

FirstEnergy's Perspective on PJM's Wholesale Electricity Markets: 2019

ADDENDUM: Q1 2019 ISSUES

This section will be updated on a quarterly basis (December 1, March 1, June 1, and September 1), whereas the main body of the report will be updated annually on September 1. The purpose of this section is to provide an overview of key FERC and PJM initiatives active in each quarter.

Executive Summary

The primary focus of this reporting period concerns attempts to reach stakeholder consensus on the proposed energy price formation changes. Stakeholders were not able to reach consensus on key issues, which forced the PJM Board to direct PJM to make a filing under its own legal authority for resolution.

Since the last reporting period, there have been changes in the Commission's composition that raise questions regarding timing and implementation of major proposed market rule changes. Commissioner Bernard McNamee was confirmed by the US Senate, filling former Commissioner Powelson's spot on the Commission. Commissioner Kevin McIntyre sadly passed away, after having stepped down from his Chairmanship due to health issues, leaving an open spot that has yet to be filled. Finally, Commissioner LaFleur issued a statement that she will step down and not seek re-nomination. Her term will expire on June 30. By law, Commissioner LaFleur can stay on the earlier of (i) the end of this session of Congress, or (ii) when a replacement is nominated and confirmed. She could also choose to leave earlier.

Capacity Market Initiatives

Fuel Security: On December 17, PJM released its report titled "Fuel Security Analysis: A PJM Resilience Initiative", consisting largely of information previously released or discussed at stakeholder meetings. In the report, PJM claimed there is no imminent threat to reliability and resilience, and that the PJM system will remain reliable into the future. PJM noted that proactive measures should be explored to value fuel security attributes via markets and recommended areas that should be studied by stakeholders. PJM plans to work with stakeholders in 2019 to examine the report and explore market-based solutions to address long-term fuel security concerns. PJM reviewed a problem statement and issue charge with stakeholders on the topic at the February 21 PJM Markets and Reliability Committee meeting.

Quadrennial Review: On October 12, PJM filed proposed revisions to its tariff resulting from the stakeholder process around the Quadrennial Review performed every four years. The filing proposes revisions to certain auction parameters, including adjustments to the Variable Resource Requirement (VRR) curve which will have the effect of significantly lowering the prices on that curve at all capacity levels. The PJM proposal also updates the technology assumed for the reference unit, which reduces Gross Cost of New Entry by over 20%. PJM requests that the proposed revisions become effective January 17. On January 15, FERC staff issued a deficiency letter in response to PJM's Quadrennial

Review filing requesting additional information regarding PJM's choice for the reference generation turbine, as well as changes to the Gross CONE calculation. PJM responded to the FERC deficiency letter on February 14.

Peak Shaving: On December 7, PJM filed its peak shaving adjustment proposal at FERC. As a result of PJM's Capacity Performance requirement that all capacity resources participate on an annual basis, some stakeholders have complained that summer-only demand response was unable to participate. Under PJM's proposal, state seasonal (summer-only) demand response programs could be recognized in the load forecast as a demand reduction, and those resources would be prohibited from participating in PJM as Price Responsive Demand, Demand Response or Economic Load Response. The result will be a reduction in the PJM load forecast, placing additional downward pressure on capacity market pricing as resources compete for less load. On February 4, FERC staff issued a deficiency letter in response to PJM's Peak Shaving Adjustment proposal. FERC staff's questions went to the types of entities and programs that are eligible for the proposed construct, limitations on double counting or recovery, the methodology for calculating the necessary load adjustment; and potential cost shifting between market participants. PJM's deficiency response is due March 6.

Market Monitor Performance Assessment Interval complaint: On February 21, the PJM Independent Market Monitor (IMM) filed a complaint under Section 206 of the Federal Power Act against PJM alleging that the current methodology for calculating the expected number of Performance Assessment Intervals (PAIs) under the PJM Capacity Performance construct is unjust and unreasonable. The IMM proposes to change the formula for calculating the Market Seller Offer Cap from $(\text{Net CONE}) * B$ to $((\text{one-sixth} * \text{Net CONE}) * B)$. This would reduce the expected PAI to 30 intervals (5 hours) per year. Units with an avoidable cost rate higher than the Market Seller Offer Cap would have to go through the unit specific review process with the IMM to offer above the new market seller offer cap. The potential impact of the Market Monitor's complaint is significant as it could drastically reduce PJM capacity market revenues, and would trigger unit specific review for many more resources.

Minimum Offer Price Rule: No activity this reporting period; still pending at FERC.

Energy Market Issues

Energy Market Price Formation: On December 12, PJM released a white paper in response to a letter to members from the PJM Board. In the white paper, PJM estimated that its proposals will increase Energy and Reserve market revenues by approximately \$1.92 billion, with an offsetting effect (*i.e.* decrease) in the capacity market ranging from \$440 million to \$1.5 billion. The net cost increase will be anywhere from 1% to 3.4%, which is not enough to provide adequate support for resilient resources. PJM estimated a 1-2% increase in costs for retail customers. PJM's Board directed PJM management to work with stakeholders on a comprehensive package for energy and reserve market reforms and determine areas where consensus can be reached by the end of January. Stakeholders worked on the issue throughout January and February, but timely consensus was not achieved. The PJM Board directed PJM management to make a filing with FERC to address the reserve procurement and pricing issues. It is expected that PJM's filing will be similar to the proposal outlined in the PJM whitepaper, but there will be no energy and ancillary services offset transition. In addition, we expect that PJM will adopt the IMM's recommendation to adjust generator forced outage rates, and the demand response cap for synchronized reserves will be raised to 50%. These needed reforms provide

modest incremental change, but fall short of the fundamental changes that are needed to support baseload electric generator units over the long-term.

