**UNITED STATES OF AMERICA**
**BEFORE THE**
**FEDERAL ENERGY REGULATORY COMMISSION**

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| **PJM Interconnection, LLC** | **)** | **Docket No. ER15-852-000** |

# PROTEST OF THE NRG COMPANIES

Pursuant to Rule 211 of the Rules of Practice and Procedure of the Federal Energy Regulatory Commission (the "Commission"),[1] the NRG Companies[2] (collectively, "NRG") protest the January 14, 2015 proposal by PJM Interconnection, LLC ("PJM") to eliminate PJM's existing demand response program, and to replace it with alternative rules that simulate the effects of demand response in the wholesale market by permitting load serving entities to buy less capacity from the market. PJM refers to its filing as its "Stop Gap" proposal ("Stop Gap Proposal" or "Proposal"), and intends that the new rules would only take effect if the United States Supreme Court elects not to review the *Electric Power Supply Association v. Federal Energy Regulatory Commission* case.[3]

## I. INTRODUCTION

The Stop Gap Proposal would enshrine a deeply anticompetitive regime in which some market participants are permitted to represent their demand response transactions in the wholesale market, while others are artificially barred from accessing the wholesale market. Fortunately, the Commission need not reach the merits of PJM's flawed proposal, because it violates the jurisdictional divide established in *EPSA v. FERC* by continuing to "lure" retail demand response customers into the wholesale market. This time, the lure is no longer a direct

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1 18 C.F.R. § 385.211 (2014).

2 The NRG Companies are NRG Power Marketing LLC and GenOn Energy Management, LLC. The NRG Companies ultimate parent company is NRG Energy, Inc.

3 *Elec. Power Supply Ass'n v. FERC*, 753 F.3d 216 (D.C. Cir. 2014) ("*EPSA v. FERC*" or "*EPSA*").

payment of dollars, but instead a "credit" against a Load Serving Entities' ("LSEs") capacity purchases. While PJM changes the terminology from "demand response" to "Wholesale Load Reduction," the end result is that PJM purports to continue allowing demand response to set wholesale capacity prices in the identical manner as it did prior to the *EPSA* case. Clearly, the D.C. Circuit's jurisdictional holding cannot be swept under the rug in such a misguided manner.

Further, should the Commission reach the merits of PJM's proposal, rejection is also warranted under the Federal Power Act's just and reasonable standard and the accompanying prohibition against undue discrimination or preferences. Implementation of this program would have serious negative consequences both to the wholesale market and to the burgeoning demand response industry, including:

- The Stop Gap Proposal is irredeemably anti-competitive. It denies competitive demand response companies any meaningful role in the wholesale market, unless they somehow receive the blessing of the LSE, which in many cases has business interests that may be contrary to competitive, unaffiliated demand response providers.

- The Stop Gap Proposal gives PJM no meaningful ability to deter the exercise of buyer-side market power by "net buyers" in PJM's capacity market. Inexplicably, PJM instead handed these net buyers a blue print for how to use Wholesale Load Reduction bids to artificially interfere with competitive price outcomes.

- By foregoing the opportunity to reflect retail demand response in its load forecasts, the Stop Gap Proposal hamstrings any State programs that would otherwise fill the regulatory gap created by *EPSA*. Such an outcome is at odds with the Federal Power Act's directive for the Commission to "encourage" demand response.[4]

While NRG opposes the Stop Gap Proposal, NRG agrees with PJM on two major points. *First*, NRG agrees with PJM that the *EPSA* decision was wrongly decided and, accordingly, NRG has announced its intention to file a Friend of the Court brief support the Solicitor

[4] *See* Section 1252 of the Federal Power Act ("It is the policy of the United States that . . . demand response . . . shall be encouraged[.]")

