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March 17, 2015

(via email only)

Dave Anders
Facilitator, FTR/ARR Senior Task Force
Secretary, PJM MRC and MC Committees
PJM Interconnection, LLC
955 Jefferson Avenue
Norristown, PA 19403

Re: Pending Proposals to Impose Balancing Congestion and Market to Market Congestion Charges on Electricity End-Use Customers

Dear Mr. Anders:

This letter is to advise PJM and its stakeholders that the Organization of PJM States, Inc. (“OPSI”)¹ opposes proposals being discussed before the FTR/ARR² Senior Task Force that would make revisions in PJM markets to require end users to fund Balancing Congestion and Market to Market (“M2M”) charges. Currently, Balancing Congestion and M2M payments are included in the total congestion revenue used to fund FTRs. Removal of these components from the FTR revenue calculation would impose upon electricity end-users an unjustified subsidy for the benefit of FTR holders while not addressing the underlying causes of FTR revenue inadequacy. We therefore recommend that the current treatment of Balancing Congestion and M2M payments be continued.³

¹ This letter is supported by the following OPSI members: Delaware, District of Columbia, Illinois, Indiana, Kentucky, Maryland, Michigan, New Jersey, North Carolina, Pennsylvania, Virginia and Tennessee. The states of Ohio and West Virginia abstained.

² Financial Transmission Rights (“FTRs”)/Auction Revenue Rights (“ARRs”).

³ The two cost items at issue both relate to costs imposed by transmission system congestion including “Balancing Congestion”, which represents the difference between the estimated cost of transmission of electricity associated with the PJM Day Ahead Market based on PJM modeling assumptions and the actual cost of such transmission associated with the Real Time Market (i.e. reflecting the transmission system’s actual operation) and (ii) Market to Market (M2M) congestion associated with transactions to import electricity to meet PJM load from the Midwest RTO.

As an initial matter, OPSI recognizes and commends PJM on its initiatives and recent achievements regarding improvements in the funding of FTRs, and also the reduced level of energy market uplift costs. PJM has advised that FTR revenue adequacy through January 2015 is 100%.⁴ Additionally, as shown on Slide 9 of PJM's Market Report dated January 20, 2015, the level of energy market uplift costs is shown as greatly reduced from historical levels.⁵ As discussed further below, however, OPSI has significant concerns and opposes current initiatives being pursued by PJM and stakeholders to inappropriately shift costs to end-use customers.

The effect of these proposed funding modifications would be to require electricity end-use customers to pay substantial portions or all of Balancing Congestion and M2M charges whenever FTRs are "underfunded," thereby enhancing the profits of FTR holders in this PJM market. OPSI Members understand that several such proposals are under consideration. First, two such proposals have been offered by PJM that end-users contribute funds to pay 50% of Balancing Congestion and M2M or that portion of such costs associated with emergency outages shown to be underfunded by a daily FTR revenue/cost analysis, in either case only where FTR underfunding is also shown to be present on an annual basis. Second, proposals have been offered by financial market participants and generator affiliates that end-users pay 100% of these costs. OPSI Members oppose these FTR Market modifications, first, because the FTR Market is a discrete market which should not be subsidized by end-use customers⁶. Also, the FTR market primarily supports financial transactions and the market activities of Financial Market Participants, not end-use customers.⁷ Finally, to the extent that FTR transactions involve end-use customers, only a subset of such customers (specific ARR holders) would be benefitted by the balancing congestion/M2M payments that would be made by all end-use customers as proposed most recently by PJM. Moreover, OPSI Members are aware of, and find unpersuasive, the arguments that have been presented to the FTR/ARR Senior Task Force that these funding modifications are equitable to end users. Clearly, the added costs to end use customers, by transferring these costs could be quite large, *i.e.* at present an estimated \$114 million on a partial year basis.⁸ In past years, with less attention to proper outage modeling accuracy, the magnitude of ARR allocations and due to greater weather extremes, such FTR underfunding related costs approximated and even exceeded \$300 million.⁹

⁴ See <http://pjm.com/~media/committees-groups/committees/mc/20150120-webinar/20150120-item-09a-markets-report.ashx> -- (Slides 33-36); PJM Solutions Package Presentation "FTRSTF" (March 5, 2015) at <http://www.pjm.com/committees-and-groups/task-forces/ftstf.aspx>.

⁵ *Id.* at Slide 9.

⁶ See FTR/ARR Matrix Packages 10, 11, 17 and 18 (available at <http://www.pjm.com/committees-and-groups/task-forces/ftstf.aspx>); PJM Solution Package Presentation – FTRSTF (March 5, 2015) at <http://www.pjm.com/committees-and-groups/task-forces/ftstf.aspx>.

⁷ 2014 Third Quarter State of the Market Report at p. 412; 2013 State of the Market Report at p. 362. 70 to 80% of transactions in the FTR market are undertaken by Financial Market Participants.

