

# Sustainable FERC Project

Policies for a Clean Electric Grid

February 4, 2019

PJM Board of Managers  
PJM Interconnection  
PO Box 1525  
Southeastern, PA 19339-1525

Dear PJM Board of Managers,

The undersigned Environmental Organizations write to raise two concerns regarding reform of the energy and operating reserve markets. At the January 24, 2019 Markets and Reliability Committee meeting none of the five reserve market reform proposals voted on received the requisite supermajority support to move forward. However, the Board indicated in its December 5, 2018 letter that it intends to direct PJM to file reforms under section 206 of the Federal Power Act absent such consensus. If the Board is committed to proceeding with market reforms in the immediate future, we urge the Board to require PJM's filing to address the central issues described below.

First, demand resources currently provide a significant portion of PJM's reserves, but have been neglected in stakeholder discussions on reserves market reform. We struggle to comprehend how any filing to FERC that provides substantial additional revenues to fossil-fueled generation while not accounting for low- and zero-carbon resources that *are already under obligation to provide the needed services* could be considered just, reasonable, or even complete. Second, the capacity market already compensates many resources for the obligation to provide energy and reserves. Any proposal must fully adjust for the double payments that will occur due to increases in energy and ancillary services revenues for these resources. Not only must these aspects be addressed to ensure just and reasonable rates, they are crucial steps to bringing PJM's energy market reforms in line with the power sector's transition toward decarbonization driven by economics and the reality of climate change.

PJM and its demand response providers have gone to significant effort to develop demand resources tailored to the very reserves needs the current market reform effort seeks to address. In 2014, FERC accepted PJM-proposed tariff changes<sup>1</sup> to "ensure a more efficient use of Demand Resources in a manner that will help PJM balance demand with supply in the same manner as it relies on Generation..." and, specifically, to give PJM more flexibility to "[deploy] Demand Resources in order to avoid reserve shortage conditions."

As a result of those tariff changes, nearly five thousand megawatts of demand response resources with the ability to respond in a 30-minute timeframe are currently committed in the capacity market.<sup>2</sup> An additional four thousand megawatts of demand response currently provide reserves

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<sup>1</sup> PJM Interconnection L.L.C., Docket No. ER14-822 (Dec. 24, 2013). PJM's transmittal letter in that filing lays out a case for operational flexibility of demand resources that is highly relevant today.

<sup>2</sup> James McAnany, *2018 Demand Response Operations Markets Activity Report* at 6 (January 20, 2019).

available with longer notice or under emergency conditions<sup>3</sup>. We note the amount of demand response nearly matches the six to eight thousand megawatts of 30-minute reserves contemplated in PJM proposals. Although PJM specifically proposes to increase procurement of 30-minute reserves and adopt a demand curve to provide a price signal for those reserves when needed, proposals to date neither consider the existing demand response reserves committed on the system, nor provide a mechanism to compensate those demand resources for the reserve services they are providing<sup>4</sup>.

In its December 2018 whitepaper, PJM states that its reserve pricing reforms are underpinned by several principles, including that “reserve and energy prices reflect system conditions and appropriately value scarcity” and “the actual reserve capability on the system is accurately measured.” These principles are not achieved by ignoring existing resources that have the precise purpose of balancing the grid during conditions approaching scarcity. Any reserve market reform that does not fully incorporate the reserves value of capacity demand resources will inflate the price of energy and reserves, create false scarcity conditions, and erode price discipline in the markets for these service.

It is common wisdom that a well-functioning power market requires participation by both supply and demand<sup>5</sup>. The thousands of megawatts of demand response capacity currently providing reserves in PJM are a result of a decade-long effort by PJM and its stakeholders towards that end. PJM is well positioned to implement a reserves market that fully incorporates loads’ ability to respond to operational needs<sup>6</sup>. We urge the Board to continue PJM’s tradition of leadership in market design by doing so.

We are also deeply concerned that PJM’s proposal does not adequately address the double payments that result from its reserve pricing reforms. PJM agrees that reforms are likely to increase energy and reserve market revenues such that it is appropriate to adopt corresponding adjustments to the offsets for such revenues in the capacity market.<sup>7</sup> Absent such conforming tariff changes, base residual auction clearing prices reflect a smaller offset than actual energy and reserve revenues. The Market Monitor estimates this will result in overcompensation on the order of \$1.5 billion a year. We agree with the Organization of PJM States, Inc. that this “would result in ratepayers paying twice for the same product or service” and “such an outcome is not just and reasonable.”<sup>8</sup> Filed reserve pricing reform must fully eliminate such double payments, both during any transition period and in the long-term.

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<sup>3</sup> *Id.*

<sup>4</sup> See “Demand Resources Participation in 30 Minute Reserves,” presented at Jan 17, 2019 EPFSTF meeting. PJM contemplates allowing demand resources to optionally provide 30 minute reserves, but does not address the reserves provided by pre-emergency or emergency demand resources.

<sup>5</sup> See, e.g., FERC Order 719 at 16.

<sup>6</sup> Indeed, we believe incorporating capacity demand response into the supply of 30-minute reserves would require no changes to demand resources’ current tariff obligations.

<sup>7</sup> PJM’s December 18 proposal specifically recognizes that the historic Energy and Ancillary Services Offset, the current mechanism for ensuring capacity payments are net of other anticipated revenues, “would likely underestimate future Energy and Reserve Market revenues.”

<sup>8</sup> Jan. 23, 2019 letter of Organization of PJM States, Inc. to PJM Board.

Addressing these flaws of the reform are not only crucial to safeguarding just and reasonable rates, but to ensuring PJM remains a leader in grid operations as the power sector rapidly shifts to a decarbonized future. PJM's energy reserve reform package would unacceptably delay fully and efficiently utilizing the capabilities of clean energy technologies to serve system needs. Over 68% of load served in PJM is located in states that have clean or renewable energy targets that become increasingly ambitious in coming years.<sup>9</sup> It is no longer acceptable for consideration of clean energy technologies to be relegated to an afterthought. PJM can only achieve its mission of efficient, reliable wholesale markets that meet customer needs by developing solutions that recognize technological advances and support PJM states' decarbonization goals.

Sincerely,

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<sup>9</sup> For example, Pennsylvania, nearly 20% of PJM load in 2017-18, announced a target this past year to reduce greenhouse gas emissions by 80% by 2050, while New Jersey, around 10% of load, enacted a 50% renewable energy target by 2050, and a roadmap to achieve 100% clean energy by 2050.