General's and FERC's petition, as well as those filed by EnerNOC and other private parties, for the U.S. Supreme Court to review the case.[5] *Second*, NRG agrees that it is critical that each organized market develop a contingency plan for implementation if the Supreme Court denies *certiorari* in the *EPSA v. FERC* case. Development of a contingency plan is clearly in the best interests of reliability and proper market function. Rejecting the Stop Gap Proposal does not mean that the Commission and PJM should do nothing. Instead, the Commission should direct PJM to incorporate the results of State-driven demand response programs into its load forecast and Installed Reserve Margin calculations, and then to procure sufficient capacity through the Reliability Pricing Model to meet the modified estimate of load, plus the appropriate reserve margin. Incorporating demand response into load forecasts provides State regulators a clear framework on which to build their own demand response compensation programs, allows demand response to be reflected in the PJM market, and avoids violating *EPSA* or creating a regime that severely favors incumbent utility-affiliated Load Serving Entities over competitive market participants.

Regardless of the whether the Commission uses this docket as an opportunity to set new policy, the Commission must reject the Stop Gap Proposal. In this case, "nothing" is truly better than the legally suspect and anti-competitive "something" proposed by PJM.

## II. BACKGROUND

### 1. Background on PJM's Proposal

PJM's Stop Gap Proposal is designed to keep demand response resources subject to the rules applicable to the PJM wholesale market, despite the clear directive from the *EPSA* Court that demand response is a State-jurisdictional product and that State regulators – not FERC –

[5] *See* Notice of NRG Energy, Inc., that it intends to file an *amicus curiae* brief to the Supreme Court in the *EPSA v. FERC* case (Noticed February 4, 2015).

should be setting the rates, terms and conditions under which demand response customers participate in the retail market. PJM requests that the Commission implement its Stop Gap Proposal "only in the event the United States Supreme Court denies" the petitions for certiorari seeking review of the *EPSA* case.[6] PJM asserts that its proposed changes "establish a jurisdictionally sound basis to realize the operational and market efficiencies of demand response in the PJM Region in lieu of the risks and uncertainties that would arise if PJM cleared demand response in its capacity market auctions under the existing rules after the EPSA mandate had issued."[7]

PJM's Proposal – if triggered by a denial of certiorari by the Supreme Court – would eliminate demand response *supply* bids from the 2015 Base Residual Auction ("BRA"), which is scheduled to take place in May, 2015. Instead, PJM proposes to create a new class of Wholesale Load Reduction and Wholesale Energy Efficiency Load bids (which we refer to, collectively, as "Wholesale Load Reduction," or "WLRs"). Wholesale Load Reduction bids would represent an agreement by an LSE to lower its consumption by a stated amount at various pricing points. Under the Proposal, Wholesale Load Reduction bids would effectively shift the Reliability Pricing Model's demand curve, known as the Variable Resource Requirement Curve, or "VRR," to the left by the size of the Wholesale Load Reduction bid by the LSE. Because of the way the program is proposed to be implemented, a Wholesale Load Reduction bid would have the identical impact on capacity prices as a demand response capacity resource's bid.

PJM also proposes to limit the types of entities that will be allowed to place Wholesale Load Reduction bids in the future, as well as prohibit any LSE from placing WLR bids in excess of their load in each zone. This, PJM argues, would allow demand response resources to

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6 Stop Gap Proposal at p. 3.

7 Stop Gap Proposal at p. 3.

continue participating in the wholesale market in a manner that complies with the *EPSA* decision, since LSEs would be simply indicating to PJM the price at which they would be willing to reduce their consumption of capacity services. PJM asserts that "[w]ith such modifications, the VRR Curve will more accurately reflect the amount of capacity PJM properly should procure in RPM because it will reflect the actual (reduced) load that wholesale customers want to be served, based on the RPM clearing price for capacity."[8]

Additionally, the PJM Proposal includes several "Options" for implementation, depending on how the Commission rules on PJM's capacity market design changes currently pending before the Commission. While the details of the implementation are complicated, PJM proposes, in effect, to replicate the rules governing generation resources taking on a capacity supply obligation and apply those rates, terms and conditions to Wholesale Load Response participants.

