UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

PJM Power Providers Group	
v.	Docket No. EL11-20-000
PJM Interconnection, L.L.C.	
PJM Interconnection, L.L.C.	Docket No. ER11-2875-000
	(not consolidated)

**NEW JERSEY RATE COUNSEL'S
PROTEST OPPOSING P3 COMPLAINT AND
PJM SECTION 205 FILING**

Pursuant to Rule 211 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.211, New Jersey Rate Counsel ("NJ Rate Counsel"), an intervenor in the above-captioned dockets,[1] protests (1) the Complaint and Request for Clarification Requesting Fast Track Processing filed by the PJM Power Providers Group ("P3") in Docket No. EL11-20-000 ("Complaint"), and (2) the filing submitted by PJM Interconnection, L.L.C. ("PJM") pursuant to Section 205 of the Federal Power Act ("FPA"), 16 U.S.C. § 824d, in Docket No. ER11-2875-000 ("PJM Section 205 Filing").

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1 NJ Rate Counsel moved for leave to intervene in Docket No. EL11-20-000 on February 4, 2011. Motion for Leave to Intervene and Request for Establishment of Response Date (Feb. 4, 2011), eLibrary No. 20110204-5148. NJ Rate Counsel moved for leave to intervene in Docket No. ER11-2875-000 on March 3, 2011. Motion to Intervene of New Jersey Division of Rate Counsel (doc-less) (Mar. 3, 2011), eLibrary No. 20110303-5027.

I. EXECUTIVE SUMMARY

This case presents, for the third time in less than five years, the question of how to meld state-mandated resource-planning and investment decisions with PJM's residual capacity market pricing mechanism. In 2006, the Commission expressly addressed and resolved that question, approving as just and reasonable the contested settlement establishing the "Reliability Pricing Model" ("RPM")—and specifically approving RPM's Minimum Offer Price Rule ("MOPR"). That settlement included a carefully-negotiated MOPR exemption for resources that are developed in response to certain state regulatory or legislative mandates. In 2009, efforts to revamp the MOPR were rejected in the face of strong support for its terms from both PJM and certain of the generating interests that here seek a contrary result. We submit that the existing exemption already strikes the right balance between ensuring the integrity of RPM and accommodating state resource-planning and procurement initiatives. Neither P3 nor PJM has demonstrated that the existing exemption provisions have become unjust and unreasonable simply because certain states, in conformity with those provisions, have taken steps to secure additional in-state generating resources to address resource mix and reliability needs.[2] We urge the Commission to reject P3's request to establish rules that would thwart states' legitimate policy initiatives to secure additional generation supplies

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[2] As discussed below, P3 barely acknowledge the exemption's existence, let alone demonstrate that it has become unreasonable. P3 nonetheless would sweep it away along with virtually all other aspects of the "carefully balanced" MOPR. *See* Reply Comments of PJM Interconnection, L.L.C. in Support of Settlement at 30, *PJM Interconnection LLC*, Docket Nos. ER05-1410-000, *et al.* (Oct. 30, 2006), eLibrary No. 20061030-5098. PJM—which, unlike P3, can modify the provision through a Section 205 filing, *i.e.,* without carrying a Section 206 burden to show that it has become unreasonable—does not propose to jettison the exemption.

unless those initiatives would have no impact on RPM prices. P3's position is akin to allowing states to build roads only if they hold airlines harmless against lost profits.

P3 seek nothing less than a fundamental shift in RPM's role in the overall market design. While they avoid saying it, the import of their position is that RPM—which was designed to be PJM's *residual* capacity market—should be the *only* mechanism by which capacity is procured and compensated. Denials aside, P3's rules would frustrate any state resource-planning and procurement effort that selects resources different than those picked by RPM on the basis of the only two factors that RPM considers: (1) price and (2) overall resource adequacy in a given local deliverability area ("LDA") (as measured by total megawatts, with no concern as to fuel or technology mix). If the complainants are successful here, then legitimate state interests—including, but not limited to, achieving preferred mixes of fuel use and generation technologies, reducing a state's dependence on energy imported from other regions, limiting the risk associated with depending on at-risk coal-powered electricity, and satisfying renewable portfolio standards—would be dashed.

The reason is that, under P3's construct, states seeking to achieve those ends would have to pay twice for capacity: once to procure the resources that serve those state policy goals and again to procure the resources that are selected by RPM on the basis solely of price and location.[3] Although the Commission has sought to deter uneconomic

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[3] Similarly, P3 seek to eliminate any realistic means for long-term bilateral contracting for capacity, unless those resources happen to be economic as determined by RPM in terms of price and location. Under P3's approach, entities may contract for capacity bilaterally but may not use that capacity to satisfy their RPM obligations, and so must pay for more capacity than they actually need.

entry by market participants seeking to suppress wholesale capacity market prices, it has not previously suggested that the deterrence rules must be so broad and unyielding as to frustrate measures duly enacted by state legislatures and governors to achieve legitimate state policies. The Commission should not do so now—especially not in PJM, which already has an agreed-upon and Commission-approved mechanism for reconciling state objectives and residual capacity markets.

More generally, the Commission should resist calls to overhaul dramatically the existing MOPR and its exceptions. It particularly should not do so on the "hurry up" basis posed here. None of the proponents seeking to change these provisions has identified any changed circumstance that renders the existing, approved rules unjust and unreasonable, let alone any urgent need to change the rules in a break-neck fashion that bypasses PJM's stakeholder processes,[4] Commission regulations,[5] and the opportunity for

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[4] As explained below, P3's Complaint truncated a nascent stakeholder process initiated in January 2011 to consider potential MOPR reforms. Since P3 filed their complaint, nothing further has occurred in that process. Instead, PJM held one conference call to inform stakeholders about the Section 205 filing that it intended to make as its "answer" to the P3 Complaint. PJM convened the call on February 9, and submitted its filing just two days later. Apart from that one phone call—during which technical difficulties constrained some participants' ability to ask questions—stakeholders have had no opportunity to engage PJM or its market monitor regarding these issues. Nor has PJM or its market monitor sought to engage PJM's stakeholders in a meaningful discussion about the issues that PJM raises in its Section 205 filing. There has been no showing that exigent circumstances are present, such as would justify end-running the stakeholder process.

[5] Rule 206(b)(9) of the Commission's regulations, 18 C.F.R. § 385.206(b)(9), requires complainants to state whether dispute resolution procedures were used or why they were not used, whether alternative dispute resolution ("ADR") under the Commission's supervision could resolve the complaint, and what ADR procedures could be used. These mandatory regulations exist to promote informal dispute resolution and conservation of the Commission's and the parties' resources. P3 effectively flout these requirements. Although P3 state that they have "attempted in good faith to resolve these matters," Complaint at 74, their efforts apparently were limited to (i) attempting to persuade the New Jersey legislature not to enact its legislation, and (ii) seeking, during a "long" but otherwise undefined period, unspecified "reforms … to improve and strengthen the [MOPR]." *Id.* The first cited "attempt[]" to "resolve these matters" was no such thing, as it focused on whether New Jersey would act, not on any of the rate-related matters raised in P3's Complaint. The second assertion is far too general to permit any conclusion that P3 engaged in efforts to

due deliberation of complex issues. That is particularly true given that West Deptford Energy, LLC ("WDE"), which is the entity most likely to seek to participate in the May 2011 Base Residual Auction ("BRA") pursuant to the challenged New Jersey legislation, already has filed with the Commission to justify its proposed bid,[6] which should substantially mitigate any perceived need to rush to approve ill-considered tariff changes.

Accordingly, and as explained below, the Commission should deny the P3 Complaint, reject PJM's Section 205 filing, and direct PJM to continue the stakeholder processes that had been initiated to address the issues raised by P3's Complaint and related matters. These related issues include important questions about the proper treatment of resources other than combustion turbines and combined-cycle units, including energy-efficiency and demand-response resources.

Alternatively, if the Commission does not deny the complaint and reject PJM's filing, then it should consolidate them, establish an evidentiary hearing to address the issues raised therein, and hold the hearing in abeyance pending settlement-judge procedures. To the extent that the Commission reaches the merits of the P3 and PJM filings, it should:

1. Deny the P3 Complaint's proposal to eliminate the existing, Commission-approved MOPR exemption for state-mandated resource procurement;
2. Either retain the existing, self-executing state exception or conditionally accept, with modifications, PJM's proposal to retain the exception but remove it from PJM's tariff-administration functions;

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resolve the matters raised by P3's Complaint before filing it.

6 Request of West Deptford Energy, LLC for Commission Determination that its Unit-Specific Minimum Capacity Sell Offer is Justified Pursuant to PJM's Minimum Offer Price Rule, and Requests For Protection of Confidential Bid-Related Information and Expedited Treatment, *West Deptford Energy, LLC*, Docket No. ER11-2936-000 (Feb. 22, 2011), eLibrary No. 20110222-5187 ("WDE Filing").

3. Reject P3 and PJM's attempted paradigm shift, which would (a) turn PJM's residual capacity market into the primary means of securing new generation in PJM, and (b) transform the MOPR from a narrowly-crafted, anti-price-manipulation provision into an administrative support propping up RPM prices despite new supplies procured for legitimate, reliability-related reasons and then bid at low prices appropriately reflecting their procurement outside of RPM;
4. Deny the P3 Complaint's proposal to replace any bid below 100 percent of the administratively-determined Net Cost of New Entry ("Net CONE") for a combustion turbine ("CT") or a combined-cycle unit ("CC") with a bid equal to Net CONE for that asset class, reject PJM's proposal to replace CT and CC bids below 90 percent of Net CONE for those classes with bids equal to the 90 percent level, and instead maintain the existing mitigation approach (which employs lower percentages);[7]
5. Provide more flexibility for project-specific justifications of offers;
6. Retain but revise the existing impact test and net short requirements; and
7. Reject proposals to extend the duration of the mitigation applied to so-called "uneconomic" offers that do not represent anti-competitive price-suppression efforts.

II. PROTESTS

As complainants under FPA Section 206, P3 bear the burden of demonstrating, first, that PJM's MOPR—which the Commission previously approved as just and reasonable—has become unjust and unreasonable and, second, that P3's proposed alternatives are just and reasonable. As explained below, P3 have met neither burden. PJM, as the proponent of a rate change under FPA Section 205, need only show that its new proposal is just and reasonable. Nonetheless, as the proponent of changes to rates that were painstakingly negotiated and agreed to by most of PJM's stakeholders—and that the Commission approved as just and reasonable over the objection of parties raising

[7] Alternatively, if the Commission does not maintain the existing conduct screen, it should adopt PJM's proposed 90 percent screen, which is more reasonable than P3's proposal.

the same claims that P3 now advance—PJM should at least be required to provide a satisfactory explanation for why it believes that its proposed changes are needed. PJM also should be required to consult meaningfully with its stakeholders before proposing a far-reaching overhaul of the MOPR. As explained below, PJM has not shown that it complied with the applicable stakeholder-consultation requirements or that the changes it has proposed are just and reasonable.

A. The Commission should reject the view that it is always illegitimate for capacity procurement outside of RPM to affect RPM prices.

