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Client Alert
Commentary

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FERC Issues Order to Mitigate the Impact of State Preferences on the PJM Capacity Market

Stakeholders in the PJM capacity market can submit comments to FERC in an expedited paper hearing regarding the form of mitigation.

Key Points:

- FERC issued preliminary findings that state preferences may suppress PJM's capacity market prices.
- FERC seeks comment on how the Minimum Offer Price Rule and the Fixed Resource Requirement should be expanded.

On Friday, June 29, 2018, the Federal Energy Regulatory Commission (FERC or the Commission) issued an order (the Order)[1] to respond to capacity market mitigation proposals in two separate proceedings relating to the capacity market administered by PJM Interconnection LLC (PJM). The first proceeding concerned a complaint filed in March 2016 (and amended in January 2017) pursuant to Section 206 of the Federal Power Act (FPA) in Docket No. EL16-49 by an ad hoc group of generating companies, seeking an expansion of PJM's Minimum Offer Price Rule (MOPR) to include existing capacity resources to mitigate the alleged capacity price suppression impacts of state programs that provided a guaranteed stream of revenue to owners and operators of certain existing nuclear generation facilities in exchange for Zero Emissions Credits (ZECs) from those facilities.

The second proceeding concerned a filing PJM made in April 2018 pursuant to Section 205 of the FPA in which PJM offered to FERC two alternative proposals (referred to as a "jump-ball" filing) regarding changes to the MOPR. The first alternative (favored by PJM) was a "Capacity Repricing proposal" under which PJM would run a two-stage annual capacity auction. In the first stage, a capacity resource receiving a "Material Subsidy" (as defined in PJM's filing) would be allowed to clear based on its submitted offers, *i.e.*, its offer price would not be subject to a MOPR. In the second stage, PJM would re-run the capacity auction using the same demand curve but with a new supply stack that would reprice the offers of a resource receiving a Material Subsidy based on administratively-determined reference prices; *i.e.*, the subsidized resource's offer would still clear but its offer price would be subject to a MOPR, which would result in a higher market clearing price. The second alternative (favored by the Independent Market Monitor for PJM) was to expand the MOPR, what PJM referred to as the "MOPR-Ex," to include new and existing resources that receive a Material Subsidy, subject to certain exemptions.

The Commission's Order (1) rejected both of PJM's proposed alternatives, (2) granted in part and denied in part the generators' complaint, and (3) instituted a new Section 206 proceeding in Docket No. EL18-178 with expedited paper hearing procedures. The Commission also consolidated the records of the previous proceedings, and established a refund effective date in Docket No. EL18-178 as of the date of publication in the Federal Register of the notice of the institution of this new complaint proceeding. The two Democratic Commissioners (Commissioner LaFleur and Commissioner Glick) dissented, and Commissioner Powelson (one of three Republican Commissioners, who recently announced his impending departure from the Commission) issued a concurrence.

The Commission offered preliminary findings and conceptual proposals, stating that circumstances have changed and the existing MOPR (which only applies to new natural gas-fired generation resources and not existing capacity resources) no longer addresses the potential price suppressive effects of state subsidy programs for state-preferred resources, such as the ZEC programs and Renewable Portfolio Standards programs. The Commission proposed that the MOPR be expanded to apply to all capacity resources (new and existing, and including renewable generation and demand response resources) that are receiving state subsidies that could result in capacity resources submitting artificially low offer prices in the PJM capacity market that could, in turn, suppress clearing prices in that market.

At the same time, the Commission provided that it did not want to interfere with the ability of states to prefer certain resources, and simply sought to react to those so-called subsidies by expanding the mitigation measures. Accordingly, the Commission also proposed allowing capacity resources to opt out of participating in the PJM capacity market through a resource-specific Fixed Resource Requirement Alternative (FRR Alternative). Under the proposed FRR Alternative, a subsidized capacity resource and a commensurate amount of load could choose to be removed from the PJM capacity market altogether, so that this capacity resource and its accompanying load would not in and of themselves impact clearing prices in the PJM capacity market.

The Commission acknowledged that its proposals to bifurcate the PJM capacity construct will require certain details to be fleshed out before they may be implemented. The Order specifically identifies the following issues that would need to be evaluated in the paper hearing proceeding in Docket No. EL18-178:

- The scope of out-of-market support that would be mitigated (and eligible for the resource-specific FRR Alternative)
- How to identify the load to be removed from the demand side of the PJM capacity market auction associated with resources electing the FRR Alternative
- The length of time for which resources that choose the FRR Alternative must remain out of the PJM capacity market
- How to address resources with split ownership
- Whether any exceptions to the MOPR should exist (*e.g.*, self-supply for public power)
- What changes to the demand curve may be required, including relating to locational resource adequacy
- Whether there are scenarios in which the resource-specific FRR Alternative could affect the competitiveness of the capacity market clearing prices

- Whether any transition mechanisms would be appropriate
- How these market changes should interact with the FERC's fuel security initiatives and federal sources of out-of-market support
- Whether to incorporate the administratively-determined MOPR reference prices (to replace the offer prices of subsidized resources) from PJM's MOPR-Ex proposal or establish different MOPR reference prices

The Commission noted that the paper hearing would address the just and reasonable replacement for PJM's existing MOPR, including not only the proposals the Commission offered but any other proposal that may be presented. The first round of testimony, evidence, and/or arguments must be filed in the paper hearing proceeding by August 28, 2018, and reply testimony, evidence, and/or arguments must be filed by September 27, 2018. The Commission noted that it expects to issue an order in the paper hearing proceeding by no later than January 4, 2019.

There remain significant questions about how the expanded MOPR and FRR Alternative, as proposed in concept by the Commission to replace PJM's existing MOPR, would work in practice. Other proposals could also be presented in the paper hearing proceeding. It remains unknown whether and how any proposals that are considered in the paper hearing proceeding will be reflected in the Commission's ultimate decision in this proceeding.

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Endnotes

[1] Calpine Corporation, et al., 163 FERC ¶ 61,236 (June 29, 2018)