### A. Background on NRG

NRG and its affiliates are one of the largest owners of conventional generation in PJM with over 16,000 MW of resources. NRG is also one of the largest providers of competitive demand response services in the PJM market, primarily through its subsidiary, Energy Curtailment Specialists, Inc., which is a registered Curtailment Service Provider, or CSP, in PJM. NRG also has several affiliates providing retail electric service throughout the PJM region in states that allow retail choice.

In reviewing the PJM proposal with these various "hats," NRG sees a proposal that does not work for any of its various business lines and in fact, would substantially reduce competition in all three of the major sectors (wholesale generation, demand response, and retail electric supply) in which NRG competes.

[8] Stop Gap Proposal at p. 3.

## III. PROTEST

### A. The Stop Gap Proposal is Not Compliant with *EPSA v. FERC*.

The D.C. Circuit's admonition was clear: "Demand response – simply put – is part of the retail market. It involves retail customers, their decision whether to purchase at retail, and the levels of retail electricity consumption."[9] PJM's desire to continue asserting control over the demand response product results in a proposal that is really no more than jurisdictional hand-waving and does nothing to give voice to the Court's directive that the Federal Power Act requires that demand response be a State jurisdictional product.[10]

PJM itself highlights the hand-waving aspects of its Proposal through its cover letter. PJM is quick to assure the Commission that the Proposal is just and reasonable because it proposes to replace direct capacity *payments* to end-users with an identical *credit* to the end-users' LSE. Thus, PJM's reasoning goes, the Commission has already established the justness and reasonableness of this compensation scheme, since the economic impact of the Stop Gap Proposal remains virtually unchanged post-*EPSA*. While the Stop Gap Proposal makes much of the fact that the flow of dollars bypasses the retail customer and only appears as a credit against the LSE's purchase obligations, this is a distinction without a legal difference. The D.C. Circuit expressly found that "luring the resource to enter the market" violates the Federal Power Act.[11] As

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[9] *EPSA*, 753 F.3d at 223.

[10] NRG, PJM and the Commission all disagree with the *EPSA* decision. However, this underlying disagreement should not affect the Commission's legal analysis of the Stop Gap Proposal. After all, the Stop Gap Proposal will only go into effect *if* the Supreme Court decides not to grant certiorari and *EPSA v. FERC* remains the law of the land.

[11] *EPSA*, 753 F.3d at 223.

the Court stated, the "lure is change of the retail rate."[12] Simply substituting one lure for another does nothing to address the Court's concern that demand response "is part of the retail market."[13]

Further, as if anticipating PJM's Proposal to change the lure from a capacity payment to a capacity credit, the Court rejected the idea that toggling between a "payment" and a "credit" would resolve its jurisdictional concerns:

> Ordering an ISO to compensate a consumer for reducing its demand is the same in substance and effect as issuing a credit. . . . Thus, while it is true demand response can occur in two ways—through a response to either price change or incentive payments – nothing about the latter makes it "wholesale." A buyer is a buyer, but a reduction in consumption cannot be a "wholesale sale." FERC's metaphysical distinction between price-responsive demand and incentive-based demand cannot solve its jurisdictional quandary.

As the Court goes on to explain, "[i]f FERC had directed ISOs to give a credit to any consumer who reduced its expected use of retail electricity, FERC would be directly regulating the retail rate." This "direct regulation" is, in effect, exactly what PJM has proposed to do in its Stop Gap Proposal – provide LSEs a credit for bringing retail demand response transactions into the wholesale market.

