

RPM: Qualifying Transmission Upgrade Credit Requirement

Problem / Opportunity Statement

H-P Energy Resources LLC, a developer of Qualifying Transmission Upgrade (QTU) projects, is proposing this Problem Statement, accompanying the Issue Charge, to address the anomalous situation of the credit requirement for a QTU being a multiple of the total project cost of the QTU, as well as the security being coupled to unrelated credit requirements (*e.g.*, planned generation). The anomaly is compounded by the *uniquely* low performance risk of a QTU relative to other RPM resources (existing generation, planned generation and demand response).

This is an important matter to resolve because an excessive credit requirement discourages entry of new resources and is a barrier to entry that artificially raises RPM prices in constrained Locational Deliverability Areas (LDAs). What needs to be addressed is how to determine the correct pre- and post- auction security and how the security requirement should be balanced between coverage risk and performance risk.

Illustration of the Problem

Assume a potential QTU project involving a simple reconductoring upgrade of a 230 kV double circuit to be built by the Transmission Owner and that this project would increase the Capacity Emergency Transfer Limit (CETL) into an LDA by 900 MW. The PJM feasibility/impact study indicates total project cost of \$7 million. However, under the current credit requirement, based on the last BRA, the pre-auction security requirement would be 0.3 Net CONE or \$32.57 million. This credit requirement is more than 400% of total project cost, and is an unnecessary barrier to the merchant developer's ability to offer the project as a QTU in the next BRA.

Please note the contrast with a new generating plant of 900 MW that could have a total project cost in the neighborhood of \$1 billion. A credit requirement of \$32.57 million to secure future availability of a plant costing \$1 billion (credit at 3.3% of project cost) would not appear excessive.

Different Credit Requirement for Other Transmission Projects in PJM

One relevant parallel is the credit requirement for major transmission projects selected in the competitive process being implemented under Order No. 1000. While that credit requirement is still in discussion, PJM proposed it to be 10% of the total project cost. <http://www.pjm.com/~media/committees-groups/task-forces/rpptf/20131017/20131017-ferc-order-1000-security-presentation.ashx>. It does not appear rational for a major RTEP transmission project "bid" by a third party to have a credit requirement of 10% of total project cost, while a relatively minor QTU transmission upgrade would have a credit requirement of more than 400% of total project cost. Similarly, as discussed in more detail below, while there is no bar to existing generation resources retiring after having entered into a performance obligation for a future year, such resources have zero credit obligation.

What Is the Relevant Risk?

The question has been raised as to whether the credit requirement should be determined based on the risk of non-payment of the deficiency penalty rather than the risk of non-performance itself. RPM credit policy in OATT Attachment Q is framed in terms of the “risk of non-performance” of the resource, not the risk of non-payment of the deficiency penalty.

RPM credit policy appropriately focuses on the risk of non-performance itself. The deficiency penalty is not an end in itself – instead it is intended to reasonably assure performance.¹ Imposing a credit requirement that is a multiple of the amount that reasonably assures performance serves no legitimate purpose and is a barrier to entry.

Furthermore, if the determining factor were to be risk of non-payment of the deficiency penalty, rather than risk of non-performance, then there would be no basis for excluding existing generation from a credit requirement. Cleared existing generation that does not show up in the Delivery Year is subject to a deficiency penalty like any other resource yet posts no security. The existing generation risk is not simply theoretical. There are many thousands of MWs of existing generation that clear in a BRA, and then are “replaced” and do not show up in the Delivery Year. These present, at the time of the BRA, a risk of non-payment of a deficiency penalty for not showing up in that BRA’s Delivery Year. Therefore, if the credit requirement must be applied to all resources for which there is risk of non-payment of a deficiency penalty, then existing generation should be subject to the credit requirement.

Role of Uniformity

It also has been suggested that the credit requirement should be uniform. This suggestion disregards the fact that the largest category of resources in RPM, existing generation, has no credit requirement. This exemption has been provided on a view that all other resources have a “materially increased risk of non-performance” (OATT Attachment Q).

However, QTUs have *less* risk of non-performance than existing generation because PJM determines that a QTU will be in service for the Delivery Year in the course of certifying the QTU for participation in the BRA, and all performance is in the hands of regulated Transmission Owners with very high performance records. And unlike other RPM resources, PJM can order transmission upgrades in the UCSA stage in the event of a resource developer default putting system integrity or reliability at risk. In contrast, existing generation has a non-negligible risk of non-performance as shown by the many thousands of MWs that clear in a given BRA and do not show up in the Delivery Year, and PJM cannot order generation.

Thus, if uniformity were the overarching consideration QTUs should have a similar credit requirement as existing generation (relative to which it is even less risky) – not the same credit requirement as other resources.²

¹ It should be noted that the deficiency penalty is a function of the project cost of a generator – the Net CONE of a generator. As a threshold matter, a generator-based deficiency penalty should not be the basis of the credit requirement for a transmission upgrade.

² Uniformity in treatment of resources is not necessarily an overarching principle in RPM. QTUs have been disadvantaged in various ways: (1) QTUs are not eligible to participate in Incremental Auctions, (2) QTUs are not eligible for the New Entry Price Adjustment, (3) a Facilities Study agreement instead of a System Impact Study agreement is required for BRA participation, and (4) the deficiency penalty is five times that for other resources. Thus, the RPM construct has not treated uniformity as an overarching principle in rule design, and any value in uniformity should not trump rational recognition of resource differences. As PJM noted in recent comments in Docket No. ER13-2108-000, filed December 3, 2013 (page 10): “... comparability does not require identical rules; comparable rules that appropriately address inherent differences between resource types are acceptable.”