"Beneficiary Pays" Allocation Methodology

EMU Phase 2 Proposal

Executive Summary

Under this proposal, uplift would be allocated on an RTO-wide basis, divided by East and West, to load, under the "beneficiary pays" allocation theory. The proposal could also be broken down to a more granular, zonal level. It would retain both DA and RT allocations, and the marginal line loss surplus would be allocated to load. That surplus could also be netted against uplift before being allocated to load instead of a *de facto* netting through the application of an uplift charge and MLSA credit to an entity.

There are two broad allocation methodologies that are FERC approved: Cost Causation and Beneficiary Pays. Most of the other phase two proposals attempt to allocate uplift on a variation of cost causation principles with different degrees of granularity. If the Notices of Proposed Rule Making in the price formation docket are any indication, then the FERC is looking to increase the amount of granularity in the electric markets. Simultaneously PJM has expressed concern with a granular and therefore complicated allocation methodology. If simplicity is a goal, then the best option is another FERC approved allocation methodology, beneficiary pays.

Uplift is a symptom of poor price formation. If the price of electricity was correct there would be very little, if any, uplift. If prices were correct the cost of reliably operating the system would be included in the Locational Marginal Price. Uplift occurs when prices are not sufficient to cover the cost of system operations. The only beneficiary of artificially suppressed prices is load. Therefore, load as the beneficiary of suppressed prices should pay for uplift that occurs due to prices being too low to reliably operate the system.

Load is also the recipient of the marginal loss over collection, and under the "beneficiary pays" methodology described above, should be the only recipient of such credits to balance its payment of uplift. The credit load received for losses was actually greater than the uplift cost in 2015. In 2015 the credit that was paid to load was $336.3m, while during the same period, the total uplift in PJM was $314.2m