Further, by its own admission, PJM's Stop Gap Proposal is designed to keep demand response resources in the wholesale market, and to do so under rates, terms and conditions that mimic the jurisdictional scheme rejected by the Court, completely undermining the *EPSA* decision which should be the controlling precedent here. PJM even details the way in which the Wholesale Load Reduction program replicates key attributes of the pre-*EPSA* demand response program, noting that:

- The capacity market price impacts are identical between an equally sized Wholesale Load Reduction bid and a supply-side demand response resource;[14]

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12 *Id.*

13 *Id.*

- The sales plans for entities placing Wholesale Load Reduction are identical to the sales plans for supply-side demand response resources, as are PJM's rules for review and validation of those plans;[15]

- Measurement and verification of participants in the new Wholesale Load Reduction program will be identical to pre-*EPSA* supply-side demand response resources;[16]

- Non-performance penalties are exactly the same for entities participating in the Wholesale Load Reduction program as they are for pre-*EPSA* demand response resources;[17] and

- New Wholesale Load Reduction resources are grouped into the identical product categories as supply-side demand response resources (such as Limited, Extended Summer, and Annual products), with identical qualification requirements.[18]

In each case, PJM proposes to apply the old rules to its "new" product. It is impossible reconcile the *EPSA* Court's requirement that demand response rates, terms and conditions be set by the States, with PJM's stated desire to continue regulating these aspects of demand response's participation in the wholesale market. In short – PJM's proposal is merely jurisdictional window dressing and must be rejected.

### B. PJM Incorrectly Suggests that the Markets will Lose the Benefits of Demand Response if the Stop Gap Proposal is Rejected.

The Stop Gap Proposal sets up a false dichotomy by suggesting that the Commission must either approve PJM's anticompetitive proposal or that demand response will simply cease

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[14] Stop Gap Proposal, at p. 50 ("WLR Loads and WEELs will not receive a capacity payment based on any clearing price. However, they will be assigned a value based on prices identified in the auction. Under Option B, for Annual WLR, this will be the clearing price determined for Annual Resources[.]")

[15] Stop Gap Proposal, at p. 47 ("The plan requirements are closely modeled on provisions that the Commission recently found to be just and reasonable in Docket No. ER13-2108–00065 and ensure that WLR Providers will be treated comparably to other RPM participants.")

[16] Stop Gap Proposal, at p. 58 ("PJM concluded, however, that the types of data PJM would need to measure and verify its performance under such a general standard would not differ materially from the kinds of data described in the provisions PJM has incorporated into its proposed tariff revisions.")

[17] Stop Gap Proposal, at p. 42 ("Any Wholesale Entity that commits WLR Load in an RPM Auction, but fails fully to honor its WLR commitments for a Delivery Year, shall be assessed compliance charges.")

[18] Stop Gap Proposal, at p. 16 ("… different types of WLR with different availability rules that exactly match the availability rules previously approved for Limited Demand Resource, Extended Summer Demand Resource, and Annual Demand Resource.")

to exist and consumers will lose all of the benefits of demand response.[19] The bitter irony is that PJM's proposal is more likely to drive competitive demand response from the PJM market than simply leaving demand response policy to the States, as *EPSA* requires. Even in the scenario where demand response becomes a State-jurisdictional product that is procured pursuant to State-mandated policies and procedures, demand response will continue to be a critical driver of energy policy in this country.

Indeed, PJM has proposed a worst-of-all-possible-worlds scenario for competitive market design where PJM continues to set the value of demand response, but allows only a subset of existing demand response market participants to compete to receive those revenues. The only "benefit" to PJM's Stop Gap Proposal is that it allows PJM to continue setting the price for demand response, the penalty rate for non-compliance, and the measurement and verification rules under which the new Wholesale Load Response resources will operate.[20] While PJM may judge that it is better to retain some control over the demand response program, even if it comes at the expense of sacrificing the competitive demand response industry, that is not a view that the NRG Companies share or that the Commission should adopt.

