Introduction

This document provides additional information for PJM stakeholders regarding the results of the 2008/2009 Reliability Pricing Model (RPM) Third Incremental Auction. The 2008/2009 Third Incremental Auction was held from January 7, 2008 to January xx, 2008.

The Third Incremental Auction

An RPM Third Incremental Auction provides capacity suppliers with a final opportunity to sell or purchase capacity for the Delivery Year through a PJM-administered auction process. Resource-specific sell offers are submitted into this auction by suppliers with excess capacity beyond what is needed to satisfy their commitments from previous auctions for the Delivery Year. All resource-specific sell offers into a Third Incremental Auction are subject to market power mitigation through the application of the Three-Pivotal Supplier Test.

Any party that desires to purchase LDA-specific UCAP for the Delivery Year may do so by submitting a buy bid in to the Third Incremental Auction. UCAP purchased in a Third Incremental Auction may be used as replacement capacity to cover Delivery Year commitment and compliance shortfalls. Those parties that do not clear buy bids in a Third Incremental Auction but still desire to purchase capacity for the Delivery Year may do so bilaterally.

A Third Incremental Auction is cleared in a similar fashion to that of a Base Residual Auction with the exception that no Variable Resource Requirement curve is utilized. The demand in a Third Incremental Auction is composed of the LDA-specific buy bids submitted by participants who wish to purchase UCAP. The relative positions of supply and demand in each region will determine the resulting cleared MW and price quantities.

Because a Third Incremental Auction provides an auction for buyers and sellers of capacity and does not procure capacity on behalf of the load in PJM, the zonal capacity prices that LSEs in PJM pay for capacity are not affected by the results of this auction. Zonal capacity prices are only affected by the Base Residual and Second Incremental Auctions. Those prices are then finalized after the ILR Certification Period.
Table 1 - 2008/2009 Third Incremental Auction Results

<table>
<thead>
<tr>
<th></th>
<th>Total Supply (MW ICAP)</th>
<th>Total Supply (MW UCAP**)</th>
<th>Total Demand (MW UCAP)</th>
<th>Cleared Demand (MW UCAP)</th>
<th>Cleared MW (MW UCAP)</th>
<th>Clearing Price ($/MW-Day)</th>
</tr>
</thead>
<tbody>
<tr>
<td>EMAAC</td>
<td>1240.5</td>
<td>1142.8</td>
<td>191.0</td>
<td>191.0</td>
<td>292.1</td>
<td>10.00</td>
</tr>
<tr>
<td>SWMAAC</td>
<td>23.0</td>
<td>20.6</td>
<td>237.5</td>
<td>20.6</td>
<td>20.6</td>
<td>223.85</td>
</tr>
<tr>
<td>RTO *</td>
<td>2491.6</td>
<td>2339.4</td>
<td>2251.8</td>
<td>1032.2</td>
<td>1032.2</td>
<td>10.00</td>
</tr>
</tbody>
</table>

* RTO supply and demand values include EMAAC and SWMAAC.
** Resource offers converted to UCAP using Delivery Year EFORd or applicable FPR and DR Factor.

Table 1 contains a summary of the offer and clearing data for 2008/2009 Third Incremental Auction. The summary includes all resources located in the RTO (including all LDAs within the RTO) and each constrained LDA separately. Each column in this table is explained in more detail in the upcoming sections of this report.

Supply in the 2008/2009 Third Incremental Auction

The 2,491.6 MW of supply offered into the Third Incremental Auction is composed of uncleared capacity from the 2008/2009 Base Residual Auction, new capacity in the form of uprates or resources were not previously capacity resources in PJM, and additional UCAP available due to an improvement in EFORd between the Base Residual and Third Incremental Auctions. Nearly half of the supply offered into the auction was from the EMAAC LDA, 1,240.5 MW, and 23.0 MW was offered from SWMAAC. All supply offers are in ICAP terms.

Each generation resource sell offer was converted to UCAP using the Delivery Year EFORd and each demand resource sell offer was converted to UCAP using the Delivery Year FPR and DR Factor. As a result, 2,339.4 MW of UCAP was offered into this auction, 1,142.8 MW from the EMAAC LDA, and 20.6 MW from the SWMAAC LDA.
Mitigation

The market power mitigation provisions in the PJM Tariff require that in each RPM auction the Three Pivotal Supplier (TPS) test is utilized to determine whether individual suppliers have the potential to exert market power. If a given supplier fails the TPS test in a given auction, all supply (with the exception of planned resources) offered by that supplier is offer-capped. In the 2008/2009 Third Incremental Auction, all suppliers in the SWMAAC LDA failed the TPS test and were offer capped. 18 out of 40 suppliers failed the TPS test and were offer capped in the RTO and EMAAC LDAs.

Demand in the 2008/2009 Third Incremental Auction

The demand in a Third Incremental Auction is composed of LDA-specific buy bids submitted by participants. The buy bids are specified in UCAP terms and if cleared are binding commitments to purchase capacity for the entire Delivery Year. There was a total of 2,251.8 MW of buy bids submitted into this auction where 191.0 MW were for capacity in the EMAAC LDA and 237.5 MW were for capacity in SWMAAC. The remaining buy bids were to purchase capacity in the unconstrained RTO.

2008/2009 Third Incremental Auction Clearing Results

In the 2008/2009 Third Incremental Auction, a total of 1032.2 MW of UCAP was cleared at a clearing price of $10/MW-Day. This price was set by the intersection of supply and demand at the specified MW and price quantity. Of the cleared MW amount, 292.1 MW were cleared in EMAAC and 20.6 MW in SWMAAC.

RTO/EMAAC Results

As seen Table 1, the 292.1 MW of cleared UCAP in the EMAAC LDA exceeds the 191.0 MW of cleared buy bids. This is a result of the large quantity of inexpensive supply available from the EMAAC LDA and the relatively small demand for UCAP from that region. However, because EMAAC is an LDA within the RTO, RTO buy bids can also be cleared with EMAAC resources if they are economic. In the case of the 2008/2009 Third Incremental Auction, the excess capacity cleared in the EMAAC LDA, 101.1 MW (292.1 MW – 191.0 MW), is used to clear RTO buy bids as it provides a lower cost solution than committing higher priced RTO supply. This occurrence also causes the price convergence between the RTO and EMAAC.

*Figure 1* shows the intersection of the combined RTO and EMAAC mitigated supply and demand curves. The plot below is truncated to show the intersection at $10.00/MW-Day.
Figure 1 – RTO/EMAAC Mitigated Supply and Demand Curves
**SWMAAC Results**

A total of 20.6 MW of UCAP cleared in SWMAAC in the 2008/2009 Third Incremental Auction. The price was set by a vertical extension of the supply curve to meet the demand at a price of $223.85/MW-Day.

The high price in the SWMAAC region is caused by a large amount of demand for a very small amount of supply. *Table 1* shows that there was 10 times the amount of demand bids to purchase capacity than there was supply offered to clear those bids. As a result, the clearing price is set at the highest price willing to be paid for those MW.

*Figure 2* on the following page shows the mitigated supply and demand curves for SWMAAC.
Figure 2 – SWMAAC Mitigated Supply and Demand Curves