RPM is—and was designed to be—a residual, administrative mechanism (designed to mimic a market to the extent possible) for the procurement of capacity not obtained by other means. Its centerpiece is named the "Base *Residual* Auction." Contrary to the philosophical underpinnings of P3's Complaint, RPM never was intended to operate as the only realistic means by which new generation could be procured and existing generation retained in PJM. Nor were RPM prices intended to be held sacrosanct, and propped up artificially, despite actions taken outside RPM by market participants pursuing legitimate business purposes or state governments pursuing legitimate state policy interests. To the contrary, an important corollary to RPM's role as a residual market is that RPM prices are *supposed* to be affected by supply and demand changes resulting from decisions made outside of that market. P3's Complaint turns this construct on its head.

As the Commission explained in ruling on the PJM filing that preceded the RPM settlement:

> *We agree with protesters that RPM is an administrative mechanism.* However, the current capacity construct is also

> an administrative mechanism, so the administrative feature can have no bearing on the choice between the current capacity construct and the capacity construct under the RPM proposal.… [A] forward procurement auction is necessary because the market alone under the existing market rules and market conditions is not eliciting the amount of resources needed to meet reliability needs. *Thus*, we conclude that, *after LSEs [Load-Serving Entities] have had an opportunity to procure capacity on their own*, it is reasonable for PJM to procure capacity in an open auction at a time when further delay in procurement could jeopardize reliability. *This*, *however*, *should be a last resort.*

PJM Interconnection, L.L.C., 115 FERC ¶ 61,079, P 71 (2006) (emphasis added). The Commission continued, noting that the purpose of RPM was to "provide price signals and price stability that will enable LSEs to purchase capacity, and generators to offer to provide capacity, in a more informed and efficient fashion." *Id.* P 169. The point was not to require all procurement to occur through RPM or to insulate RPM prices against changes in supply and demand resulting from procurement decisions occurring outside of it. Rather, the Commission held, "LSEs will still make their own business decisions about how much capacity to build or procure in long-term contracts and at what cost, and how much to obtain through PJM's auction." *Id.*

PJM itself has acknowledged the residual nature of the RPM capacity procurement mechanism. During the technical conference convened by the New Jersey Board of Public Utilities to consider the sufficiency of the capacity procured through

RPM to meet New Jersey's needs,[8] Michael J. Kormos, PJM's Senior Vice President, Reliability Services, recapped:

> I think you've heard RPM is working well. RPM is not working at all. I would offer the truth is probably someplace in between those two.
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> We are committed to continue working on RPM. Ultimately, there may be a replacement. I don't know that answer whether we will get there or not. I would offer that RPM was never meant to be the end-all and be-all for the capacity markets. We always envisioned to be a piece of it. We envisioned that there would be longer term contracts. There are ways to self supply. There are ways to literally pull yourself out of RPM. Those options were always, always built in there.[9]

PJM's post-conference comments expanded on the limited nature of RPM, explaining that "RPM was never intended to be the sole source of revenue through which resource development decisions would be made, nor was it intended to be the only mechanism through which new capacity resources could be financed or constructed."[10] Instead, RPM was designed to "augment long-term contracting" (*id.* at 5):

> RPM was never intended to be the sole market mechanism to complement the Energy and Ancillary Service Markets by which investment in new capacity resources would be made. In fact, the name of the main procurement auction held three years in advance of the delivery year, "Base

8 *See* Notice of Technical Conference, In the Matter of the New Jersey Board of Public Utilities Review of the State's Electric Power and Capacity Needs, Docket No. EO09110920 (N.J.B.P.U. June 14, 2010), http://www.state.nj.us/bpu/pdf/announcements/20100624.pdf ("Notice of Technical Conference").

9 Transcript of the June 24, 2010 New Jersey Capacity Issues Technical Conference at 196-197, In the Matter of the New Jersey Board of Public Utilities Review of the State's Electric Power and Capacity Needs, Docket No. E009110920 (June 29, 2010).

10 Comments of PJM Interconnection, LLC at 2, In the Matter of the New Jersey Board of Public Utilities Review of the State's Electric Power and Capacity Needs, Docket No. EO09110920 (July 6, 2010), http://www.state.nj.us/bpu/pdf/energy/PJM_comments.pdf ("PJM BPU Comments").

> Residual Auction," was selected specifically to convey the message that RPM does not foreclose long-term resource procurements outside of RPM auctions. Load Serving Entities (LSEs) or other entities with capacity obligations and developers of new capacity resources are free to enter into contracts at mutually agreeable prices and terms that would help the LSEs and other entities meet their capacity obligations while providing revenue certainty for the resource developer. The resulting capacity addition would then be entered into RPM auction, but the actual financial settlement between the LSE and resource developer would be governed by the contract terms. This self-supply of a load's capacity obligation in RPM results in load and the resource developer being indifferent to the RPM clearing price.

Id. at 6-7. This description of RPM's role and its relationship to bilateral contracting is markedly at odds with the P3 Complaint, the premise of which is that it is unjustly discriminatory for buyers to seek out and to contract with new resources outside of RPM.

PJM's BPU comments are also at odds with the tack that PJM has taken in its Section 205 filing in this case, which now downplays the residual nature of RPM's capacity-procurement function:

> [RPM] is the set of rules by which PJM obtains commitments of capacity to meet the PJM Region's reliability needs through auctions conducted three years before the year for which the capacity is needed (i.e., the Delivery Year). The annual RPM Base Residual Auctions therefore provide both certainty of supply three years into the future and a forward pricing signal and revenue stream to support and incent investments in capacity resources (of all types) where needed on the system to meet reliability goals.

PJM Section 205 Filing at 1. PJM's parenthetical phrase, "of all types," is worth noting, because it highlights a matter that is central to this case. While states have obvious, significant, and legitimate interests in preferring resources with particular characteristics, RPM is not designed to achieve a particular mix of resources—let alone an optimal one—

based on either fuel or technology type. Instead, RPM looks only at price and presence within a given LDA.

Both the P3 Complaint and the PJM Section 205 Filing effectively ignore the distinction between legitimate actions that have an incidental effect on RPM prices and illegitimate actions taken to suppress such prices. In this case, as discussed below, the State of New Jersey enacted energy legislation for public purposes through its duly-elected legislators and governor, as the State has previously done for renewable energy resources. In doing so, New Jersey was acting neither as a "market participant" nor as a proxy for one. It was legislating pursuant to its traditional police power to safeguard the health and welfare of New Jersey's citizens—in this case, by seeking to ensure not only that New Jersey has a sufficient number of total megawatts of capacity but that the mix and quality of the resources serves the State's capacity needs.

1. New Jersey's legislation was enacted for legitimate public purposes.

P3 go to great lengths to attempt to characterize the New Jersey legislation as a scheme to suppress capacity market prices.[11] But that characterization is contradicted by the text of the law itself and by economic logic.

[11] In late January 2011, before the bill was signed into law, RESTRUCTURING TODAY quoted Commissioner Moeller as describing the bill as "an attempt by a state to disrupt a regional market" and predicted that the New Jersey program would "crater the capacity market." Moeller shares thoughts on PJM capacity market, shale gas, Restructuring Today, Jan. 28, 2011, http://www.restructuringtoday.com/public/1217.cfm. Notwithstanding these remarks, we trust that the Commission will not have prejudged either the reasons why New Jersey enacted its legislation or the effect that the legislation may have on RPM prices. In reality, whether the legislation has *any* effect on RPM prices depends on what resources may be selected through the New Jersey program and whether those resources are economic—which is not yet known. If a resource is economic, then, by definition, it does not matter whether it bids at cost or below its cost, as it would clear either way. We ask that the Commission base its decisions about why New Jersey acted on the text of the legislation itself and that it judge the import of New Jersey's actions on the basis of

P3 ask the Commission to draw inferences about the law's purposes based on un-enacted drafts of the legislation and testimony of witnesses supporting the bill. *See* Complaint at 60-63. But the law itself—signed by the State's Governor following passage by votes of 25-10 in New Jersey's Senate and 57-15 in its House—states the reasons why it was enacted. The statute states the New Jersey Legislature's finding that:

> While [RPM] has resulted in significant capacity additions in the form of new demand response resources, new energy efficiency resources, reversals of generation unit retirements, upgrades of existing generating units and certain new peaking facilities available to the region and the State, [it] has not resulted in large additions of peaking facilities or any additions of intermediate or base load resources available to the region and the State.

P. L. 2011, c. 9, sec. 1b (N.J. 2011) (footnotes omitted). The Legislature further determined that, "[a]s a result of a lack of new, efficient electric generating facilities, New Jersey has become more reliant on coal-fired power plants." *Id.* sec. 1f. The Legislature found that increased reliance to be problematic because, according to the PJM Independent Market Monitor, "there are over 11,000 megawatts … of coal-fired units at risk of retirement due to their inability to cover their avoided costs." *Id.* sec. 1g.

Additionally, the Legislature found that "New Jersey's in-State fleet of electric generation facilities is aging, with over 50 percent of these facilities being more than 30 years old and over 70 percent being more than 20 years old." *Id.* sec. 1h. Thus, the Legislature concluded that:

> Fostering and incentivizing the development of a limited program for new electric generation facilities will help

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the record developed in this case.

> ensure sufficient capacity to stabilize power prices to assist the State's economic development and create opportunities for employment in the energy sector while helping to reduce the cost and volatility of electricity prices in New Jersey.

Id. sec. 1i. It further concluded that "the construction of new, efficient generation must be fostered by State policy that ensures sufficient generation is available to the region, and thus the users in the State in a timely and orderly manner." *Id.* sec. 1d.

In short, in the months following the New Jersey BPU's proceeding concerning capacity issues facing the State (which is reviewed below), the New Jersey Legislature found that, while RPM might eventually procure new base load and intermediate generation facilities to meet the State's needs, it was contrary to New Jersey's interests to wait for RPM to induce such entry. The Legislature concluded that any RPM-induced entry might not occur until after existing coal plants that serve New Jersey are retired due to economics or anticipated regulatory changes and that the state preferred a more timely and orderly transition. In the face of these facts, New Jersey concluded that it was in the State's interest to procure new baseload and intermediate generation resources outside of RPM with competitively-bid long-term contracts.[12]

As the Supreme Court has explained, a statute's text is the authoritative statement of a Legislature's intent. *Exxon Mobil Corp. v. Allapattah Servs., Inc.*, 545 U.S. 546, 568

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[12] New Jersey's program to secure up to 2,000 MW of new baseload and intermediate generation facilities with long-term contracts is no less of a market mechanism than RPM's auction using an administratively-determined demand curve. In response to the New Jersey program, prequalification pertaining to more than 34 units representing 6,400 MW of capacity have been submitted (including prequalifications submitted by some of the P3 complainants). N.J. gets proposals for more than 6,400 MW, Megawatt Daily, Feb. 24, 2011.