To be clear – NRG would prefer demand response to remain a FERC-jurisdictional service, governed by a seamless web of rules across the entire PJM footprint, rather than a product governed by State regulators in thirteen different states, plus the District of Columbia. However, the jurisdictional battle will be fought in the U.S. Supreme Court. A "second best" option is to allow individual States to implement comprehensive demand response programs. PJM's Stop Gap Proposal solution is a distant third. The barriers to entry for demand response

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[19] "PJM believes the rules it proposes here would preserve the reliability and economic benefits of some demand response, and would be superior to rules that do not recognize any demand response." Stop Gap Proposal at p. 3.

[20] Of course, it is exactly this behind-the-scenes control over demand response that should cause the Commission to determine that PJM's proposal does not comply with the *EPSA* decision.

are relatively low, and new resources can enter the market in relatively short order, if the appropriate State-jurisdictional payment scheme is put into place. After all, it is the actual reduction in load that benefits the economic function of the market, regardless of whether it is procured pursuant to a State or Federal program.

Indeed, several States have already begun considering contingency plans for what happens if the Supreme Court denies review of the *EPSA* decision. For example, the New York Public Service Commission recently initiated a proceeding aimed at expanding the Consolidated Edison ("ConEd") Distributed Load Relief Program across the entire State of New York.[21] This program pays distribution level customers both a reservation payment (akin to a capacity payment) and energy payment for the delivery of energy. While NRG agrees that centralized procurement of demand response services at the wholesale level is preferable to a state-by-state approach to demand response, there are countless business opportunities in state-jurisdictional demand response programs that will allow the benefits of demand response to flow through to the wholesale market.

### C. State-led Programs can (Partially) Fulfill DR's Promise – if States are Allowed to Lead as Mandated by *EPSA*.

Even if the Commission rejects the Stop Gap Proposal, PJM will continue to have a critical role in recognizing the contribution of demand response to our Nation's energy markets. There is still a great deal of work that needs to be done on the wholesale side to accommodate State demand response programs. Specifically, PJM will need to adjust its load forecasts and Installed Reserve Margin to reflect the outcome of State-driven demand response policies in the amount of capacity it procures in the forward time horizon. In order to accomplish this task, PJM will have to develop a means of forecasting the amount of demand reduction elicited by a

[21] NRG filed comments in support of the expansion. *See* Comments of NRG Energy, Inc. on Proposed Distribution-Level Demand Response Programs, filed in Case E-14-0423 (January 30, 2015).

State program, and incorporating that reduction into PJM's determination of its load forecast and Installed Reserve Margin, over which the Commission (and thus PJM) has unambiguous jurisdiction.[22]

For example, PJM currently utilizes a five-coincident peak methodology for determining a specific customer's capacity allocation. Should that customer reduce its consumption during those five coincident peaks pursuant to a State demand response program, then PJM would procure less capacity for that customer. Once the system reaches steady-state, PJM could base its load forecasting on a three-to-five year historical look-back of demand response's actual contribution during relevant peak periods. Under such a scheme, PJM would have no role in paying end-users for their demand response services and would thus be indifferent to State compensation levels and would not have to worry about measurement and verification procedures, or penalties for non-performance.[23]

While the transition to this end state will necessarily involve relatively crude estimates of what level of demand response States will incent over the next several years, this approach is competitively superior to the anticompetitive approach advocated by PJM and is clearly compliant with the dictates of the *EPSA* decision. Thus, PJM continues to have an important role in forecasting the amount of demand response that will enter the market and to procure the appropriate amount of capacity and energy to meet the modified demand on a forward- and real-time basis.

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[22] As PJM correctly points out, the courts have repeatedly held that the establishment of the Installed Reserve Margin is wholly within the Commission's jurisdiction. *See* Stop Gap Proposal at pp. 33-34 (citing, among other cases, *Municipalities of Groton v. FERC*, 587 F.2d 1296 (D.C. Cir. 1978) and *Conn. Dep't of Pub. Util. Control v. FERC*, 569 F.3d 477, 479 (D.C. Cir. 2009)).

[23] This is not to say that PJM data wouldn't be employed; simply that PJM would not be the entity directly involved in setting performance criteria or allocating payments or penalties.

