Order, a "High ACR Resource" is "a resource whose avoidable costs exceed the amount that it can earn in Performance Bonus Payments . . . as an energy-only resource . . . ."[117] As a result, the default MSOC of Net CONE x B is only "inappropriate" when the Penalty Rate (and corresponding Bonus Payments) have not been adjusted based on an updated PAI/PAH so as to properly reflect the risk and opportunity cost associated with a capacity commitment. Rehearing is thus required because the September 2 Order departs, without explanation, from the Commission's prior findings and is based on erroneous conceptions of what the Commission found in the March 18 Order.

C. The September 2 Order Fails to Reconcile the Revised MSOC with the RPM Capacity Performance Structure

As discussed above, the September 2 Order ignores numerous arguments and concerns raised by the Indicated Parties and others. Notably, this failure extends to arguments regarding the need for the Commission to adopt an MSOC that is consistent with PJM's Capacity Performance construct. As the Indicated Suppliers Initial Brief explained:

> The Capacity Performance construct is premised on the understanding that "capacity must carry with it meaningful performance obligations, and corresponding incentives and penalties, to ensure that those resources actually deliver when needed." As the Commission recognized, "[w]ithout more stringent penalties, PJM has shown there is little incentive for a seller to make capital improvements, or increase its operating maintenance for the

116 March 18 Order, 174 FERC ¶ 61,212 at P 72.

117 CP Initial Order, 151 FERC ¶ 61,208 at P 339.

> purpose of enhancing the availability of its unit during emergency conditions." As Dr. Shanker further explains, the rationale underlying the Capacity Performance penalty structure is that "if a unit cannot be available for the estimated need, then it should be at jeopardy of losing its capacity payment and having to pay for replacement capacity," where, "[l]ogically, these replacement costs should be recovered over the expected hours of nonperformance." . . . This rationale, in turn, resulted in the MSOC being set at Net CONE times B, "which represents the amount of revenue at which a resource is indifferent between being an energy-only or capacity resource." Using different PAI values for the MSOC and Non-Performance Charge Rate calculations would therefore effectively negate the intent of the MSOC to represent the opportunity cost associated with assuming a capacity obligation.[118]

As a result, the Indicated Suppliers further explained that "in the event that the Expected PAI is indeed reduced below the 30 PAH under PJM's current rules, the penalty rate must be increased proportionately in order to ensure that suppliers continue to take the steps necessary to ensure that they are available when needed."[119] Similarly, the P3/EPSA Reply Brief emphasized the need for the default MSOC to reflect opportunity costs, and for the Penalty PAI to be the same as the PAI used to calculate the default MSOC.[120]

Just as the September 2 Order ignored so many of the other arguments raised by the Indicated Parties, the Commission brushed aside the Indicated Parties' concerns without any discussion and adopted an MSOC at odds with the Capacity Performance construct.[121] As discussed in Section III.A, suppliers will be subject to MSOCs that are effectively calculated assuming PAI/PAH of zero or close to zero, while the Penalty Rate is still based on the assumption

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118 Indicated Suppliers Initial Brief at 14-15 (footnotes omitted).

119 *Id.* at 15.

120 *See* P3/EPSA Reply Brief at 5-8.

121 *See, e.g.*, *PPL Wallingford*, 419 F.3d at 1198; *NorAm*, 148 F.3d at 1165.

that there will be 30 PAH/360 PAI. Nowhere in the September 2 Order did the Commission provide a rationale for this disconnect, rendering the order "illogical on its own terms . . . ."[122]