(2005) ("[T]he authoritative statement is the statutory text, not the legislative history or any other extrinsic material.") While the resources that are secured by means of the New Jersey pilot program can be expected to affect the supply conditions in RPM and thus to affect RPM clearing prices, and while proponents of the legislation assessed those impacts during the legislative process, there is no evidence that New Jersey's Legislature and Governor enacted and signed the law with the primary objective of suppressing capacity prices. P3 ignore what is in the law and rely instead on what is not there, characterizing the Legislature's decision to omit references to capacity prices from the bill's final text as a legislative whitewash designed to conceal the Legislature's real intentions in enacting the law. *See* Complaint at 60 ("Although most recent versions of the New Jersey Law have been scrubbed of most references to capacity price levels, earlier public drafts were less discreet."). To the contrary, the omission of such references demonstrates that the NJ Legislature did not base its passage of the new statute on capacity price-suppression grounds.[13] Instead, the Legislature passed the law for other reasons—those stated in the law itself. The Commission should therefore disregard P3's exhortations to ascribe to New Jersey improper motives that cannot be found in the legislative text.

Further, to the extent that other entities' allegations regarding New Jersey's motives are relevant, P3 and their allies effectively concede that the State was motivated

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[13] *See* 2A Norman J. Singer and J.D. Shambie Singer, Sutherland Statutory Construction § 48:4 (7th ed. 2007) ("[W]here the language under question was rejected by the legislature and thus not contained in the statute it provides an indication that the legislature did not want the issue considered.")

not by a naked desire to suppress market prices, but by a "belie[f] that insufficient new capacity has been constructed in that State"[14] and by a concomitant desire to enter into long-term contracts to procure additional capacity. The observation that New Jersey previously sought RPM reforms, which the Commission rejected, in order to spur the development of new electric generating capacity in the State should not brand New Jersey as a malefactor.[15] And it certainly does not support the inference that P3 and their allies would draw—that New Jersey is seeking now to exercise buyer market power to depress RPM prices. Unlike New Jersey, entities interested in depressing RPM prices would not have conducted a proceeding to determine whether existing supplies were adequate because they would not have cared one way or the other.

Both Commission precedent and the testimony of P3's own witness further undermine P3's claim that New Jersey's pilot program was enacted to suppress RPM prices, rather than to secure new resources that the State legitimately believed to be needed. As the Commission has found, states in multi-state RTOs like PJM are unlikely to subsidize new entry for price-suppression reasons because such states would bear all of the cost of subsidizing new entry, while reducing clearing prices in other states as well, thus putting themselves at a competitive disadvantage compared to neighboring states:

> [I]in a multi-state Regional Transmission Organization (RTO) like PJM and ISO New England, individual state support for new entry that happens to be uneconomic translates into subsidies for customers in other states—that is, the customers of one state pay for new capacity that is

[14] Comments of the Electric Power Generation Association at 4, Docket No. EL11-20-000 (Feb. 28, 2011), eLibrary No. 20110228-5157 ("EPGA Comments").

[15] Indeed, PJM itself acknowledges that RPM reform is needed. *See* PJM Section 205 Filing at 21-22.

> bid into a capacity market at a below-market price in order to guarantee it clears the market. This drives down the market-clearing price for all market participants including those in other states. An individual state is much less likely to do this in a multi-state RTO like PJM and ISO-New England than in a single state RTO like NYISO, given the localization of costs and dispersion of benefits in the case of a multistate RTO.

New York Indep. Sys. Operator, Inc., 124 FERC ¶ 61,301, P 37 (2008), *clarified*, 131 FERC ¶ 61,170 (2010).

P3 witness Roy J. Shanker makes a related point in explaining why individual market participants—even those that are net short of capacity—are unlikely to subsidize new entry for price-suppression reasons.[16] In his testimony supporting the P3 Complaint, witness Shanker was asked whether market participants who attempt to exercise buyer-side market power but who represent only a fraction of the market will sustain a competitive disadvantage. He answered:

> Yes. This occurs because the party exercising buyer-side market power—the party bidding into the market below cost—incurs the "extra" cost of the uneconomic new resource. It benefits from the price suppression, but it also has to incur the cost of building a new unit. Everyone else—all of the remaining participants who purchase capacity—get the same price suppression benefit without the expense of building the unit.

Id. at 13. He went on to explain why this competitive disadvantage makes such strategies unlikely:

> [I]f there is no state or other "partner" to protect the party seeking to exercise market power, the party engaging in

[16] Testimony of Roy J. Shanker, Ph.D., on Behalf of the PJM Power Providers Group, Exhibit 1 to Complaint ("Shanker Testimony").

> anti-competitive behavior will likely have an average price that is significantly higher than its competitors who serve the remaining load in the system (or locational delivery area). This occurs because while the party engaging in anti-competitive behavior buys some power at the suppressed prices, it also pays "market" for the additional uneconomic supply. Its competitors, on the other hand, only pay the suppressed market-clearing price.
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> Under a competitive regime where retail load may be served by multiple sellers, this type of behavior, even though profitable in the short term for the party exercising market power, cannot persist over the long term because, although the costs to the exerciser of market power decline, the party exercising market power would have higher average unit costs than its competitors because it is the only party that pays the price for the distortion. Ultimately this factor would cause the party exercising market power to lose market share to its competitors and, in turn, eventually lose the benefits of exercising market power in the first place. Thus, while there may be a short-term incentive for this behavior when there is competition for sales, it is not sustainable in the long term, at least not without state help to socialize the cost of the exercise of market power across all of the beneficiaries.

Shanker Testimony at 13-14. As explained in the attached Affidavit of James F. Wilson, this is "especially true" for the upcoming auction because transmission enhancements and lower electric demand reduce the likelihood that prices in LDAs will separate.[17] Thus, "most PJM load-serving entities will be buying capacity in a large, multi-state market area, and the benefits of any price suppression they might be able to cause would be shared with many other buyers, making it unlikely to be profitable." *Id.*

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[17] Affidavit of James F. Wilson in Support of Protest of New Jersey Rate Counsel, P 30 ("Wilson Aff.").

Because of these dynamics, witness Shanker believes that uneconomic entry for price-suppression purposes depends on States playing a nefarious role to render such behavior profitable (Shanker Testimony at 13):

> The state can impose non-bypassable charges or other discriminatory practices that assure recovery for the party bidding below cost, to permit it to make up the costs it incurs to build the plant. The party exercising market power bids below market but receives a discriminatory payment or subsidy from the state. As discussed later, recognizing this factor becomes a crucial element in the appropriate design of a mitigation strategy for short-term resources.

One obvious flaw in witness Shanker's depiction of the roles played by states is that, as the Commission recognized, the same "competitive disadvantage" dynamic occurs among states in a multi-state RTO. 124 FERC ¶ 61,301, P 37. Witness Shanker never explains why it would be economically rational for a state, motivated solely by RPM price reduction, to disadvantage itself vis-à-vis neighboring states by shouldering all of the above-market new-entry cost while other states reap much of the resulting RPM price reduction.

Reduced to its essence, P3's position is that they know better than New Jersey's elected representatives both (1) *why* they enacted P. L. 2011, c. 9, and (2) *whether* doing so was in New Jersey's long-term interests.[18] The Commission should reject both

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[18] *See* Shanker Testimony at 10 ("It has become increasingly clear to me that certain states and market participants operate under the belief that price discrimination is a legitimate and desirable goal to be pursued in a capacity market design.… [W]hile artificially suppressed prices may appear attractive to consumers in the short run, they cannot be sustained, and actually result in higher costs in the long run.").

propositions.[19] Acting in the months following the NJ BPU's proceeding aimed at determining the State's situation with respect to needed capacity resources, the New Jersey Legislature enacted legislation which explains on its face that the State is responding to what it perceives to be a potential shortfall in baseload and intermediate generation in New Jersey. As explained below, the State's action falls well within the confines of the MOPR exception contained in PJM's tariff—an exception that was painstakingly negotiated and carefully crafted to exclude from price mitigation resources that are procured in response to such state regulatory or legislative mandates.

2. New Jersey's pilot program fits the MOPR exception currently contained in PJM's tariff.

As noted above, RPM is a residual, administrative capacity-procurement mechanism, and the carefully-negotiated limitations on RPM's MOPR were designed to reflect the limited nature of RPM itself. One such limitation was the MOPR exception for resources developed in response to certain state-mandated procurement programs:

> Notwithstanding the foregoing, the Net Asset Class Cost of New Entry shall be zero for: … (iv) any Planned Generation Capacity Resource being developed in response to a state regulatory or legislative mandate to resolve a projected capacity shortfall in the Delivery Year affecting that state, as determined pursuant to a state evidentiary proceeding that includes due notice, PJM participation, and an opportunity to be heard.

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19 Indeed, if P3's paternalistic and patronizing view—that consumers cannot accurately perceive what is in their own long-term economic self-interest—were true, it would undermine the foundation of the Commission's attempt to rely on markets to establish just and reasonable rates.

PJM Tariff, Attachment DD § 5.14(h)(1). This exception, which P3 all but ignore,[20] is important for at least two reasons: First, it shows that the RPM design anticipated—and was intended to accommodate—state resource-planning efforts. Second, it shows that when such efforts are undertaken, resulting resources are expected to act as price-takers in ensuing RPM auctions, notwithstanding that such offers will affect the resulting RPM auction price. Indeed, the purpose of the exception was to allow offers to sell at prices lower than otherwise would have been required by the MOPR and to allow such offers to affect the RPM clearing price. If that were not the case, it would have been unnecessary to include the MOPR exception in the RPM rate design.

As explained in the attached Affidavit of Robert M. Fagan, this state-level exception was particularly important to New Jersey because the structure of the state's retail electricity market effectively precludes New Jersey's load-serving entities from self-supplying capacity resources in RPM.[21] As Mr. Fagan explains (P 4), a large portion of New Jersey's retail load is served by means of Basic Generation Service ("BGS") auctions, through which the state's electric distribution companies—which have divested their own generation—acquire resources to serve load not served by third party suppliers or competitive retailers. Because the BGS procurement auction has not yet been held for the 2014-15 PJM planning year, Mr. Fagan explains, "the entities that would supply this load and take on the load serving entity obligation in the PJM marketplace for this period

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[20] *See* Shanker Testimony at 4 (complaining that "[t]here are too many exceptions" to the MOPR, but focusing on exceptions other than the state-mandated procurement exception).

[21] Affidavit of Robert M. Fagan on Behalf of the New Jersey Rate Counsel ("Fagan Aff.").

are unknown." *Id.* P 5. Thus, when PJM conducts its BRA for 2014-15, the providers with an obligation to serve most of New Jersey's load will not yet be known, and there will be "no private party that could enter into a long-term capacity contract without incurring an unacceptable level of risk." *Id.*

The New Jersey legislation—and the resources that may be developed as a result of it—fall squarely within the existing MOPR exception. The text of the law leaves no doubt that resources participating in the pilot program will have been developed "in response to a state regulatory or legislative mandate to resolve a projected capacity shortfall in the Delivery Year affecting that state."[22] As explained above, the New Jersey Legislature concluded that RPM has not induced "large additions of peaking facilities or any additions of intermediate or base load resources available to the region and the State," P. L. 2011, c. 9, sec. 1b; that New Jersey had thus become "more reliant on coal-fired power plants," which are at risk of retirement, *id.* secs. 1f and 1g; and that New Jersey's generation fleet was aging, with over 50 percent of these facilities being more than 30 years old, *id.* sec. 1h. The Legislature therefore decided that it was important to "[f]oster[] and incentiviz[e] the development of a limited program for new electric generation facilities" to ensure that "sufficient generation" will be made available to New Jersey electricity consumers "in a timely and orderly manner." *Id.* secs. 1i and 1d.