Fast Start Pricing: No activity this reporting period; still pending at FERC.

Ancillary Services Market Initiatives

Regulation Market Rule change: On January 18, FERC approved PJM's request to no longer factor certain resources into its regulation market clearing price. The proposal was designed to minimize price spikes in PJM's regulation market due to a flaw in the way in which the clearing price was being calculated. FERC found that PJM's proposal solved the unique market pricing issue while having a minimal effect on the number of hours resources with an extremely low benefits factor would be prevented from clearing.

Emerging Technologies

Electric Storage Participation and Distributed Energy Resource (DER) Aggregation: On December 3, PJM submitted its compliance filing with FERC relating to energy storage. In February 2018, FERC issued Order 841, which required ISOs and RTOs to submit tariff changes to remove barriers to energy storage participation in ISO/RTO markets, and develop participation models to accommodate energy storage resources. PJM submitted two compliance filings to FERC in response to Order 841. The main filing outlines a participation model for Energy Storage Resources (ESRs) to participate in the PJM wholesale markets. A second filing was made, with a shorter acceptance timeline, to start the accounting processes necessary to accommodate Order 841. FERC approved PJM's ESR-accounting proposal on February 1. PJM requested that FERC issue an order on the main ESR filing by May 30.

Other

Stakeholder Super Forum: On January 30, PJM held its second Stakeholder Super Forum. The Super Forum will meet monthly through summer to discuss ways to improve the PJM stakeholder process. The Super Forum will look at prioritization of meetings (including limiting the number of topics stakeholders work on at a given time), resolving transparency issues (voting reports, etc.) and developing a new process for dealing with contentious issues that are not likely to find resolution through the stakeholder process. It is not expected that the Super Forum process will delve into issues on the balance of voting power.

GreenHat Update: On January 30, FERC denied PJM's request for a waiver of certain Financial Transmission Rights (FTR) liquidation rules in connection with the July 2018 FTR auction. The request was filed as part of a package of steps PJM and members implemented last year to mitigate the impact of the June 2018 default of GreenHat Energy LLC. The order requires PJM to rerun the July 2018 FTR auction and to replace the July 2018 results with the auction results that would have included the liquidation of the GreenHat portfolio for September 2018 through May 2019. The order also directs PJM to unwind the default allocation and related settlements from September 2018 through January 2019. According to PJM, the projected impact of this order would:

- Increase the total default allocation assessments to members by about \$250 - \$300 million, resulting in a revised total default reference of at least \$430 million;
- Likely place a number of members in breach of their collateral requirements of PJM's credit policy and require them to fulfill a collateral call within two business days; and

- Require PJM to resettle every FTR portfolio impacted by rerunning and revising prior cleared FTR auction results.

On February 21, PJM filed a motion to stay the January 30 order pending the outcome of its expected request for clarification and/or rehearing filing. Requests for rehearing in response to FERC's January 30 order are due March 1.

[NERC report:](#) On December 18, NERC released the final version of its report titled "Generator Retirement Scenario" analyzing a stress-test scenario of generator retirements. The report found that generation retirements in the scenario could reduce planning reserve margins to levels below reference levels, that infrastructure (gas pipeline and electric transmission) would need to be built in a short timeframe, and that there are backstop mechanisms in place (capacity markets, RMR's, etc.), though the backstop mechanisms may not be effective in securing long-term supply or mitigating issues. The report recommends a review of planning processes, incorporation of fuel security analysis in generator retirement assessments and additional flexibility for permitting processes to allow for quicker builds of needed infrastructure. The final report is not as extreme as a draft report leaked in September, both in terms of the number of retirements analyzed and the conclusions and recommendations.

[NIAC report:](#) On December 11, the President's National Infrastructure Advisory Council (NIAC) released a report titled "Surviving a Catastrophic Power Outage, which examines the United States' ability to respond to and recover from an outage "of a magnitude beyond modern experience, exceeding prior events in severity, scale, duration, and consequence." NIAC was tasked with considering an outage that extended beyond days and weeks, out to months or even years, while affecting large portions of the country. NIAC found that the United States' existing plans, response resources, and coordination strategies would be outmatched by an event of this severity. NIAC recommends designing a national approach for catastrophic power outages and mitigating cross-sector interdependencies and cascading failures.

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Summary: Notice of Quarterly Update Pursuant to Section V.C.2. of the Third Supplemental Stipulation and Recommendation electronically filed by Mr. Scott J Casto on behalf of The Cleveland Electric Illuminating Company and The Toledo Edison Company and The Ohio Edison Company