At the same time, the September 2 Order also fails to explain how a Penalty Rate that is based on a Penalty PAI that the Commission has expressly found to be too high[123] will provide the performance incentives that were supposedly the bedrock of the Capacity Performance structure. The CP Rehearing Order found that "[a] fundamental principle underlying PJM's Non-Performance Charge is that a non-performing capacity resource should be penalized at a rate that approximates the expected full costs of procuring replacement capacity, because a Capacity Performance Resource that does not perform during emergencies 'is tantamount, from the perspective of system loads, to never having obtained the capacity in the first place.'"[124] The Commission therefore held that the Penalty Rate should be based on Net CONE divided by the number of expected PAI, because "replacement capacity must be priced at an approximation of the cost of procuring either new capacity or other existing capacity capable of performing in place of the nonperforming resource"[125] and "a higher penalty based on Net CONE helps to ensure that resources will perform."[126] But keeping the Penalty PAI at 360 PAI/30 PAH, when the expected PAI is in fact much lower, will mean that a supplier will know that it is unlikely to ever be at risk of incurring anywhere near the full cost of procuring replacement capacity. Nonetheless, the

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122 *GameFly*, 704 F.3d at 148 (citation omitted).

123 *See* March 18 Order, 174 FERC ¶ 61,212 at P 65 (finding that "360 PAI exceeds market participants' reasonable, actual expectations of the number of PAI the system will experience in a given year" (footnote omitted)).

124 CP Rehearing Order, 155 FERC ¶ 61,157 at P 66 (footnote omitted).

125 *Id.* at P 67.

126 *Id.* at P 69.

September 2 Order failed to make any attempt to reconcile the Commission's refusal to modify the Penalty PAI with its determinations in the CP Orders.[127]

In short, under the September 2 Order, the Penalty Rate is either too high because it imposes risks and opportunity costs that suppliers cannot recover in their offers, or too low because it is based on the 360 PAI that the March 18 Order expressly found "exceeds market participants' reasonable, actual expectations of the number of PAI the system will experience in a given year."[128] Rehearing is therefore required because the September 2 Order "entirely failed to consider an important aspect of the problem"[129] and failed to "consider[] the relevant factors and articulate[] a rational connection between the facts found and the choice made."[130]

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[127] *See, e.g., Good Samaritan*, 858 F.3d at 629 (explaining that "[o]ne of the bases for finding an agency decision arbitrary and capricious is a deviation from its own prior precedents without sufficient explanation or reasoning" (citation omitted)); *West Deptford*, 766 F.3d at 20 (emphasizing that "[i]t is textbook administrative law that an agency must 'provide[] a reasoned explanation for departing from precedent or treating similar situations differently'" (citation omitted)); *Williams*, 475 F.3d at 322 (vacating Commission orders because the Commission "neither explained its action as consistent with precedent nor justified it as a reasoned and permissible shift in policy").

[128] March 18 Order, 174 FERC ¶ 61,212 at P 65 (footnote omitted). At the same time, while the default gross ACRs used to calculate the default MSOC assume a PAI/PAH of zero, Dr. Shanker explained that it would not be appropriate to use a corresponding assumption for purposes of setting the Penalty Rate, and that:

> at *very low or zero estimated PAI or at very high estimated PAH, the right conclusion may be to select another paradigm*. At zero or near zero PAI, the penalty rate approaches infinity, while the system as a whole is deemed to be almost riskless in terms of performance events. That results in a resource having an inordinately high penalty exposure, while being allowed only to submit offers based on its net ACR (without any risk premium beyond the [Capacity Performance] quantifiable risk as approved by the IMM to account for the penalty exposure).

Shanker Initial Affidavit at ¶ 33 (emphasis in original).

[129] *State Farm*, 463 U.S. at 43.

[130] *Baltimore Gas*, 462 U.S. at 105 (citations omitted). *See also, e.g., Allentown*, 522 U.S. at 374 (the process by which an agency arrives at a particular "result must be logical and rational").

IV.

CONCLUSION

WHEREFORE, for the foregoing reasons, the Indicated Parties respectfully request that the Commission grant rehearing of the September 2 Order as requested herein.

Respectfully submitted,

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Dated: October 4, 2021

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document on each person designated on the official service lists compiled by the Secretary of the Federal Energy Regulatory Commission in these proceedings.

Dated at Washington, D.C., this 4th day of October, 2021.

/s/ Neil L. Levy
Neil L. Levy