

AUTHORITY FOR PJM TO REQUIRE PARTIES PROPOSING TO SELL DEMAND RESOURCES IN RPM AUCTION TO DEMONSTRATE THAT THEIR OFFERS ARE SUPPORTED BY REASONABLE EXPECTATION THAT THEY WILL HAVE IN PLACE FOR THE DELIVERY YEAR THE CAPABILITY TO PROVIDE THE COMMITTED LEVEL OF REAL REDUCTIONS IN PHYSICAL LOAD

Capacity Market Sellers¹ in PJM’s Reliability Pricing Model (“RPM”) are required to base their Capacity Resource offers on real, identifiable, firm resources. The RAA, for example, requires that all Load Serving Entities that offer resources into the capacity auction shall arrange for “specific, firm Capacity Resources” that must be capable of fulfilling capacity commitments “on a firm basis without interruption for economic conditions.” RAA, section 7.6. Those specific firm resources must also have “other characteristics that are necessary to support the reliable operation of the PJM Region,” expressly referencing in that regard RAA Schedules 6, 9, and 10. *Id.* Schedules 9 and 10 of the RAA prescribe requirements for establishing, respectively, the capability of specific generation resources to provide the committed levels of capacity, and the firm deliverability of specific generation resources to PJM system load from either inside or outside the PJM Region. Schedule 6 of the RAA specifies in detail the criteria for Demand Resources and states that only resources that qualify under those criteria may be offered in the RPM auctions. RAA, Schedule 6, section A. Among other requirements, Schedule 6 provides that PJM presently recognizes only three types of Demand Resources, i.e., Direct Load Control, Firm Service Level, and Guaranteed Load Drop, and it specifies the particular type of physical load management involved with each of those three types of Demand Resources. *Id.* at section H. Demand Resources, moreover, are expressly defined in section 1.13 of the RAA as resources “with a demonstrated capability to provide a reduction in demand or otherwise control load in accordance with the requirements of Schedule 6.” Thus, a “Demand Resource,” i.e., the product that a Demand Resource provider offers into an RPM auction, is a commitment to provide a real reduction in physical load attached to the PJM system.

FERC has recognized that the PJM capacity construct requires specific identifiable firm resources. For example, when PJM integrated the Commonwealth Edison Company (“ComEd”) control area in northern Illinois into the PJM Region, a number of Load Serving Entities (“LSEs”) in that control area objected to PJM’s “more stringent” capacity rules that, among other things, would “bar[]” their current practice of meeting capacity obligations with arrangements “that do not specify the generation units that will provide the capacity.”² FERC denied those protests and accepted PJM’s position that “designated capacity resources must be capable of being delivered” to the

¹ Capitalized terms used in this document have the meaning provided in the PJM Open Access Transmission Tariff (“Tariff”) or Reliability Assurance Agreement among Load Serving Entities in the PJM Region (“RAA”).

² *PJM Interconnection, L.L.C.*, 106 FERC ¶ 61,253, at PP 43, 50, *reh’g denied in relevant part*, 109 FERC ¶ 61,094, at PP 30-31 (2004).

ComEd area in emergencies.³ FERC accepted PJM’s proposal to work with the affected LSEs “to develop mutually agreeable lists of underlying generating units with enough specificity to meet [PJM’s] needs,” while expressly citing PJM’s caveat on that process that “firm liquidated damages contracts cannot be relied upon to support service to all loads in an emergency because they would provide a guarantee only of financial compensation, not energy.”⁴

Capacity Market Sellers cannot ignore these requirements when they submit Capacity Resource offers into the RPM auctions. To the contrary, they must abide by them. A Capacity Market Seller that offers a “Demand Resource” into the auction is representing that it has, or at a bare minimum reasonably expects to have, a “Demand Resource,” i.e., a demonstrated capability to provide a reduction in physical load at the levels specified in its offer. Parties that submit Demand Resource offers knowing that they will not have the capability specified in their offers, or that have not exercised due diligence to support a reasonable expectation that they will have the capability specified in their offers, *are proceeding in reckless disregard of the explicit requirements of the governing agreements*. Such conduct would be inconsistent not only with the explicit requirements of the RAA, but would also be inconsistent with such market participant’s obligation under the PJM Operating Agreement (“OA”) to “follow Good Utility Practice;” and to “cooperate with [PJM] as necessary for the operation of the PJM Region in a safe, reliable manner consistent with Good Utility Practice.” OA, Schedule 1, section 1.7.4(a).

PJM has the authority and responsibility under the existing agreements to adopt implementing procedures that prevent such conduct. One of the “primary” responsibilities of the PJM Board is to ensure that PJM performs its duties in a manner consistent with “the safe and reliable operation of the PJM Region.” OA, section 7.7(i). To ensure PJM is able to discharge this obligation, market participants agree to provide PJM not only all information specified in the governing agreements, but also “such other information as the Office of the Interconnection may reasonably require for the reliable and efficient operation of the PJM Region.” OA, Schedule 1, section 1.7.4(d).

In the present case, PJM’s review of the available data raises a very serious concern that Demand Resources offered into the upcoming Base Residual Auction could exceed the Demand Resource capability that is supported by demonstrated historic load reduction measures, and may not reflect practical levels of demand response penetration. Under these circumstances, PJM is authorized, and indeed obligated, by the existing

³ *Id.* at P 49.

⁴ *Id.* at P 50 & n.27. *See also Midwest Independent Transmission System Operator Inc.*, 125 FERC ¶ 61,061, at P 19 (2008) (“power purchase agreements with liquidated damages provisions” do not satisfy the purpose of a resource adequacy plan, which is “is to ensure that enough MWs are available to be delivered in peak conditions. . . . A financial payment is not a demonstration of resource availability under peak demand conditions”).

agreements, to seek to verify that parties offering Demand Resources presently have, or reasonably expect (following diligent inquiry) to have, load reduction capabilities at the levels specified in their offers that satisfy the requirements of the governing agreements. PJM therefore proposes to obtain from parties intending to submit Demand Resource offers certain data to support their claimed Demand Resource levels.⁵ To accommodate the business practices of Demand Resource providers that may not have all arrangements in place at the time they submit their Demand Resource offers, PJM also is requesting certifications that providers, after exercising due diligence, reasonably expect to have the physical load reduction capabilities in place at the level needed to support their offer.

⁵ To tailor the information requirements to the need for the information, PJM will implement two tiers: more extensive data in areas with greater risk of duplicative or overlapping Demand Resource offers; and a lesser level of data in all other areas.