As Mr. Fagan explains, the Legislature's findings were well founded. Mr. Fagan confirms that more than 25 percent of New Jersey's electric supplies come from imports

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22 PJM Tariff, Attachment DD § 5.14(h)(1).

from western PJM, including a substantial amount of coal-fired capacity that is at risk of retirement.[23] At the same time, recent increases in transmission export capability to New York put additional pressure on the availability of resources to meet New Jersey's needs. *Id.* P 11. Furthermore, in recent years, PJM has "repeatedly warned of eastern PJM reliability concerns that can only be alleviated by increasing generation resources" or transmission import capability into the region. *Id.* P 13. In its 2008 and 2009 New Jersey RTEP Overviews, PJM expressed concern that load growth, generation retirements, and a failure to develop new generation and transmission solutions in the region could impair reliability in the state. *Id.* PP 13-15. PJM amplified these concerns in evidentiary hearings before the New Jersey Board of Public Utilities regarding the Susquehanna-Roseland Line, a 145-mile, 500-kV transmission line and upgrade of an existing 230-kV line from Susquehanna, Pa., to Roseland, NJ. *Id.* P 18.

As the record of that proceeding revealed, PJM's 2007 RTEP showed 23 reliability criteria violations, which the 2008 RTEP and 2009 Retool Update confirmed would occur as early as 2012. *Id.* During a February 2010 hearing, PJM asserted that 2010 peak load forecasts remained almost identical to those in the 2009 forecast. *Id.* PJM further noted that, since 2003, almost 1,250 MW of generation had retired in the eastern Mid-Atlantic area of PJM and that 7,500 MW of the remaining generation in that area was more than 40 years old. *Id.* P 19. PJM further emphasized that more than 50 percent of the 5,211 MW of generation capacity that failed to clear for the 2011-12 period was located in the eastern Mid-Atlantic region, as was 28 percent of 6,346 MW that failed to

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[23] Fagan Aff. P 10.

clear for 2012-13. *Id.* The region has 1,130 MW of older coal units smaller than 200 MW, which can be expected to have difficulty justifying the investments necessary to continue operations with the implementation of carbon restrictions. *Id.*

In light of these considerations, the New Jersey Board of Public Utilities unanimously approved the Susquehanna-Roseland Line, *id.* P 21, but PSE&G has delayed the in-service date for the project by 2-3 years due to on-going environmental permit reviews, *id.* P 22. The delay further magnifies concerns regarding New Jersey's reliance on imports of out-of-state resources and the need for additional in-state generating resources. *Id.* P 23. Indeed, in a June 2010 letter to the New Jersey Department of Environmental Protection, PJM explained that, without the line, "'PJM will be developing specific operational procedures to … define, among other things, the circumstances under which service to customers in northern New Jersey will have to be curtailed to minimize the potential for broader service disruptions.'"[24]

The New Jersey Legislature's enactment of P. L. 2011, c. 9, also followed the conclusion of a New Jersey Board of Public Utilities evidentiary proceeding expressly convened to assess New Jersey's capacity needs. Like the proceeding regarding the Susquehanna-Roseland line, the Board's capacity-issues proceeding involved "due notice, PJM participation, and an opportunity to be heard."[25] On June 14, 2010, the Board issued a Notice of Technical Conference to be held on June 24, 2010.[26] The Technical

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[24] *Id.* P 23 (quoting June 17, 2010 letter from Steven Herling, PJM to Lou Cattuna, NJDEP).

[25] PJM Tariff, Attachment DD § 5.14(h)(1).

[26] Notice of Technical Conference.

Conference was convened to "seek information on the challenges raised during the 2010 BGS proceeding regarding additional electric generation and capacity needs of New Jersey." *Id.* Specifically, the Board indicated that it was "concerned with ensuring that sufficient generation exists to meet the electric power needs of New Jersey going forward." *Id.* The Board therefore directed its Staff to "develop a process to review the State's power and capacity needs in a separate proceeding, and to make the necessary arrangements to convene a technical conference that would include the participation of key stakeholders." *Id.*

PJM participated actively in the Technical Conference through two executives—Steve Herling, Vice President, Planning, and Mike Kormos, Senior Vice President, Reliability Services—who took part in each of the conference's three panel discussions, *id.*, and delivered a 19-slide powerpoint presentation addressing New Jersey's capacity issues.[27] PJM also submitted 21-page written comments following the Technical Conference.[28] As Mr. Fagan recounts, PJM reported that 1,121 MW of New Jersey generation had retired since 2002, with an additional 671 MW pending deactivation.[29] The New Jersey generation at risk of retirement includes a number of facilities retained by PJM for reliability reasons under reliability-must run contracts. *Id.* PP 34-39.

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[27] PJM, New Jersey Power Supply Load and Capacity Data, New Jersey Capacity Issues Technical Conference, Docket No. EO09110920 (Jun. 24, 2010) (available at http://www.state.nj.us/bpu/pdf/energy/HERLING%20AND%20KORMOS.pdf).

[28] PJM BPU Comments, *supra* n.10. The Board's proceedings in Docket No. EO09110920 thus constitute "a state evidentiary proceeding that includes due notice, PJM participation, and an opportunity to be heard," PJM Tariff, Attachment DD § 5.14(h)(1).

[29] Fagan Aff. P 32. The New Jersey DEP also testified, explaining that more than 4,630 MW of New Jersey's 7,800-MW "High Electric Demand Day" units would become subject to phase II NOx emission restrictions by 2015 or 2017, which could cause a substantial number of those facilities to retire. *Id.* P 31.

Given the role played by PJM in documenting the impending potential capacity shortage in New Jersey and the resulting reliability ramifications, PJM's "participation" and "opportunity to be heard" regarding the prospect of a capacity shortfall in New Jersey is beyond question. Nor can there be any dispute as to whether the record compiled in the New Jersey BPU evidentiary proceedings informed the enactment of P. L. 2011, c. 9, or whether PJM had an opportunity to be heard in the legislative process leading to the law's enactment. Hearings on the bill were held in both the Assembly Telecommunications and Utilities Committee and the Senate Environment and Energy Committee, where interested parties were allowed to testify in support or in opposition to the bill. In Assembly committees, "full discussion and consideration of bills and resolutions [are] made in public."[30] In the Senate, "[t]he public is permitted to attend meetings of any Senate committee," and "[c]itizens present who wish to be heard on a matter under consideration by the committee [are] afforded an opportunity to speak."[31] In fact, PJM's independent market monitor testified at the Assembly Telecommunications and Utilities Committee hearing,[32] and submitted a joint letter with PJM to the New Jersey Board of Public Utilities stating their views with respect to the legislation.[33]

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[30] Rules of the General Assembly of the State of New Jersey sec. 10:10, Sept. 30, 2010.

[31] Rules of the Senate of the State of New Jersey sec. 22:2a, Jan. 12, 2010.

[32] A copy of Dr. Bowring's testimony is available at http://www.monitoringanalytics.com/reports/Reports/2010/Bowring_NJ_Assembly_3442_Testimony_20121216.pdf.

[33] Letter from Andrew L. Ott, Senior Vice President, Markets, PJM, and Joseph E. Bowring, President, Monitoring Analytics, to Lee A. Solomon, President, New Jersey Board of Public Utilities (Dec. 3, 2010), http://www.monitoringanalytics.com/reports/Market_Messages/Messages/PJM-MMU_Letter_to_NJ_BPU_20101203.pdf.

3. Contrary to P3's suggestions, New Jersey's legitimate public purposes may not be able to be achieved if resources responding to its pilot program are subjected to MOPR mitigation.

As explained above, New Jersey's legislative and executive branches enacted P. L. 2011, c. 9, out of concern regarding the age and composition of the generating fleet serving New Jersey's customers and a perceived need to spur the development of new, efficient, baseload or intermediate generation facilities in New Jersey. P3 allege that the MOPR reforms they seek will not frustrate legitimate state policies, but will merely insulate RPM prices against inappropriate price suppression.[34]

The facts do not conform to P3's rhetoric. P3 purport to allow States to decide when new entry may be needed, based on reasons broader than RPM's focus on whether sufficient total megawatts of whatever resource type clear in an LDA. But, in reality, their proposed mitigation reforms would make RPM the *de facto* arbiter of whether such entry actually occurs. The reason is that, as P3 puts it, "[l]egitimate state-sponsored entry can occur, but its offers into the capacity market will be mitigated and, once mitigated, might not clear the auction."[35] The ramifications of the P3 position are clear. If the resources that satisfy the State's policy goals fail to clear in RPM, the State's only means to fulfill its policy goals is to require its consumers to pay twice: once for the resources that satisfy the State's needs but failed to clear in RPM and, again, for the resources that did clear

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[34] *See* P3 Complaint at 9 ("[States] remain free to sponsor new entry by generation facilities, even if uneconomic by any rational measure. Effective mitigation does not preclude state-sponsored entry. All effective mitigation does is protect organized capacity markets from harm caused by any entity artificially suppressing wholesale price outcomes.").

[35] *Id.* at 9.

RPM, selected solely on the basis of the bid-stack within an LDA and without regard for resource type or other characteristics that the State might value. As a result, under the P3 scenario the State's consumers would be required to purchase more capacity than they need.

This situation can lead to only two outcomes. If the state procurement goes forward, then PJM will charge the state's load-serving entities unjust and unreasonable rates, requiring them to pay RPM prices for RPM-selected capacity that is not actually needed. Alternatively, if that prospect proves to be unpalatable, the state will be forced to abandon its procurement initiative, and RPM mitigation rules ostensibly designed as a check against market manipulation will have frustrated legitimate state interests in determining how its resource-adequacy needs are met.

The existing MOPR avoids this dilemma by allowing resources procured pursuant to certain state programs, like New Jersey's, to offer their capacity into RPM, without mitigation, at low prices reflecting that the resources will be developed regardless of the level of RPM's clearing prices. As explained by Mr. Wilson, such offers are economically rational and consistent with the proper functioning of competitive markets. The resulting effect on RPM prices, *if any*,[36] is not inappropriate price suppression. It is the result of RPM, a residual capacity market, appropriately reflecting the introduction of new

[36] Price-taker offers alter market outcomes only if the resource in question otherwise would fail to clear on the basis of price. As no resources have been procured yet through the New Jersey program, it is not possible to tell how the submission of price-taker offers for the resources that ultimately are selected would effect RPM prices.

resources that have been selected on the basis of criteria different than those employed by that residual market.

B. The Commission should retain the MOPR exception for resources developed as a result of state-mandated resource planning and procurement processes.

The Commission should retain the MOPR exception for resources developed in response to state-mandated resource-planning and procurement efforts. In this respect, our position overlaps with that of PJM, which proposes to retain the exception but to remove PJM's decision-making role. But PJM's proposal could be just and reasonable if it were modified in certain significant respects, as discussed below.

