

FirstEnergy's Perspective on PJM's Wholesale Electricity Markets: 2021

Q4 2021 ISSUES

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

Executive Summary

PJM and its stakeholders are continuing the trend of discussing broad, holistic reforms in PJM's capacity, energy, and ancillary services markets. Phase II capacity market issues will largely be addressed through a new stakeholder group, the Resource Adequacy Senior Task Force. PJM continued efforts toward the Quadrennial Review of its capacity auction curve. PJM resumed activities in the Energy Price Formation Senior Task Force after a 2-year hiatus to discuss the potential adoption of a Circuit Breaker, should prolonged scarcity pricing take place—as was experienced in ERCOT in the Winter of 2021. Stakeholders now have several avenues to discuss various market reforms, including a new FERC rulemaking proceeding related to reactive power compensation and a proposal to create a new task force to address broad market reforms at PJM. Finally, PJM members are continuing to make progress on reforms to Auction Revenue Rights and Financial Transmission Rights markets.

Capacity Market Initiatives

PJM MOPR Filing: PJM employed the Critical Issue Fast Path (“CIFP”) process, an accelerated stakeholder process, to develop its Minimum Offer Price Rule (“MOPR”) reform proposal. Under the commonly named Focused MOPR, market participants are asked to sign attestations declaring they are not receiving state subsidies conditioned upon clearing in any PJM capacity auction and that they are not exercising buyer side market power. If a Capacity Market Sellers are suspected of exercising market power, PJM and the IMM will conduct “fact-specific, case-by-case reviews”, and referrals will be made to FERC for a final determination. On September 29, 2021, PJM's Focused MOPR filing became effective by operation of law as FERC did not act within the 60-day statutory deadline. Chairman Glick and Commissioner Clements issued a joint statement noting their support for PJM's Focused MOPR, while Commissioners Danly and Christie outlined the reasons they find PJM's Focused MOPR unjust and unreasonable.

PJM Market Seller Offer Cap: On September 2, 2021, FERC issued an order finding that a Unit-Specific Avoidable Cost Rate (“ACR”) is an appropriate way to calculate the Market Seller Offer Cap (“MSOC”) and directing PJM to submit a compliance filing establishing new pre-auction activity deadlines within five business days of the order and to make an additional compliance filing within 30 calendar days of the order revising its tariff. PJM made the first of these two filings on September 10, 2021, recommending, amongst other things, that the upcoming auction for the 2023/2024 Delivery Year

be delayed for 55 days and providing a schedule to extend the deadline dates for certain pre-auction activities. On October 4, 2021, PJM submitted its compliance filing with proposed Tariff revisions. In a separate filing on the same day, PJM submitted a Request for Clarification and Request for Rehearing in the matter. On October 25, 2021, FERC issued an order accepting PJM's revised pre-auction deadlines and granting PJM's waiver request for a delay of certain upcoming auctions.

PJM Capacity Reforms: During this period, PJM held two capacity workshops to discuss the scope of the second phase of broader capacity market reforms, the distribution of the work amongst a few stakeholder groups, and the proposed timeline for each identified issue. PJM had previously proposed to establish a Capacity Market Design Senior Task Force ("CMDSTF") to act as a managing group for the various issues that were to be worked through other stakeholder groups but found little support as stakeholders were not interested in broad distribution of the issues across stakeholder groups. Rather, stakeholders were largely supportive of forming a new stakeholder group, the Resource Adequacy Senior Task Force ("RASTF"), to work on Phase II reforms. The RASTF's charter was approved at PJM's October 10, 2021 Markets and Reliability Committee meeting and the group held its initial meeting on October 22, 2021.

Quadrennial Review: PJM's Open Access Transmission Tariff ("OATT") requires PJM to review the shape of the Variable Resource Requirement ("VRR") Curve, the calculation of the Cost of New Entry ("CONE") used in the VRR Curve, and the methodology for determining the Net Energy & Ancillary Services ("E&AS") revenue offset used to calculate Net CONE every four years. PJM has retained The Brattle Group to facilitate this review. Based on the results of Brattle's review, PJM will prepare a recommendation to either modify or retain the existing VRR Curve shape. PJM will present its Staff proposals no later than May 15, 2022. Members will have the opportunity to vote on proposals no later than August 31, 2022, and PJM will submit its FERC filing by October 1, 2022. Any updates to the VRR Curve parameters will apply for planning years 2026/2027 through 2029/2030. PJM held one meeting to discuss the Quadrennial Review with stakeholders this period.

