

INSIGHTS

FERC Accepts PJM Capacity Performance Proposal

June 16, 2015

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On June 9, 2015, FERC issued an order accepting PJM's proposal to modify its forward capacity market, the Reliability Pricing Model ("RPM"®), to establish a new capacity product, the Capacity Performance Resource. PJM's proposal is designed to tighten the performance standards applicable to resources that receive a capacity obligation through the RPM and is intended to address poor resource performance that has been experienced since implementation of the RPM, especially during the 2014 polar vortex. Once implemented, PJM's proposal will impose more stringent performance standards on resources that receive a capacity obligation through the RPM, including imposing non-performance charges when resources fail to perform and bonus payments for over-performance. All capacity resources will be eligible to offer as Capacity Performance Resources, and demand resources, energy efficiency resources, capacity storage resources, and intermittent resources will be allowed to aggregate their capabilities in order to reliably perform during emergency conditions. A Non-Performance Charge will be assessed on resources who fail to perform during system emergencies. ***FERC's Changes to the Proposal*** Though FERC largely accepted PJM's proposal, it did order PJM to make the following key changes:

- FERC rejected PJM's proposed requirement that sellers make a good-faith representation that it will make investments necessary to ensure that its resource has the capability to provide energy when called upon and meet applicable operational requirements by the delivery year. FERC noted that this requirement was vague and ambiguous and could chill the participation of even well-performing resources.
- FERC rejected PJM's proposal to require market-based offers for capacity resources to be parameter limited (e.g., based on the specific physical characteristics of that resource, rather than economic and budgetary considerations) and to require start-up and notification time of 24 hours or less. FERC found that PJM's proposal may prevent resources from reflecting in its energy market offer limitations caused by legitimate, non-physical constraints (e.g., physical limitations on natural gas pipeline flows or fuel contract requirements). FERC also found that the start-up and notification time cap was unreasonable because it would not take into account unit-specific physical constraints faced by resources. Thus, the Commission directed PJM to modify its Tariff to permit resources to recover costs incurred when operating within actual constraints through make-whole payments.

- FERC required PJM to provide clarification on how it will assess the performance of external resources with and without a capacity commitment when an Emergency Action is triggered PJM-wide. FERC noted that the language of PJM's proposed revisions suggested that PJM would not calculate an expected performance value or actual performance value for resources importing into PJM during system emergencies and that such a design would be inconsistent with PJM's proposed treatment of internal capacity resources.
- FERC rejected PJM's proposal to eliminate the ability of generation capacity resources to designate offers submitted in the Day-Ahead Market as a "Maximum Emergency Offer,"² which prevents PJM from calling on the resource unless PJM declares a Maximum Generation Emergency. While PJM claimed that the existing rules unreasonably prevented it from dispatching resources in real-time, FERC found that PJM had not demonstrated that the current rules are unjust and unreasonable. Although FERC acknowledged that the existing Maximum Emergency Offer provisions may be subject to misuse, the Commission stated that the application of Non-Performance Charges to resources that designate their offers as Maximum Emergency Offers and not dispatched by PJM as a result should be subject to Non-Performance Charges.

Transition Period PJM proposed to fully implement the Capacity Performance Resource model by June 1, 2020. For PJM's capacity auctions as applicable to the 2018-19 and 2019-20 delivery years, the existing capacity market product will be reclassified as a Base Capacity product. Base Capacity Resources will be subject to Non-Performance Charges at reduced rates, and will also have an opportunity for bonus payments if they over-perform during assessment hours. PJM proposed to hold two Incremental Auctions to seek voluntary offers of Capacity Performance Resources: one for the 2016-17 delivery year, covering up to 60 percent of PJM's reliability requirement; and the second for the 2017-18 delivery year, covering up to 70 percent of PJM's reliability requirement. FERC accepted the transition proposal, finding that a five-year transition struck the right balance between providing enough time for resources to make gradual improvements and immediately increasing the incentives for performance in the energy market, and disagreeing with protests and comments that called for either a faster or slower implementation. FERC also disagreed that the transition mechanism violates the filed rate doctrine, finding that the proposal concerns prospective changes only and provided ratepayers with sufficient notice of the tariff changes. As a result of the Commission's acceptance of PJM's proposal, the Capacity Performance Product will be incorporated into the upcoming Base Residual Auction for the 2018-19 delivery year, which begins August 10th. In addition, the Capacity Performance Product will be incorporated into upcoming incremental auctions for the 2016-17 delivery year (auction begins July 27th) and the 2017-18 delivery year (auction begins August 3rd). The timeline for the upcoming auctions is available [here](#). **Next Steps** FERC's order directs PJM to file a compliance filing no later than July 9, 2015 revising its Tariff to comply with the Commission's directives. In addition, the Commission also directed PJM to make annual informational filings with the Commission addressing whether its decision to base its Non-Performance Rate on the assumption that there will be 30 hours of Emergency Actions annually accurately reflects system operation. Further, PJM must make annual filings each year for five years detailing the performance and net revenues received from the Non-Performance Charges and Performance Bonus Payments. It is unlikely that the Commission's order will be the final

word on PJM's Capacity Performance Proposal. Given the significant concerns expressed by market participants regarding PJM's proposal, it is highly likely that numerous parties will seek rehearing and clarification of FERC's order. In recent years, proposed changes to PJM's forward capacity market have resulted in protracted litigation before FERC and the courts.