1. P3 fails to show that the MOPR exception for state-mandated resources has become unjust and unreasonable.

While P3 ask the Commission to eliminate the existing MOPR exception, P3 identify nothing that has changed to render that exception unjust or unreasonable. The parties to the RPM settlement, including several P3 members,[37] carefully negotiated the MOPR exception for resources procured as a result of certain state resource-planning and procurement efforts, and they did so expressly anticipating the kind of process that New Jersey has now undertaken. As recounted in the Explanatory Statement submitted with the 2006 RPM settlement,[38] the negotiations that produced that settlement were both

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[37] The P3 members who either supported or did not oppose the 2006 RPM settlement include: Constellation Energy Group Inc., Dayton Power & Light, Edison Mission Energy, Exelon Corp., Mirant Energy Trading (now part of GenOn), and NRG Energy.

[38] Settlement Agreement and Explanatory Statement of the Settling Parties Resolving All Issues, *PJM Interconnection L.L.C.*, Docket Nos. ER05-1410-000 *et al.* (Sept. 29, 2006), eLibrary No. 20061004-0159 ("Explanatory Statement").

protracted and intense. More than 150 individuals, representing more than 65 parties, engaged in more than 25 days of settlement discussions with direct Settlement Judge involvement and the assistance of the Commission's Dispute Resolution Service.[39] The settling parties included most of the active parties and spanned a "broad cross-section of load interests, generation owner interests, and state regulators."[40] The MOPR, in particular, was a "carefully balanced and limited rule"[41] that reflected give and take on the part of all settling parties.

Robert B. Stoddard—a Vice President of CRA International who represented Mirant in the negotiations and who has testified for generation interests in other cases involving capacity markets around the country[42]—submitted an affidavit in support of the negotiated MOPR.[43] Mr. Stoddard testified that he "participated fully in nearly all settlement meetings and conference calls," had "extensive personal involvement in the development and negotiation of several key aspects of the proposed market design that would be created by the proposed settlement," and "carefully reviewed the Settlement Agreement and the accompanying tariff sheets." *Id.* P 2. Mr. Stoddard submitted his

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39 Explanatory Statement at 3-4.

40 *Id.* at 1 n.1. Only six parties opposed the settlement term sheet, while four additional parties opted later to oppose the settlement. *Id.* at 4 n.15, 5 n.17.

41 Reply Comments of PJM Interconnection, L.L.C. in Support of Settlement, at 30, *PJM Interconnection, LLC*, Docket Nos. ER05-1410-000 *et al.* (Oct. 30, 2006), eLibrary No. 20061030-5098 ("PJM 2006 Settlement Reply Comments").

42 *E.g.*, Affidavit of Robert B. Stoddard On Behalf of New England Power Generators Association, Docket No. ER10-787-000 (Mar. 23, 2010), eLibrary No. 20100323-5076.

43 Supplemental Affidavit of Robert B. Stoddard, Attachment E to Settlement Agreement and Explanatory Statement of the Settling Parties Resolving All Issues, *PJM Interconnection L.L.C.*, Docket Nos. ER05-1410-000 *et al*. (Sept. 29, 2006) ("Stoddard 2006 Affidavit").

affidavit "in support of the overall settlement and, in particular, two elements of the settlement: the New Entry Price Adjustment Rule and the Minimum Offer Price Rule." *Id.* P 3. Mr. Stoddard noted that, "[a]s with all settlements, the proposed [RPM] market design reflects a number of compromises necessary to resolve this case without litigation" and that, "[w]ith this background in mind, it is my professional opinion that it is a reasonable market design." *Id.* P 4. Mr. Stoddard testified regarding the negotiated MOPR specifically, including the exception for resources developed in response to state-mandated resource-planning and procurement, explaining that it "should, in my professional opinion, reduce the incentive of buyers to undertake … wasteful over-investment in new capacity without restricting their ability to engage in, and realize the full value of, commercially reasonable bilateral contracts to provide for loads' future reliability needs." *Id.* P 8.

Mr. Stoddard reached his conclusions about the reasonableness of the balance struck in the negotiation over the MOPR with full awareness of the matters that are now advanced as revelations in the P3 complaint. First, Mr. Stoddard participated actively in the negotiations during which, presumably, witness Shanker raised the same concerns (discussed *infra*) that he later expressed in opposition to the settlement. Second, Mr. Stoddard was aware of, and discussed in his affidavit, a request for proposals by the Connecticut Department of Public Utility Control "seeking 'new or incremental capacity.'"[44] According to Mr. Stoddard, that new capacity was "required to submit bids

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[44] Stoddard 2006 Affidavit P 9 n.3.

into the New England Forward Capacity Market ('FCM') in a way narrowly tailored to be as low as possible without triggering the rule analogous to the MOPR, regardless of actual costs." *Id.* Connecticut was to "pay the difference between the bid cost and the revenue requirements of the new suppliers through supplemental contract payments." *Id.*

Despite his "concern" about such state programs and their effect on residual capacity prices, *id.*, Mr. Stoddard concluded that the MOPR, with its exceptions, represented a "reasonable" and "workable" market design that "reflect[ed] a widely-supported compromise of suppliers, buyers and regulators." *Id.* P 4. In his view, the MOPR and its exceptions "strike[] an equitable balance" that gives "contracting parties the benefit of the particular contract, while neutralizing large price distortions created by purchases well in excess of forecast reliability needs." *Id.* P 19.

Three years later, with even more information at his disposal regarding Connecticut's resource procurement and its interaction with FCM, Mr. Stoddard continued to defend PJM's MOPR as appropriately framed to balance states' interests with the need to protect RPM against anti-competitive actions. As Mr. Stoddard explained:

> The complexity of the MOPR is not unwarranted; each of its provisions was carefully and laboriously negotiated in the RPM Settlement Agreement to strike an acceptable balance between protecting wholesale markets from price manipulation, on the one hand, and allowing developers to offer long-lead-time resources rationally and allowing states to take necessary actions to preserve reliability.[45]

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[45] Affidavit of Robert B. Stoddard in Support of The Mirant Parties, at 9 P 13, Attachment A to Comments of the Mirant Parties Opposing Settlement Offer, *PJM Interconnection, L.L.C.*, Docket Nos. ER05-1410-012, *et al.*,(Feb. 23, 2009), eLibrary No. 20090223-5122 ("Stoddard 2009 Affidavit"). To the

At the time the Commission considered the 2006 RPM Settlement, certain other P3 members objected to the MOPR, raising arguments identical to those now advanced in the P3 complaint.[46] But the objecting parties persuaded neither PJM nor the Commission. In its reply comments supporting the settlement, PJM recounted the contesting parties' opposition and explained why those comments were off-base:

> PSEG/PPL nonetheless want the [MOPR] provision to go farther, by eliminating one of its exceptions. The [MOPR] establishes that certain types of new entry offers … will not require further scrutiny, such as base load resources that presumably recover all of their revenue requirements in the energy market. Similarly, a zero-price new entry offer will not be subject to re-pricing if the resource is being developed "in response to a state regulatory or legislative mandate to resolve a projected capacity shortfall in the Delivery Year affecting that state, as determined pursuant to a state evidentiary proceeding that includes due notice, PJM participation, and an opportunity to be heard."[47]

PJM explained that "[the] mandated RTO participation, along with the other conditions on that exception, distinguish[ed] the state action contemplated by the settlement from" the anti-competitive price-suppressing scheme described by PSEG/PPL. *Id.* at 32. PJM

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extent Mr. Stoddard's 2009 Affidavit revealed any concern about the MOPR's effectiveness, that concern was mild at worst. *Id.* at 10, P 14 ("If there is any weakness in the MOPR, in my view, it is that its exemptions may be over-broad and, therefore, allow some below-market supply offers to suppress the capacity clearing price."). But Mr. Stoddard appeared to accept those exceptions as reasonably necessary to protect states' interests in "tak[ing] necessary actions to preserve reliability," *id.* at 9, P 13. In any case, Mr. Stoddard—who joined Dr. Shanker as a witness in support of the New England Power Generators' efforts to modify New England's "Alternative Price Rule," *see* Complaint Requesting Fast Track Processing by New England Power Generators Association, *New England Power Generators Association Inc. v. ISO New England, Inc.*, Docket No. EL10-50-000 (Mar. 23, 2010), eLibrary No. 20100323-5076—has not espoused any need to modify either the PJM MOPR or its exceptions.

[46] *See* Affidavit of Roy J. Shanker, Ph.D., Exhibit B-1 to the Initial Comments of the PPL Parties and the PSEG Companies In Opposition To Proposed Settlement, *PJM Interconnection, L.L.C.*, Docket Nos. ER05-1410-000, *et al.*, PP 42-52 (Oct. 19, 2006), eLibrary No. 20061019-5068 (Shanker 2006 Affidavit).

[47] PJM 2006 Settlement Reply Comments at 31-32.

went on to explain why the MOPR's balanced provisions were superior to PPL/PSEG's approach:

> While PSEG/PPL apparently would have the Commission develop a rule that attempts in advance to proscribe or limit a broad range of possible state actions, *the settlement takes a respectful, reasonable, and balanced approach on this question. Not surprisingly, this exception was very important to certain state regulatory authorities, and helped the parties reach a compromise that allowed the Minimum Offer Price Rule to be added to RPM.*

Id. (emphasis added).

PJM was correct in that assessment. And P3's effort to claw back now concessions that some of its members made in 2006 (no doubt in exchange for offsetting concessions by the other side)[48] would substantially change the balance struck in that agreement. Although the settlement was made subject to modification using a just-and-reasonable standard, not the *Mobile-Sierra* public-interest standard,[49] the Commission has stated repeatedly that it does not take contract modification lightly even under a just-and-reasonable standard.[50] Absent unforeseen changed circumstances, none of which has been alleged let alone proven, there is no basis to declare unreasonable now provisions

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[48] For example, the demand curve adopted in the 2006 settlement was far closer to PJM's initially-proposed curve than it was to the construct previously in place. *See PJM Interconnection, L.L.C.*, 117 FERC ¶ 61,331, PP 80-81 (2006). More generally, the Commission appears to have recognized that the MOPR applied to buyer market power was one of the generators' "gets" in the negotiations and that the exception for state-mandated resource procurement was one of their "gives." *See id.* P 86.

[49] *See* Settlement Agreement at 46.

[50] *See PacifiCorp v. Reliant Energy Servs., Inc.*, 99 FERC ¶ 61,381, P 27 & n. 21 (2002) ("[E]ven under a 'just and reasonable' burden of proof standard, parties who seek to overturn market-based contracts into which they voluntarily entered will bear a heavy burden… By emphasizing that a complainant bears a heavy burden of proof, we state the obvious that the sanctity of contracts is presumed and that the Commission will not lightly undo the terms of existing contracts even under the just and reasonable standard of review.")

that sophisticated parties agreed to as a reasonable compromise of complicated market-design questions. Rights secured through a settlement agreement should not be declared unreasonable simply because an entity makes use of them.