### D. The Stop Gap Proposal Relies on an Inherently Discriminatory Market Framework that Favors LSEs and Destroys the Competitive Demand Response Business Model.

The Stop Gap Proposal, if adopted, would be a severe blow to the competitive demand response industry. Indeed, as discussed above, competitive demand response providers have better opportunities to flourish with a State-by-State approach to determining demand response compensation than they would have under the PJM proposal. The biggest problem is that the Stop Gap Proposal makes Load Serving Entities the sole market participants allowed to engage in demand response services. This misguided structure means that the LSEs will be the sole arbiter of demand response participation in the PJM market, but with few (if any) rules or requirements to constrain their market behavior.

And while competitive companies, including NRG, have LSE affiliates selling electricity in retail-choice states, this does nothing to address the anti-competitive nature of PJM's proposal. *First*, the vast majority of PJM's load is still served by Local Distribution Companies ("LDCs") through Provider of Last Resort, Default Service, or similar arrangements. *Second*, many CSPs register multiple customers across a particular load zone to prudently manage performance risk. That is, one customer may under-perform in a given test, while others may over-perform. By limiting Wholesale Load Reduction bids to the size of a particular LSE's load, only the largest LSEs will be able to achieve the necessary scale. Further, these largest LSEs are typically affiliated with integrated utilities and LDC interests.

The result is that the majority of entities that PJM proposes to allow to place Wholesale Load Reduction bids are associated with self-interested market participants with agendas that do not always align with the goals of a sustainable demand response program. Some LSEs will be affiliated with major generation interests. Others have affiliates that provide demand response services that they will naturally want to favor. Others are associated with LDCs and have a

financial interest in suppressing market prices through uneconomic support of new entrants. Still others may become subject to State requirements to engage in bidding behavior that furthers buyer-side market power. PJM's proposal to put these entities in the demand response driver's seat must be rejected.

### 1. The Stop Gap Proposal violates the Federal Power Act's prohibition against undue discrimination.

PJM asserts that "[t]his filing is premised on a simple proposition: a functional market should accurately reflect demand, as well as supply."[24] While NRG agrees with this proposition in theory, the Stop Gap Proposal does not fulfill the "simple premise" that PJM promises because it allows only certain loads – those with a willing Load Serving Entity as its retail electric supplier – to participate in the market. The Commission should insist that any just and reasonable proposal allowing *all* load to participate in whatever program replaces PJM's existing supply-side demand response program.

PJM actively concedes that "[CSPs] have historically accounted for a majority of the demand response registered in PJM, but would not be permitted to offer demand response directly into the PJM market under this proposal."[25] Section 205(b) of the Federal Power Act ("FPA") prohibits, any public utility, "with respect to any transmission or sale subject to the jurisdiction of the Commission," to:

> (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or
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> (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

[24] Stop Gap Proposal at p. 3.

[25] Stop Gap Proposal at p. 3.

Putting CSPs at such an enormous competitive disadvantage is a clear violation of both of these prohibitions. PJM's admission that it is singling out a particular class of market participants for elimination is breathtaking – and represents a *per se* violation of Section 205(b)'s prohibitions.

PJM will undoubtedly respond that such discriminatory treatment is warranted, *i.e.*, that this is due discrimination. This argument also falls flat. The Commission must recognize that this discriminatory treatment arises *only* because of PJM's end-run around the *EPSA* decision. Had PJM simply acknowledged that, under *EPSA*, the States become the drivers of demand response policy, there would be no need for the type of arbitrary distinction proposed by PJM. Put simply – it is only PJM's unlawful insistence that demand response must be compensated through a wholesale market credit that drives the arbitrary exclusion of CSPs from the marketplace.