⁸ See "FTR and Balancing Congestion" at Slide 3, columns Balancing Congestion and M2M, a presentation prepared by PJM and presented to OPSI at the Joint OPSI/PJM February 9 Teleconference. <http://pjm.com/~media/committees-groups/state-commissions/private-state/20150209/20150209-agenda-2-financial-transmission-rights.ashx>

⁹ *Id.*

PJM, Generators and Financial Market Participants, first proposed this strategy in 2013, in a proceeding before the Federal Energy Regulatory Commission (“FERC”). In FERC Docket No. EL13-47, the PJM Independent Market Monitor (“IMM”), supported by several OPSI Members, argued that FTR holders are the appropriate entities to bear these costs, as they are the ones who value FTRs in the market and can thus best reflect any underfunding in FTR market value that they agree to pay for these instruments.¹⁰ FERC accepted the IMM position and rejected the PJM/FTR Holder proposed funding modification, stating as follows:

“FirstEnergy has not demonstrated that the existing Tariff is unjust and unreasonable, and we dismiss the complaint. . . . The amount paid by FTR holders should reflect the expected value of a given FTR. Thus, if the value of FTRs is reduced by underfunding, then the FTR holders should pay less for these instruments, and will receive the value for which they have paid. . . .

FirstEnergy also does not provide evidence demonstrating why all transmission customers, who already pay for access to the transmission system, should pay for the underfunding. . . . [T]here is a rational basis for allocating real-time congestion costs [*i.e.* balancing congestion and Market to Market] to FTR holders. FTRs are based on PJM’s modeling of the transmission system. To the extent that PJM’s modeling is inaccurate, it is not unreasonable to allocate the results of that inaccuracy to the holders of the FTRs, as they are arguably in the best position to value this product. FirstEnergy has not shown that allocating these costs to other parties will create any better incentive to address the underlying causes of FTR underfunding.

First Energy essentially is arguing that the current allocation mechanism for real-time congestion costs be replaced with an equally, if not, more arbitrary mechanism. While some parties, like FirstEnergy, may benefit from such a reallocation, FirstEnergy has not shown that such a reallocation will benefit the overall market structure in PJM nor allocate costs to those that cause the costs to be incurred or have the incentive to reduce those costs.”¹¹

OPSI Members further agree with the following *additional* positions advanced by the IMM against these proposals in its 2014 *State of the Market Report* – that FTR holders have no right “to financially firm transmission service” nor to “revenue adequacy”, and thus “load should never be required to subsidize payments to FTR holders”. Rather, as the IMM explains, “loads . . . pay both day ahead and balancing congestion,” and thus “To eliminate balancing congestion from the FTR revenue calculation would require load to pay twice for congestion.”¹² Although PJM is to be commended for its work in the current FTR market year to improve transmission outage and modeling accuracy and thus to substantially reduce FTR underfunding, the proposal to transfer balancing and M2M costs to end-use customers should be rejected. Completion of recent transmission projects and modifications of ARR allocations provide no certainty as to future system conditions that may affect FTR funding levels.

¹⁰ For this reason, FTRs have remained profitable for Financial Market Participants and other FTR holders over the years.

¹¹ *FirstEnergy Solutions Corp. and Allegheny Supply Co. LLC v. PJM Interconnection, L.L.C.*, 143 FERC ¶ 61,209 (2013) at ¶s 40, 42-44. The Commission also held that FTRs are not entitled to full funding. *Id.* at ¶ 41. A rehearing petition has been filed as to this Order and has not yet been adjudicated by FERC.

¹² IMM 2014 *State of the Market Report for PJM*, Volume 2 at 436-439 (March 12, 2015).

Rather than adopting a market rule change whose clear objective is to increase the profitability of FTR transactions at the cost of electricity end users, PJM should continue to expand its efforts to improve transmission system modeling such that FTR underfunding is further improved without further reduction to future ARR allocations. OPSI members understand that such additional opportunities have been discussed at FTR/ARR Task Force meetings, and are suggested by both PJM and the IMM.¹³

Accordingly, for these reasons, and because end-use customers should not be required to subsidize market profits of FTR positions, OPSI Members strongly urge PJM and stakeholders to reject proposals to shift responsibility for Balancing Congestion and M2M charges to end use customers.

Please post this letter on the FTR/ARR Task Force web-page on the PJM website, and also on the MRC and MC web-pages on the PJM website, as an item for stakeholder consideration in preparing to address this issue at the MRC/MC April or later meetings at which discussion or voting on this matter is expected to occur.

Sincerely yours,

s/s Gregory V. Carmean

Gregory V. Carmean
Executive Director OPSI

¹³ See, e.g., IMM FTR Underfunding Education and Options (September 17, 2014) available at <http://www.pjm.com/committees-and-groups/task-forces/ftstf.aspx>.