Similarly, absent unforeseen changed circumstances, there is no reason for the Commission to reverse its previous finding, on the merits, that the MOPR—including the exception for resources developed in response to state-mandated procurement—was just and reasonable. In reviewing the contested settlement, the Commission recognized that "PJM and its members engaged in extensive negotiations to resolve the many difficult questions contained in this Settlement, and went to great lengths to arrive at compromises that were acceptable to the majority of PJM members."[51] Nonetheless, because the Commission found a need to modify the settlement in certain respects, the Commission could not accept the settlement as a package under the second *Trailblazer* approach, as PJM and the Settling Parties had asked.[52]

Instead, the Commission "describe[d] and evaluate[d] …*each of the contested elements of the Settlement, and [made] a determination whether the provisions are just and reasonable*, taking into account the integrated nature of the capacity market design."[53] With certain exceptions not relevant here, the Commission expressly found

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[51] *PJM Interconnection, L.L.C.*, 117 FERC ¶ 61,331, P 51 (2006) (citing Explanatory Statement and November 9, 2006 Report on Contested Settlement by Settlement Judge).

[52] *Id.* P 57.

[53] *Id.* P 58 (emphasis added). *See also* Answer of PJM Interconnection, L.L.C. to Motion to Vacate Order, Motion for Stay, Requests for Clarification, and Certain Requests for Rehearing, at 10, *PJM Interconnection, L.L.C.*, Docket Nos. ER05-1410-000, *et al.* (Feb. 6, 2007), eLibrary No. 20070206-5057 ("When the Commission reviews a contested settlement under that approach, it 'renders a binding merits decision on each contested issue' [which] is exactly what it did here.") (citation omitted).

that "the Settlement's provisions for market power monitoring and mitigation are reasonable." *Id.* P 100. More specifically, the Commission found the negotiated MOPR to be "a reasonable method of assuring that net buyers do not exercise monopsony power by seeking to lower prices through self supply." *Id.* P 104. The Commission further held that "[t]he exception to which PPL/PSEG primarily objects—namely, reliability projects built under state mandate—is reasonable because it enables states to meet their responsibilities to ensure local reliability." *Id.*

None of the P3 members sought rehearing of the Commission's approval of the negotiated MOPR, including its exceptions. P3's challenge—which fails to articulate any new, unforeseen circumstances—is simply a collateral attack on (and an untimely request for rehearing of) the Commission's approval of those provisions as just and reasonable. Having negotiated a settlement that authorized the conduct now challenged, or (with respect to the P3 members who contested the settlement) having chosen not to appeal the Commission's rejection of objections to the provisions authorizing that conduct, P3 cannot now mount a successful challenge based on state actions that were both foreseeable and foreseen.

2. PJM's proposal to retain the MOPR exception for state-mandated resource procurement, while removing PJM's decisional role, could be reasonable if it is modified appropriately.

Since approving the 2006 settlement discussed above, the Commission has continued to recognize the need to harmonize state resource-procurement decisions with wholesale capacity pricing mechanisms. Even in New York, a single-state RTO that the

Commission has found to be more vulnerable than PJM to price-suppression efforts,[54] the Commission has acknowledged that states must be able to seek exemptions from minimum offer-price requirements that could frustrate state policy.

New York ISO ("NYISO") proposed a minimum offer price rule that, unlike the PJM rule, lacked an exception for resources developed in response to state resource-planning and procurement initiatives.[55] The New York Public Service Commission ("NYPSC") protested NYISO's filing. The Commission initially rejected the NYPSC's claims, contending that NYISO's filing merely determined "how prices for capacity in the wholesale markets should be determined" and would not "adversely affect NYPSC's regulation of resource adequacy in NYC."[56] The NYPSC sought rehearing,[57] explaining that FERC's decision (like P3's position here) "would create a situation where LSEs could be forced to pay twice to meet resource adequacy requirements: once for any State-selected facilities that do not clear the auction due to the imposition of the mandatory minimum bid requirement and again for the ICAP that clears the auction." *Id.* at 9-10.

On rehearing, the Commission agreed with the NYPSC. It recognized that states may legitimately conclude that "the procurement of new capacity, even at times when the market-clearing price indicates entry of new capacity is not needed, will further specific

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54 *New York Indep. Sys. Operator, Inc.*, 124 FERC ¶ 61,301, P 37 (2008).

55 *New York Indep. Sys. Operator, Inc.*, 122 FERC ¶ 61,211, PP 100-112 (2008), *reh'g granted in part*, 124 FERC ¶ 61,301 (2008), *pet. for rev. pending sub nom. NRG Power Marketing LLC et al. v. FERC* (D.C. Cir. filed July 26, 2010).

56 122 FERC ¶ 61,211, PP 111-112.

57 Request for Rehearing of the Public Service Commission of the State of New York, at 2, *New York Indep. Sys. Operator*, *Inc.*, Docket No. EL07-39-000 (Apr. 7, 2008), eLibrary No. 20080407-5167 (quoting 16 U.S.C. § 824o(i)(2)).

legitimate policy goals, such as renewable portfolio standards."[58] Consequently, the Commission agreed that "*it may be appropriate to exempt such new resources from the price floor proposed by NYISO*," although it found that the NYPSC had not provided enough specificity to allow the Commission to frame an appropriately narrow exemption. *Id.* (emphasis added).[59]

In its Section 205 filing in this case, PJM proposes to retain a MOPR exemption for state-mandated resource procurement, to remove PJM's decisional role in implementing it, and to require resources or states seeking to use it to make a Section 206 filing with the Commission. As explained below, we do not quarrel with PJM's suggestion that the Commission administer the exceptions, nor do we challenge the notion that those seeking to operate under the exception make a filing with the Commission to implement it. However, we object to the notion that those seeking to avail themselves of a self-executing exception found in the current MOPR would, under the new regimen, be obligated to (1) bear a Section 206 burden of proof in order to invoke the exception, and (2) satisfy criteria that go well beyond those found in the Commission-approved MOPR.

PJM is correct that "states in the PJM region … continue to have an important oversight role in the procurement of generation,"[60] and that it is "reasonable to

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[58] 124 FERC ¶ 61,301, P 38 (2008).

[59] Because the NYPSC had not provided sufficient detail to enable the Commission to craft an appropriately narrow exemption, the Commission invited the NYPSC to "make a filing under section 206 of the FPA to justify a mitigation exemption for entry of new capacity that is required by a stated-mandated requirement that furthers a specific legitimate state objective." *Id.*

[60] PJM Section 205 Filing at 4.

acknowledge the possible legitimacy of 'reliability projects built under state mandate,' because they 'enable[] states to meet their responsibilities to ensure local reliability.'"[61] We thus agree that PJM should "retain a[MOPR] exception for offers that are justified on state policy grounds."[62] PJM proposes tariff changes, however, in order to eliminate what it views to be its decisional role in implementing that exception.[63] PJM believes that the Commission should administer the exception instead:

> [W]hether to allow capacity sell offers from such projects [developed through state procurement efforts] if they fail the MOPR screen can present difficult issues and likely would involve a balancing of competing policy interests. Such determinations go well beyond the limited role of a tariff administrator and are properly the province of the Commission. Accordingly, PJM is replacing the current, purportedly self-implementing, exception process for state-mandated reliability projects with an exception process, like that approved for the NYISO, that necessarily involves the Commission, through an FPA section 206 filing.

Id. at 15-16. PJM states that it is "adopt[ing] language from the *NYISO* orders to capture the principles that will govern such [an] exception request."[64]

Rate Counsel does not oppose having the Commission, rather than PJM, determine whether offers from resources procured in response to a specific state program

[61] *Id.* at 15 (citation omitted).

[62] *Id.* at 14.

[63] *Id.* at 15 ("As currently drafted, therefore, this provision puts PJM (as Tariff administrator) in the position of having to pass on the adequacy of state administrative processes as part of determining whether to accept a sell offer that might otherwise fail the MOPR screens. PJM also would have to determine, in the first instance, whether an offer was legitimately intended to address a projected capacity shortfall in the relevant area.").

[64] *Id.* at 16.

fall within the MOPR exception.[65] But we object to the way in which PJM purports to implement that shift. There are two areas of concern: first, how the exception is phrased and, second, the procedure by which it is invoked. On the first issue, there is no reason (and PJM offers none) why removing PJM's decisional role in implementing the exception requires changing its scope. Thus, the existing exception should be retained as-is, with the only change being that the Commission would determine whether the conditions set forth in the exception had been met.

PJM asserts that it has "drafted the exception language to focus the parties on new entry that is pursuant to 'a state-mandated requirement that furthers a specific legitimate state objective' and that the Sell Offer would not 'lead to artificially depressed capacity prices' or directly and adversely impact [the Commission's] ability to set just and reasonable rates for capacity sales in the PJM Region or any affected Local Deliverability Area." *Id*. at 16. Only the first quoted criterion—referring to state-mandated requirements furthering legitimate state objectives—is taken from the NYISO rehearing order. The other two criteria are new, and have been proposed by PJM. If read incorrectly, the new criteria could negate the potential for such an exception altogether. Specifically, if all downward price pressures resulting from state resource-procurement efforts or from bidding such resources as price takers were considered to be "artificial" price

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65 PJM has overstated the extent of its decisional role in implementing the existing exception, however. We agree with PJM that it should not be in the position of having to pass on the adequacy of state administrative processes, whether an offer was legitimately intended to address a projected capacity shortfall, or the "sufficiency of state policy justifications." *Id*. at 15. In the circumstances of this case, however, the purposes for which New Jersey enacted P. L. 2011, c. 9, are clear on the face of the legislation, and there will be no question whether offers for particular resources are connected to the legislative program, as the state legislation will result in long-term contracts for the relevant resources.

suppression, as P3 for example believes, then PJM's new proposed criterion would swallow the exception. PJM's re-write of the state-procurement exception should therefore be rejected.

Similarly, shifting the locus of decision-making from PJM to FERC creates no reason to erect a new, Section 206 barrier to the use of an existing exemption. Section 206 is the means by which entities petition the Commission to find that an existing rate is unjust and unreasonable and must be changed. In this case, unlike New York, the PJM tariff already includes a MOPR exception which the Commission has approved as just and reasonable. Accordingly, entities submitting offers to be treated in accordance with that exception should not be forced to satisfy the standard applicable to a change to a filed rate. Instead, resources seeking to be treated in accordance with the existing exception for state-mandated resource procurement should be permitted to make a filing demonstrating that the conditions of the exception have been satisfied. Such a filing could be a Section 205 filing if the seller is a public utility, a comparable submission if the seller is non-jurisdictional, an information filing or request for declaratory order, or some other mechanism. But it should *not* be a Section 206 filing and should not be evaluated using Section 206's standards. So long as the applicant demonstrates that its offer is consistent with the term of the PJM tariff, including the tariff's existing exemption for state-mandated resource procurement, the Commission should direct PJM to use the offer in conducting the auction.

C. FERC should not transform the MOPR from a narrow provision addressing anti-competitive conduct to a broad-ranging check on the incidental price effects of legitimate behavior.

P3's proposal (not shared by PJM) to eliminate the MOPR exception for resources developed through state-mandated resource procurement is but one troubling element in the campaign for the adoption of a broader, unspoken, and unjustified shift in the MOPR's underlying paradigm. As conceived, the MOPR was a narrowly-tailored rule designed to prevent purposeful, anti-competitive price suppression by buyer-side market participants (or by entities whose interests are aligned such participants).[66] What P3 and, to a lesser extent, PJM now propose is something much different. They propose to transform the MOPR into a wide-ranging, administrative price support designed to insulate RPM's residual capacity auction from the incidental price impacts of legitimate market-participant and state regulatory (or legislative) activities.

