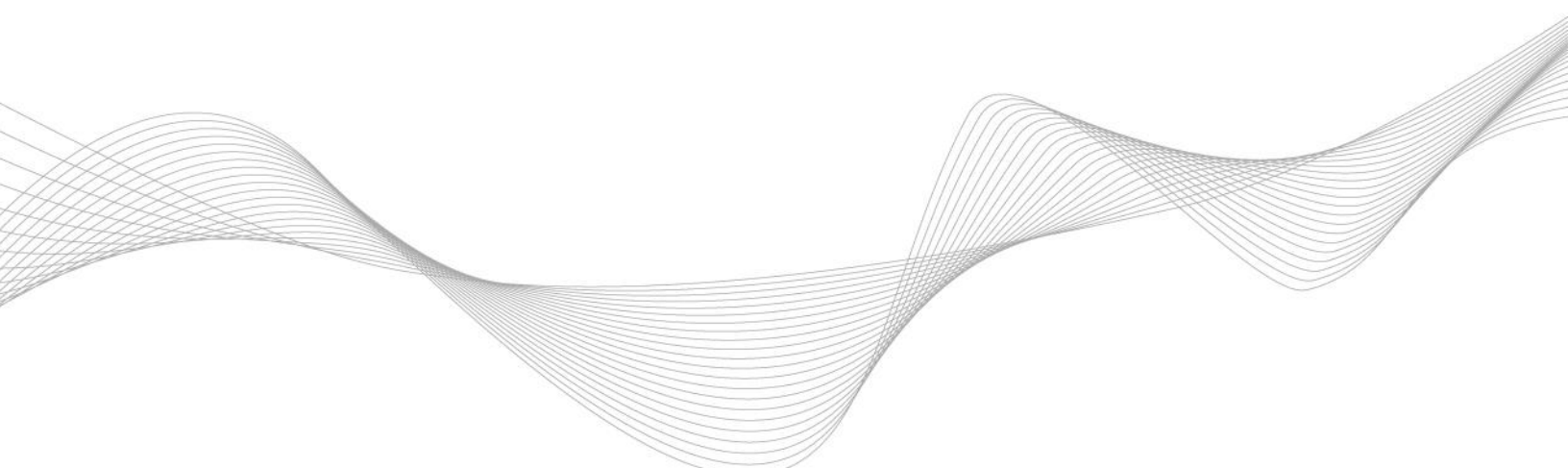




**Financial Market Reform Project
Position Paper:
Due Diligence & Assessment Criteria Process**

August 2019



1 Purpose

The purpose of this position paper is to introduce process improvements for performing background checks for new Applicants seeking membership with PJM and to identify compliance requirements that existing Members must satisfy in order to retain their membership with PJM. This paper only addresses membership qualifications. The creditworthiness of new Applicants and existing Members is addressed in the *Financial Criteria for Participation and Financial Surveillance Process* discussion paper.

2 Summary

In the GreenHat report, the consultants recommended that PJM build a customer awareness program that goes beyond market procedures and rules. Specifically, recommendation C1 suggests that background checks should be performed for any applicant seeking PJM membership.

This paper specifies the information Applicants must provide and establishes criteria they must satisfy to become a PJM Member. The paper also specifies the requirements that existing PJM Members must satisfy in order to maintain their membership in PJM and comply with the same information disclosure and criteria. It should be considered along with the PJM position paper on *Discretion to Deny or Revoke Trading Rights* and the discussion paper on *Financial Criteria for Participation and Financial Surveillance Process*.

3 Initial Disclosure of Information

PJM's governing documents have differing information disclosure requirements for Applicants and Members. PJM's current Operating Agreement obligates Applicants to satisfy all the requirements for membership but does not explicitly require them to disclose any prior or current investigations and bankruptcies, even though this information is solicited during the online application process. Alternatively, Attachment Q of the Tariff requires each Participant to provide information of any known material litigation, commitments or contingencies as well as any current or prior bankruptcy declarations or material defalcations by the Participant, or its predecessors, subsidiaries or Affiliates. The Tariff also requires Participants to disclose the existence of any ongoing investigations.