Energy Market Issues

Energy Price Formation: After a two-year hiatus, PJM resumed the Energy Price Formation Senior Task Force ("EPSTF") in August 2021. PJM and its stakeholders are exploring potential "circuit breaker(s)" or other stop loss approach(es) that could limit extreme pricing whose cost may exceed the value of its contribution to preserving grid reliability, citing recent events in ERCOT as support for a "circuit breaker" in PJM's Operating Reserve Demand Curve ("ORDC") and Transmission Constraint Penalty Factor rules. As part of this work, stakeholders will explore enhancements to the PJM's ORDC rules to address the impact of recent changes in PJM's dispatch protocols on forecast uncertainty embedded with the approved curve shape that are set to go into effect in 2022. The ORDC faces challenges at FERC as well; in August, FERC filed and was granted a Motion for Voluntary Remand on its Order approving PJM's Reserve Pricing Proposal (FERC Docket No. EL19-58, ER19-1486) by the District of Columbia Circuit Court of Appeals. Additionally, FERC held a Technical Conference Regarding Energy and Ancillary Service Markets on September 14, 2021, in which panelists were asked to discuss the role of reserve market reforms that may contribute to the record regarding PJM's Reserve Pricing Proposal. On November 12, 2021, PJM filed a Motion for Extension of the Effective Date, requesting to adjust the planned implementation date of reserve market reforms from May 1, 2022 to October 1, 2022, citing vendor issues and the need to avoid implementation during the summer months as

grounds for the motion. The extension will allow more time for PJM and its stakeholders to consider circuit breaker proposals and continue the work of the EPSTF ahead of implementation of reserve market reforms.

ARR/FTR Proposal: On October 20, 2021, stakeholders endorsed a joint PJM-stakeholder proposal to address auction revenue rights (“ARRs”) and financial transmission rights (“FTRs”) at PJM’s Markets and Reliability Committee meeting and passed in a sector weighted vote at the PJM Members Committee Meeting on November 17, 2021. The proposed changes are the product of a two-year stakeholder process that was initiated following the GreenHat Energy default in 2018, including a six-month review by an independent consultant, London Economics International (“LEI”), and work done at the ARR/FTR Market Task Force. The proposal was broken into three separate areas, as recommended in LEI’s report, with an ARR track dealing with equity issues, an FTR track for efficiency issues and a transparency track for a simplicity model. PJM anticipates the ARR changes will take effect by February 2023; other changes in the proposal could happen sooner.

Ancillary Services Market Initiatives

Reactive Power Compensation: PJM’s Reactive Power Compensation Task Force (“RPCTF”) held its inaugural meeting on November 15, 2021. The RPCTF will undertake work to seek solutions to address the lack of uniform compensation of VAR capacity reactive rates and compensation methodologies that will avoid the significant time and litigation costs associated with the current process. The RPCTF will work toward developing proposed market rule changes that would establish a rate mechanism that would reduce the procedural risks and costs associated with the existing methodology. PJM shared with the RPCTF that in conversation with FERC staff, roughly half of FERC’s case load is dedicated to reactive power compensation litigation, a remark that gained credence at the FERC meeting on November 18, 2021, when FERC Staff reviewed the caseload of reactive power proceedings before introducing a Notice of Inquiry (“NOI”) proceeding regarding reactive power compensation. The Commission is seeking comment on various aspects of the AEP methodology-based compensation, potential alternative methodologies, and reactive power compensation through transmission rates for resources that interconnect at the distribution level. The Commissioners voted unanimously to approve the proceeding.

Emerging Technologies

No significant updates in this reporting period.

Other

FERC Commissioner Update: On November 16, 2021, the U.S. Senate unanimously confirmed D.C. Public Service Commission Chairman Willie Phillips as a new member of the Federal Energy Regulatory Commission. Phillips may take his seat on the Commission as soon as he arranges to take the oath of office. Phillips’s confirmation brings FERC back to its full, five-member complement.

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Summary: Report Quarterly Update Report Pursuant to Section V.C.2. of the Third Supplemental Stipulation and Recommendation electronically filed by Ms. Christine E. Watchorn on behalf of Ohio Edison Company and The Cleveland Electric Illuminating Company and The Toledo Edison Company