PJM asserts that the MOPR must be modified because it has never been triggered.[67] But mitigation is not an end in itself, and the most likely reason why there has been no triggering of the MOPR is that the anti-competitive, price-suppressing activities to which it is directed have not occurred (and, for the reasons set forth above, are unlikely to occur). As one of P3's members previously explained:

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[66] *E.g.*, Stoddard 2009 Affidavit at 5, P 7. As Mr. Stoddard explained, the MOPR was a "narrowly crafted" rule designed to "limit the ability of load-serving entities ('LSEs') that are net buyers of capacity to suppress prices in a BRA below competitive levels through offers of supply at prices that do not reflect their actual cost." Reflecting its limited, though important, function, the MOPR included "several exemptions, including one that effectively permits state commissions to override the MOPR if it is established in an evidentiary proceeding that new supply is needed." *Id.* (citations omitted).

[67] PJM Section 205 Filing at 3.

> [T]he fact that the MOPR has not been triggered falls far short of demonstrating that it is ineffective: To the contrary …, this could equally be read as proof that the MOPR is fulfilling its intended purpose to deter any attempts by net buyers to exercise monopsony power.[68]

The Commission should therefore resist calls to broaden the MOPR's net so that it will catch *something*—even if that something is not anti-competitive behavior. Instead, it should continue to maintain the MOPR's focus on purposeful, anti-competitive price suppression.

Mr. Wilson explains (P 8), that the absence of MOPR intervention during RPM's first seven residual auctions and the absence of allegations that the rule should have triggered during those auctions show that "[t]o the extent the problem addressed by the MOPR exists, the rule apparently has been sufficient to date." In contrast, the P3 and PJM proposals to revamp the MOPR "have the potential for considerable harm to consumers and the market by discouraging new entry and denying capacity payments to new generation that has been built for legitimate business and/or state policy purposes and not as an exercise of market power." *Id.* P 10.

Mr. Wilson explains that the P3 and PJM proposals are based on a "fundamental misconception regarding how major new resources are developed and offered into RPM." *Id.* P 13. As he explains:

> The proposal rests on the belief that the sponsors of new power plants will (or should) offer their projects into

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[68] Comments of the Mirant Parties Opposing Settlement Offer, *PJM Interconnection, L.L.C.*, Docket Nos. ER05-1410-012 *et al.* (Feb. 23, 2009), eLibrary No. 20090223-5122; *see also id.*, Stoddard 2009 Affidavit at 8, P 12 ("To the contrary, the existence of a rule may be an effective deterrent from engaging in the proscribed behavior: had the MOPR not been in place, it is possible that new, uneconomic entry … would have occurred …").

> RPM's auctions at prices based on their full levelized cost of new entry net of an estimate of net earnings from energy and ancillary services markets, and allow the auction result to determine whether or not they will build the resource.… [I]n fact, the sponsors of new power plants generally will not, and certainly should not be forced to, offer their plants into an RPM auction at prices determined in this manner. Decisions to build new long-lived power plants are rationally based on a long-term view of plant economics, and sponsors will generally not submit their decision to the result of an auction whose outcomes are notoriously volatile and which in any case determine a capacity payment for only a single year. Instead, decisions to build major new power plants generally occur outside of RPM and then are reflected in offers into RPM that the sponsors fully expect will clear.

Id. Mr. Wilson points to the offers and outcomes of the first seven RPM base residual auctions, which neither P3 nor PJM has challenged, to prove his point. He shows that "[n]ew power plants, including combined cycle ('CC') and combustion turbine ('CT') plants have consistently been offered into RPM at prices far below Net CONE." *Id.* P 14. Specifically:

> For the most recent base residual auction (2013/2014 delivery year), PJM reported that 1,670.4 MW of new generation capacity was offered, and all of it – all 1,670.4 MW – cleared. Most of this capacity (961.1 MW) was offered and cleared in the Rest of RTO region, meaning it was offered at a price no greater than $27.73/MW-day, a small fraction of Net CONE. In the base residual auction that attracted the most offers for new generation (2011/2012; there were thirteen offers for new CTs and CCs, compared to no more than 7 in any other base residual auction), 1,135 MW of new combined cycle capacity was offered. PJM's Independent Market Monitor ("IMM") reported that only 43.5 MW of combined cycle capacity was offered at a price greater than $35/MW-day in this

> auction, far below the clearing price of $110/MW-year, or Net CONE, which was higher still.[69]

Mr. Wilson observes (*id.*) that actual experience in the RPM auctions thus contradicts PJM's "expect[ation]" that "very few" offers from CCs or CTs would be priced significantly below Net CONE.[70] Conversely, he points out, "according to PJM's proposed screen, nearly all of the offers from new power plants into RPM to date would have been deemed 'uneconomically low' by a wide margin." *Id.* P 15. Mr. Wilson explains that implementing the P3 and PJM proposals would thus interfere with the "normal competitive process by which new resources are brought to the market," *id.* P 12.[71]

If the Commission is nonetheless inclined to entertain MOPR changes like those proposed by P3 and PJM, we urge that it proceed cautiously. The adoption of a regimen that "over-mitigates" will result in unreasonable interference with both capacity-sellers' legitimate business decisions and states' legitimate regulatory programs. To avoid such

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69 *Id.* (citations omitted).

70 PJM Section 205 Filing at 14.

71 In effect, and consistent with the conception of RPM as a residual capacity market that provides only short-duration price certainty to potential entrants, RPM prices are not—and should not be expected to be—the primary driver of new entry. Mr. Wilson cites "two major reasons why the notion that new construction should rely solely on spot market revenues should be rejected." *Id.* P 18. First, he explains, "both buyers and sellers prefer longer-term commitments and the price stability and assurance of supply that go with longer-term arrangements." *Id.* P 19. Second, he notes, "resource additions are increasingly being selected based on a range of attributes that RPM and the other PJM spot markets do not value," such as "environmental attributes, fuel diversity, and operational characteristics, among other factors." *Id.* P 20. And once entry decisions are made for such reasons, it is both economically rational for the resource—and consistent with the proper functioning of a residual capacity market—for the resource to offer its capacity at a low price reflecting its going-forward costs and for the residual market price to respond accordingly.

harm, any MOPR changes adopted in this proceeding should conform to the recommendations set forth in Mr. Wilson's affidavit. Specifically:

- The purpose of the MOPR should continue to be to mitigate potential exercise of buyer market power and should not be changed to "preventing uneconomically low offers" from new entry generation;
- Because Net CONE is a very imperfect proxy for a competitive offer price, the offer screen and substitute price should reflect a substantial discount off the nominal values;
- Market participants should be afforded the opportunity to justify unit-specific offer prices through a Net CONE or Net Present Value analysis reflecting a sponsor's forecasts of all revenues, including capacity revenues or revenues under a bilateral contract; unit-specific incremental costs; and incentives offered for preferred resource attributes;
- Mitigation should apply for one year unless a resource is being used in an attempt to suppress capacity market prices;
- Real, not nominal, levelization of CONE is appropriate for the MOPR; [and]
- The "net buyer" and impact tests in the current MOPR should be retained but improved.

Id. P 26. Additionally, as we explained above, the exemption for state-mandated resources should be retained. *Id.* We address below key aspects of each recommendation. Mr. Wilson's affidavit contains a detailed discussion of these recommendations as well as their underlying bases.

1. It is not just and reasonable to set the screen and the substitute offer to 90 percent or 100 percent of Net CONE, particularly when done in conjunction with eliminating the net-buyer requirement and impact test.

As Mr. Wilson explains, "[t]he most critical element of market rules designed to mitigate low-priced offers is the criterion used to determine whether mitigation will be applied and to set the replacement offer price that will be imposed." Wilson Affidavit, P 38. Mr. Wilson explains that the P3 and PJM proposals to set screens and mitigation to 90 percent or 100 percent of Net CONE "preclude competitive offer prices from new generation." *Id.* P 40. He acknowledges that the current MOPR employs the same approach, albeit with lower percentages, but notes that the current MOPR "includes features such as the 'net buyer' and impact tests that ensure the mitigation would be applied …infrequently." *Id.* Consequently, he finds, "the flaws in this approach to screening and mitigation are relatively benign under the current rules." *Id.* PJM's proposed approach would mitigate a much broader class of offers that fail the screen without regard for whether they represent attempts to exercise market power, and would thus result in mitigated offer prices "well above competitive levels under common circumstances, creating a substantial barrier to entry." *Id.*

Mr. Wilson begins by explaining why Net CONE is a poor proxy or estimate for a competitive offer price. *Id.* P 42. He observes the basic economic principle that project sponsors will invest if they expect the present value of all revenues over the life of the project to exceed the present value of all of the costs to build and operate it, including the risks associated with doing so. *Id.* P 43. The Net CONE calculation deviates from this principle in two important ways. First, Net CONE is a levelized or annual value rather than a present value. *Id.* P 44.[72] Second, future capacity revenues are excluded from the calculation. *Id.*[73]

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[72] Mr. Wilson demonstrates that PJM's proposal to change the levelization method, from real to nominal levelization, is unreasonable. *See id.* PP 73-86.

[73] Mr. Wilson explains that the Net CONE calculation "can be understood to impose the assumption that whatever capacity price is received in the first auction will also be received in all future auctions over the life of the plant." *Id.* P 48. If a new entrant's expectations of future capacity revenues diverge from this assumption, Net CONE's value as a proxy for a competitive entry offer diminishes.

Mr. Wilson explains that these flaws in the Net CONE approach have two implications for MOPR mitigation. First, they suggest that market participants should be permitted to justify their offers based on a net present value ("NPV") calculation as an alternative to the Net CONE calculation. *Id.* P 49. Second, if the Net CONE approach is retained and NPV-based justifications are not permitted, then the screens and mitigation levels should be set at levels well below the nominal Net CONE values. *Id.*

Mr. Wilson also identifies another flaw in the proposed approach to screening and mitigating new entry offers. The calculations "assume the entire construction cost for a resource is incremental cost." *Id.* P 53. That is, they assume that "a decision to build the unit has not yet been made, there are as yet no 'sunk' costs or other commitments, and the sponsors can walk away from the project at little or no cost." *Id.* But that is not always the case. *Id.* As Mr. Wilson explains, states may adopt programs to encourage or to sponsor new entry by resources that have attributes not valued by RPM. These may include environmental attributes, fuel diversity, the resource's operational characteristics, or location, among other factors. And once a decision to sponsor entry of such resources is made (for reasons having nothing to do with RPM), most of the cost associated with such entry is effectively sunk.

Mr. Wilson explains that project sponsors should be permitted to justify offers using different methods than the single, rigid approach advocated by PJM. *See id.* P 59. Under PJM's revised MOPR provision, to gain approval for a unit-specific offer price, sponsors would have to demonstrate that their offer is "consistent with the competitive, cost-based, fixed, nominal levelized, net cost of new entry were the resource to rely solely on revenues from PJM administered markets." *Id.* (quoting revised PJM tariff).