**2. Enshrining self-interested LSEs as the arbiter of demand response bids harms competition and decreases innovation.**

Requiring all competitive demand response providers to sleeve their trades through an LSE will destroy the innovation that has been a hallmark of the demand response industry over the past decade. Demand response providers have historically been key innovators in the energy markets, developing new ways of signing up customers and new technologies to maximize the contribution of demand response to the market. If PJM's proposal is accepted, however, all of these competitive suppliers will either be forced (at best) to become contractors to LSEs, many of whom have utility affiliates, compete for the fraction of the market served by an amenable independent LSE, or be driven from the market entirely.

There is no question as to what will happen when a self-interested LSE is put in the position of being the sole buyer of demand response services within its own service territory: barriers to entry will immediately spring up and the prices paid to competitive demand response firms will go down. Decreases in payments will flow through to lower prices paid to the ultimate

end-user electing to participate in demand response, severely curtailing the attractiveness of engaging in demand response. Utility-affiliated LSEs are traditionally risk-averse entities with guaranteed rates of return and little incentive to work with unaffiliated competitive demand response suppliers in their service territories.

**3. The agency relationship is poorly defined.**

The Stop Gap Proposal also includes a proposal to allow LSEs to designate certain CSPs as their "agents" for the purposing of entering demand bids into the capacity market. PJM asserts that this "agency" relationship ameliorates some of the anti-competitive aspects of its proposal, while also satisfying the jurisdictional dictates of the *EPSA* decision. The agency proposal, however, provides no real protections to competitive demand response suppliers and fatally undercuts PJM's jurisdictional arguments.

The anticompetitive implications of the agency rules are truly frightening. There is nothing to stop an LSE from exercising its agency authority on a discriminatory basis by, for example, forbidding anyone but its affiliates from offering Wholesale Load Reduction bids in its service territory or for its customers. This structure leaves LSEs free to discriminate against selective CSPs, either by favoring their affiliates or simply throttling the amount of competition allowed into the market. For example, the agency section of the Stop Gap Proposal does nothing to specify the rates, terms or conditions governing the agency relationship. This virtually encourages LSEs to offer unacceptable contractual terms for sleeving the CSP transactions to the market, imposing unreasonable pricing, collateral, or other terms and conditions. Many utility-affiliated LSEs could simply impose insurmountable collateral requirements that only their

affiliates (which are often the only investment-grade entities in the market) would be capable of meeting.[26]

Moreover, the agency relationship calls into question the jurisdictional underpinnings of PJM's proposal. Under PJM's logic, a retail customer, represented by a CSP, may still be "lured" into the FERC-jurisdictional market – so long as it has the permission of the customer's LSE. PJM's attempt to categorize the CSP's involvement as simply a reduction in the purchases the LSE is making, based on the expected demand response, is unavailing. In reality, PJM is attempting to bypass the dictates of *EPSA* by simply providing retail customers a thinly-disguised avenue to reach the wholesale market.

However, should the Commission somehow find that the agency relationship meets the jurisdictional threshold, then it must *regulate* the agency relationship and ensure that LSEs are entering into these arrangements on a non-discriminatory basis, consistent with the Commission's open access policies. While NRG has serious reservations about whether the agency proposal comports with *EPSA*, the only tenable outcome is that if the Commission has the jurisdiction to approve the participation of demand response through these arrangements, then it also has the jurisdiction to ensure that the arrangements are entered into on a fair and non-discriminatory basis.

#### 4. LSE-only bidding structure is bad policy because it creates the opportunity and incentive for the exercise of market power.

The Stop Gap Proposal creates the unacceptable prospect of LSEs exercising an unacceptable amount of discretion over the participation of demand response load bids into the capacity market. This excessive discretion can result in the exercise of market power that is

[26] The credit issues increase significantly if the Commission both approves the Stop Gap Proposal and approves the Capacity Performance rule changes, which imposes significant parallel penalty risk to both generation suppliers and participants in the Wholesale Load Reduction program.

virtually impossible for the Commission to police or monitor. Interestingly, the exercise of market power could be exercised differently by different types of LSEs – some may seek to encourage demand response in order to artificially suppress wholesale capacity prices, while others may decide to forbid any demand response from entering their service territories in order to favor their affiliated generation interests. Neither is an acceptable policy outcome.