In order to remedy these inconsistencies and to gain more awareness about all entities seeking membership with PJM, Applicants will be required to submit more information than they are currently required to submit. Specifically, Applicants will be required to provide the following:

- List of Principals, who are individuals with the following roles and responsibilities:
 - The sole proprietor of a sole proprietorship
 - A general partner of a partnership
 - A manager, managing member or a member vested with the management authority for a limited liability company or limited liability partnership
 - Any person or entity that:
 - Is the direct owner of 10 percent or more of any class of an organization's equity securities
 - Has directly contributed 10 percent or more of an organization's capital
 - A director, president, chief executive officer, vice president, secretary, treasurer, operating officer, risk officer, general counsel, compliance officer, financial officer, general manager, comptroller or senior officer (or equivalent positions) of a corporation or other organization

- Any person or entity that has the power to exercise supervisory authority or influence over an organization's activities
- List of officers and representatives who are authorized to sign agreements on behalf of the Applicant or Member
- List of any relevant material criminal or civil litigation involving the Applicant or any of the Principals or Affiliates of the Applicant
 - Theft, robbery, embezzlement, fraud, perjury, intentional misrepresentation and other similar crimes
- List of any past or ongoing investigations against the Applicant or any of the Principals or Affiliates of the Applicant, by the Federal Energy Regulatory Commission, the Securities and Exchange Commission, the Commodity Futures Trading Commission, any exchange monitored by the National Futures Association or any entity responsible for regulating activity in energy markets
 - Identify whether sanctions were imposed and indicate whether the sanctions are still in effect
- Written summary of any bankruptcy, dissolution, merger or acquisition of the Applicant in the preceding five years
- A list of current retail and wholesale electricity markets-related operations in the United States, other than in the PJM markets
- Certificate signed by a Principal stating that the Applicant has obtained all applicable FERC licenses and approvals
 - Market-Based Rate Authority
- Certificate signed by a Principal stating that the Applicant has either established or contracted for:
 - Risk management procedures that are applicable to participation in the PJM markets
 - Appropriate training of relevant personnel that is applicable to its participation in the PJM markets unless the Applicant represents in writing that it will not participate in the PJM markets
- Additional information needed to resolve questions or deemed necessary to aid in the application approval process.

PJM may also audit the information supplied by the Applicant. If PJM requires an audit, it will provide notice to the Applicant at least 10 days in advance of the initiation of the audit. Any expenses incurred by the Applicant due to the audit will be the responsibility of the Applicant.

Any Applicant that fails to provide this information will not be considered for membership in PJM until the required information is provided. If the Applicant fails to provide any additional information requested by PJM within 20 days, its application for membership will be rejected.

4 Ongoing Disclosure of Information

PJM's current Operating Agreement does not require existing Members to disclose any prior or current investigations and bankruptcies. To provide consistency between initial and ongoing membership requirements, PJM will now require existing Members to comply with the same information disclosure requirements as Applicants. On an ongoing basis, Members must notify PJM within 10 business days of any changes related to the information disclosure requirements. Additionally, on an annual basis, PJM will require Members to recertify the information by April 30 of each year. A Member that fails to provide this

information or other information requested by PJM will be prohibited from participating in the PJM markets until the information is made available.

5 Criteria to Become a Member

The information provided during the application process, along with any additional information that is gleaned from search queries using publically available data, will be used to determine if approval of an Applicant is in the best interest of the PJM membership.

The following criteria will be used in the determination of membership:

- Membership could be denied if the Applicant or any of the Principals or Affiliates of the Applicant were convicted of a felony as defined by the Commodity Exchange Act.
 - If any Principal of an Applicant was criminally convicted, the termination of employment or any affiliation of the Principal with the Applicant could be used as a justification to approve membership.
- Membership could be denied if there are any past or ongoing investigations against the Applicant or any of the Principals or Affiliates of the Applicant by the Federal Energy Regulatory Commission, the Securities and Exchange Commission, the Commodity Futures Trading Commission, any exchange monitored by the National Futures Association or any entity responsible for regulating activity in energy markets and whether sanctions were imposed.
 - The following mitigating factors could be evaluated to approve membership:
 - Risk management procedures have been established or contracted for that are applicable to participation in PJM.
 - Appropriate training has been established or contracted for relevant personnel, which is applicable to its participation in PJM.
 - Compliance practices and internal risk controls have been implemented to prevent reoccurrence of the activities leading to the investigations.
 - Corrective steps were taken, including but not limited to, disciplinary action or termination of employment of Principals or employees whose behavior were the root cause of or who participated in the activities leading to the investigations.
- Membership could be denied if the Applicant or any of the Principals or Affiliates of the Applicant have a previous PJM default or have defaulted in any other Regional Transmission Organization or Independent System Operator.
 - Justification could be made to approve membership if the default has been cured.

6 Criteria to Maintain Membership

The information provided on an annual basis, along with any additional information that is gleaned from search queries using publically available data, will be used to determine if PJM membership should continue or terminate. The same criteria applied to Applicants will also apply to existing Members when determining the future status of membership.