Instead, project sponsors should be permitted to present any of the following:

- A specific forecast of net energy, ancillary services, and capacity revenues over the life of the project;
- Long-term revenues provided under a bilateral contract;
- Incentives in recognition of preferred resource attributes that are not valued in RPM;
- Incremental costs that exclude sunk costs (costs already spent or committed);
- A net present value comparison of total anticipated net revenues from all sources (including capacity payments) over the life of the project compared to present value costs;
- A net present value or Net CONE calculation based on incremental costs excluding any sunk costs.

Id. P 60. Unless such factors are considered in evaluating project-specific offers prices, competitive offers will be disallowed, reducing the market's efficiency. *Id.* P 61.

In any case, if Net CONE continues to be used as the primary (or exclusive) touchstone of what constitutes an "economic" offer, but the net buyer and impact tests are eliminated, then the screen percentages should be lowered, or at least left at their current levels. As the Commission has recognized, each of the two components used to determine Net CONE—gross CONE and future energy and ancillary service revenues—is highly uncertain. *Id.* PP 67-68. Thus, basing mitigation screens on a higher percentage of the nominal Net CONE value would preclude many competitive offers. *Id.* P 67.

2. The proposals to do away with the net-short requirement and the impact test are unjust and unreasonable.

P3 and PJM each propose to eliminate two significant features of the current MOPR: the net-buyer requirement and the impact test. Each of those market-design elements has served as a check on potential over-mitigation of offers that were not likely aimed at suppressing market prices or that could be shown to have little effect. Removing those provisions raises the specter of over-mitigation—administrative interference with offers that actually are consistent with rational economic behavior and properly functioning markets. Mr. Wilson explains that those provisions should be retained but improved. *Id.* PP 87-90. The net-buyer test should be revised to apply mitigation not only to resources owned by net buyers but to resources offered by counter-parties of net buyers. *Id.* PP 88-89.

Mr. Wilson asserts that the impact test should also be retained because, like the net buyer limitation, it serves as an important check on over-mitigation. "Mitigating offers from new resources that would have little or no impact on clearing prices may cause them not to clear, with another resource (likely a high-cost older resource with much shorter remaining useful life) clearing instead." *Id.* P 90. That result would not be efficient. But Mr. Wilson acknowledges that the current impact thresholds are quite loose and should be tightened to the 5-10 percent range. *Id.* P 89.

3. The proposal to extend the mitigation period is not just and reasonable and could erect barriers to entry by subjecting new entrants to risks that they will be mitigated for reasons beyond their control.

Mr. Wilson explains (P 62) that under the current MOPR a new resource is mitigated in the first year for which it qualifies to offer into RPM, but PJM proposes to impose mitigation until the resource clears, despite mitigation, plus two additional years. While that could be an appropriate response to intentional price-suppression efforts, it is not appropriate in a mitigation scheme focused on price impacts, regardless of intent. Mr. Wilson states that if the MOPR's purpose is expanded, then mitigation should be limited to one year. *Id.* P 63. He explains that:

> Under PJM's proposal, a resource that is not being used to exercise market power could be prevented from clearing and receiving a capacity supply obligation for several years. For instance, if other entry, or new transmission facilities, lower RPM clearing prices below the offer price floor imposed on the resource, it could fail to clear even though the clearing prices exceed the resource's going forward cost and it is economic. This is plainly unacceptable and a serious barrier to entry, as it would impose substantial risk on future projects due to the unpredictability of market conditions and RPM clearing prices. It would also be unfair to resources that may at present be in an advanced stage of development under the current rules.

Id. Mr. Wilson explains that the current MOPR duration, one year, should be retained as the default and that PJM, the independent market monitor, or any market participant could file under FPA section 206 to have mitigation extended for any resource that they believe should be mitigated longer. *Id.* P 66.

D. The Commission should deny the complaint, reject PJM's filing, and instead direct that PJM consider any needed changes to the MOPR and related tariff provisions in consultation with its stakeholders.

The P3 Complaint seeks to force (and already has forced) consideration of significant tariff changes at an unduly breakneck pace. Proceeding in such a fashion is neither wise nor necessary. The Commission should deny the complaint and reject PJM's filing without prejudice to the potential submission of a later Section 205 filing developed following due consultation with PJM stakeholders.

It is plain that P3's Complaint rushed PJM's development of a position on these matters, and prevented PJM's stakeholders from considering them in a deliberate and deliberative fashion. At the December 15, 2010 meeting of the PJM Markets and Reliability Committee, a member recommended that "PJM initiate a process to review

RPM rules to see if they could be further enhanced in light of pending legislation in New Jersey." At the Committee's January 19, 2011 meeting, a document describing the issue and suggesting a process for addressing those issues was introduced.[74] The document noted PJM's support for the review, as well as its view that "realistically any recommendations that would come out of this group could not be implemented for the 2014-2015 Base Residual Auction," *id.* at 2. The document indicated the drafters' expectation that the RPM Task Force's work would be completed by the end of summer 2011, "so that if revisions to the RAA must be FERC filed, there will be sufficient time for FERC to rule in time for the 2015-16 auction." *Id.* P3 filed their complaint less than two weeks later, however, which effectively truncated the stakeholder process. To our knowledge, nothing further has occurred with respect to this stakeholder initiative since January 19, 2011.

Instead, in response to the complaint, PJM determined that "the most effective means of presenting for Commission consideration PJM's alternative approach to MOPR reform" was to submit a Section 205 filing proposing changes different from those sought by P3. The Commission generally requires RTOs such as PJM to vet proposed rule changes through their stakeholder advisory processes. But in this case, no such process occurred.

In lieu of a process, PJM held a single conference call, on February 9, to inform stakeholders of the Section 205 filing that it intended to make as its "answer" to the P3

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[74] "RPM Enhancements: Problem Statement," available at http://www.pjm.com/~/media/committees-groups/committees/mrc/20110119/20110119-item-06-rpm-issues-problem-statement.ashx.

complaint. PJM submitted its Section 205 filing just two days later. Convening a 200-300 party conference call to discuss a decision that had already been made is in no way a "stakeholder process." Indeed, even if this cattle-car approach to stakeholder deliberation were acceptable, technical difficulties during the call limited the opportunities for questions and answers. Stakeholders have otherwise had no opportunity to engage PJM or its market monitor regarding these issues. Nor has either PJM or its market monitor engaged PJM's stakeholders in a meaningful discussion about the issues that PJM raises in its Section 205 filing.

The Commission's regulations are similarly designed to give affected entities a chance to resolve issues collaboratively before the Commission is called on to resolve contested issues through adjudication. Notwithstanding these regulations, P3 did not do so and thus deprived other PJM stakeholders of an opportunity to consider potential MOPR changes before P3 filed their complaint. Rule 206(b)(9) of the Commission's regulations, 18 C.F.R. § 385.206(b)(9), requires complainants to state whether dispute resolution procedures were used or why they were not used, whether alternative dispute resolution (ADR) under the Commission's supervision could resolve the complaint, and what ADR procedures could be used. These regulations exist to promote informal dispute resolution and thus to conserve both the Commission's and the parties' resources, but P3 failed to abide by those requirements.

P3 assert that they "attempted in good faith to resolve these matters," but their efforts apparently were limited to (i) attempting to persuade the New Jersey legislature not to enact its legislation, and (ii) seeking, during a "long" but otherwise undefined period, unspecified "reforms … to improve and strengthen the [MOPR]."[75] Neither constitutes a *bona fide* effort to resolve informally the matters raised in P3's Complaint. Attempting to persuade New Jersey not to enact its legislation is a far cry from engaging PJM and its stakeholders in meaningful dialog about the subject of P3's Complaint: whether (and, if so, how) the MOPR should be changed in light of that legislation. And P3's vague assertions that they have "long, but without signal success" sought MOPR reforms at the stakeholder level is far too general a statement to permit any conclusion that P3 attempted to resolve the matters in P3's Complaint before filing it.

Because P3 raced to the courthouse,[76] and because PJM hurriedly developed and filed a counter-proposal without meaningful stakeholder input, PJM's stakeholders have not had adequate time to assess their proposed MOPR overhauls thoroughly and thoughtfully. This impairs not only the stakeholders' ability to protect their own interests but also the quality of the presentations made to the Commission and, ultimately, the quality of the Commission's decision-making.

By contrast, in New England, substantial stakeholder discussions preceded the generators' filing of a complaint seeking changes to the region's Forward Capacity Market; the Commission convened a paper hearing with three rounds of briefs; and the

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[75] Complaint at 74.

[76] In fact, P3 raced to multiple courthouses. In addition to asking the Commission to modify the MOPR on a fast-track basis, P3 filed a lawsuit in the United States District Court for the District of New Jersey seeking to have the law declared unconstitutional and its enforcement enjoined. *PPL Energyplus, LLC et al. v. Solomon et al.*, Docket No. 2:11-cv-00745-PGS-ES (D.N.J. complaint filed Feb. 9, 2011). P3 members also have asked the Board to stay its implementation of P. L. 2011, c. 9. *See* Motion to Stay, In the Matter of the Long-Term capacity Agreement Pilot Program, BPU Docket No. EO11010026 (Feb. 18, 2011).

Commission's decision has been pending since September.[77] Issues raised by proposed redesigns of regional capacity markets simply are not conducive to hurried decision-making.

Even more fundamental, assuming *arguendo* that P3 are correct regarding the MOPR's short-comings, there has been no showing that a rush to judgment is necessary. Here, given the recent vintage of the New Jersey legislation and the early stage of the New Jersey Board of Public Utilities proceeding to implement it, few of the potential participants in the New Jersey pilot program are likely to participate in the May 2011 auction. The only entity of which we are aware that intends to participate in that auction is West Deptford Energy, LLC, which recently filed with the Commission a request for a determination that its offer "to sell capacity … in PJM's May 2, 2011 Base Residual Auction … is consistent with WDE's unit-specific costs and expected revenues from the PJM-administered markets."[78] If the Commission grants WDE's request, any need for expedited resolution of the matters raised in these proceedings likely will vanish.

Thus, we submit that the Commission should deny the complaint, and reject the PJM filing without prejudice to the submission of a new PJM 205 filing developed following due consultation with stakeholders. Alternatively, the Commission should set both the complaint and the 205 filing for evidentiary hearings, hold the hearings in abeyance, and establish settlement judge procedures. In either case, the Commission should allow PJM and its stakeholders, including interested state entities, a meaningful

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[77] Third-round briefs were filed in Docket Nos. ER10-787-000 *et al.* on September 29, 2010.

[78] WDE Filing, *supra* n.6.

opportunity to address the issues raised in the PJM and P3 filings—*not* whether the New Jersey legislation was sound policy, but whether (and, if so, how) the PJM tariff should be revised.

III. CONCLUSIONS

For the foregoing reasons, the Commission should deny the complaint, and reject the PJM filing without prejudice to the submission of a new PJM 205 filing developed following due consultation with stakeholders. Alternatively, the Commission should set both the Complaint and the Section 205 filing for evidentiary hearings, hold the hearings in abeyance, and establish settlement judge procedures.

Respectfully submitted,

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