As the Commission has repeatedly explained, capacity markets are extremely sensitive to the entry of even small amounts of non-competitive supply. In its 2013 ruling approving PJM's revisions to its Minimum Offer Price Rule ("2013 MOPR Case"),[27] the Commission specifically identified "net buyers" of capacity as having a direct economic interest in suppressing capacity market prices. The Commission explained that it was necessary to mitigate bids placed by such net buyers:

> PJM's MOPR is a mechanism that seeks to prevent the exercise of buyer-side market power in the forward capacity market, which occurs when a large net-buyer – that is, an entity that buys more capacity from the market than it sells into the market – invests in capacity and then offers that capacity into the auction at a reduced price. Given the uniform clearing prices in PJM's markets, such behavior would benefit the net-buyer so long as the reduction in the net-buyer's purchasing costs exceeds its losses from selling the underpriced capacity.

By mandating that only LSEs (who are net buyers, almost by definition), the Stop Gap Proposal creates a powerful price suppression tool that clearly warrants application of MOPR-type mitigation. Under the Stop Gap Proposal, a megawatt of Wholesale Load Reduction demand response will have an identical pricing impact on the wholesale capacity markets as a megawatt of supply. This truism would allow an LSE, motivated the promise of suppressing capacity prices (or the direction of their State regulator), to simply bid excess load reduction into the capacity market, thereby reducing the overall clearing price. These "net buyers" could clearly

[27] *PJM Interconnection, LLC*, 143 FERC ¶ 61,090 (2013), *affirmed sub nom. N.J. Bd. of Pub. Utils. v. FERC*, 744 F.3d 74, (3rd Cir. 2014).

employ such a stratagem to bypass the Commission's Minimum Offer MOPR rules, without the apparent ability for the Commission to regulate the underlying contract between the LSE and their customers, which, under *EPSA*, are non-jurisdictional transactions.

Indeed, PJM recognizes this possibility in its Stop Gap Proposal and does not appear to have an answer to the problem. The Stop Gap Proposal practically encourages such an outcome by offering that, "each Wholesale Load Reduction will broadly benefit all capacity buyers" and encouraging LSEs and state regulators to "monetize" this "benefit" through retail rate proceedings.[28] While the Commission has previously declined to impose a mitigated price floor on demand response bidding into its capacity market, there was no doubt pre-*EPSA* that the Commission had the *authority* to address subsidized demand response bids entered into the capacity market with the purpose of suppressing prices. That authority would not appear to exist post-*EPSA*. And while PJM proposes to continue screening Wholesale Load Response plans submitted by LSEs for feasibility, it is not clear that PJM will be able to successfully deter such behavior.

The possibility that an LSE will simply eliminate competitive demand response within its service territory is equally problematic from a market power standpoint. For example, some large LSEs (whether affiliated with a utility or independent) may seek to freeze out and minimize the participation of competitive demand response either for the purpose of increasing the value of their affiliated wholesale generation fleet or simply freezing out competitors to their own or affiliated demand response companies. Thus, while PJM apparently believes that including Wholesale Load Reduction bids in its wholesale market will help discipline generation prices, the exact opposite result may occur.

[28] Stop Gap Proposal at p. 20.

## III. CONCLUSION

For the foregoing reasons, NRG respectfully requests that the Commission reject PJM's Stop Gap Proposal, and instead, direct PJM to immediately commence stakeholder discussions designed to accommodate state-driven demand response policies and to incorporate the results of those policies into PJM's forward procurement decisions.

February 13, 2015

Respectfully submitted,

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**Certificate Of Service**

I hereby certify that I have served a copy of the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Princeton, New Jersey this 13th day of February, 2015.

/s/ *Kathryn Wig*
Kathryn Wig