

129 FERC ¶ 61,294
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer and Philip D. Moeller.

PJM Interconnection, L.L.C.

Docket No. ER10-168-000

ORDER ACCEPTING TARIFF REVISIONS,
SUBJECT TO CONDITIONS

(Issued December 30, 2009)

1. On October 30, 2009, PJM Interconnection, L.L.C. (PJM) filed proposed revisions pursuant to section 205 of the Federal Power Act¹ to its Open Access Transmission Tariff (Tariff) and Amended and Restated Operating Agreement (Operating Agreement).² In its filing, PJM proposed the following revisions to its credit policies: (i) grant PJM discretion in the calculation of a participant's Peak Market Activity to allow an adjustment for the loss of short-term load contracts; (ii) allow participants with unsecured credit to make up to ten payments per year to reduce their Peak Market Activity; and (iii) establish rules related to the reinstatement of members that fail to meet their payment and/or collateral obligations to PJM.
2. For the reasons discussed below, we accept PJM's proposed tariff changes, subject to conditions, to become effective, as requested, on January 1, 2010.

¹ 16 U.S.C. § 824d (2006).

² Fifth Revised Sheet No. 523H and Fourth Revised Sheet No. 523H.01 to PJM Interconnection, L.L.C.'s FERC Electric Tariff, Sixth Revised Volume No. 1, and Sixth Revised Sheet No. 50 and First Revised Sheet No. 50A to PJM Interconnection L.L.C.'s Third Revised Rate Schedule FERC No. 24.

Background

A. Discretion to Account for Loss of Short-Term Load Contracts

3. PJM proposes an adjustment to the calculation of Peak Market Activity, which is used to determine the level of financial security needed to support a participant's activity in the PJM Market. According to PJM, some non-residential load contracts acquired pursuant to state-sponsored auctions are for durations as short as three months, and the loss of such load contracts is known and measurable, and could substantially alter a participant's expected market activity going forward. As such, PJM proposes to amend section II.D of Attachment Q of the Tariff to grant PJM discretion to adjust a participant's Financial Security Requirement if PJM determines that the Peak Market Activity is not representative of the participant's expected activity as a consequence of known, measurable, and sustained changes, including the loss (without replacement) of short-term load contracts, acquired through state-sponsored retail load programs, with terms of three months or more.

B. Early Payments for Members with Unsecured Credit

4. PJM explains that its current Tariff provisions allow a participant with unsecured credit to make up to three early payments per year to reduce its Peak Market Activity for credit requirement purposes as a way to normalize spikes in market activity. According to PJM, under prior monthly billing and settlements, three early payments was sufficient to allow a participant to account for one season, thereby normalizing peaks of demand. However, PJM states that, since the implementation of weekly billing and settlements, this provision is of little to no benefit. Therefore, PJM proposes tariff revisions to section II.E of Attachment Q of the Tariff to allow a participant with unsecured credit to make early payments up to ten times in a rolling 52-week period in order to reduce its Peak Market Activity for credit requirement purposes. As proposed, PJM states, such early payments must be received prior to the issuance or posting of the invoice for the relevant billing period.

C. Reinstatement Guidelines for Defaulting Members

5. PJM argues that currently, its Operating Agreement does not provide sufficient disincentives against repeated abuses of PJM's financial default rules. Section 15.1.5 of the Operating Agreement allows PJM to penalize a member who has not remedied a breach after a sufficient notice and breach-cure period. PJM notes, however, that the Operating Agreement neither requires defaults to be cured within a prompt time frame, nor limits how many default-cure cycles a member is permitted. PJM states that, without such limitations, a defaulting member can default and cure numerous times, without experiencing any long-term loss of rights, potentially resulting in excessive administrative costs and inefficiencies for PJM and the membership as a whole. Thus, PJM asserts, the absence of such limitations fails to provide the proper incentive to avoid

defaults. Further, PJM asserts, the occurrence of multiple instances of defaults by a single party, even though eventually cured, is an indicator of financial risk that is not currently addressed by PJM's policies.

6. PJM proposes to implement a new section 15.1.6 of the Operating Agreement to, broadly, establish a tiered limitation of reinstatement rights for members that have been declared in collateral and/or payment default (after the applicable breach-cure period) of their obligations under the Operating Agreement and/or Tariff. PJM states that the purpose of this revision is to provide incentives to ensure that defaults are avoided to the largest extent possible, to further protect PJM's members from defaults by a participant that is exhibiting behavior consistent with high-risk companies, and to alleviate the potential burden and costs that numerous breach-cure cycles may have upon PJM's administrative processes.

7. PJM proposes a tiered system for handling defaults. Under proposed new section 15.1.6(a), "[a] Member that has been declared in default ... or fails to otherwise comply with PJM's credit policies **once** within any [rolling] 12 month period may be reinstated in full after remedying such default."³ Under section 15.1.6(b), however, if that one default was for "failing to [] make timely payments" or if the Member were to fail to follow any other "credit policies, **twice** during any [rolling] 12 month period," then that Member would lose voting rights and access to unsecured credit for the subsequent 12 month period.⁴ Finally, under section 15.1.6(c), if during any rolling 12 month period, the member were to fail to "make timely payments when due **twice** ... or adhere to any of its obligations under this agreement, including ... credit policies, **three** times," then its membership "shall be terminated," and its market positions liquidated.⁵

8. PJM also explains that under its current tariff, a member can be terminated for a default. PJM proposes to add a tariff provision governing the situations in which a member terminated for default can re-apply for membership. Under the proposed new section 15.1.6(c), a violating member "shall ... not be eligible to be reinstated as a Member" and "shall be precluded from seeking future membership," except by following the procedures outlined in the proposed new section 15.1.6(d). That section allows ex-Members to invoke a modified version of Schedule 5, the Operating Agreement's

³ PJM Proposed section 15.1.6(a), Proposed Sixth Revised Sheet No. 50 (emphasis added).

⁴ PJM Proposed section 15.1.6(b), Proposed Sixth Revised Sheet No. 50 (emphasis added).

⁵ PJM Proposed section 15.1.6(c), Proposed Sixth Revised Sheet No. 50A (emphasis added).

standard dispute resolution procedure. Under the proposed new section 15.1.6(d), which may only be used for reinstatement and “not [] to stay the ability of PJM to exercise” the Member’s expulsion, the ex-Member “may be reinstated provided that the member can demonstrate ... (a) that it has otherwise consistently complied with its obligations under [the Operating] Agreement and the PJM Tariff; and (b) the failure to comply was not material, and; (c) the failure to comply was due in large part to conditions that were not in the common course of business.”⁶ PJM states that this “fail safe” provision is designed to ensure that members otherwise in good standing have the opportunity to seek redress for determinations made by PJM and, ultimately, will not be barred from participation based upon non-material defaults of their obligations.

Notice and Responsive Pleadings

9. Notice of PJM’s filing was published in the *Federal Register*, 74 FR 58271 (2009), with protests and interventions due on or before November 20, 2009. American Municipal Power, Inc. (AMP) filed a timely motion to intervene and protest; Old Dominion Electric Cooperative and Exelon Corporation also filed timely motions to intervene. On December 7, 2009, PJM submitted an answer to AMP’s protest.

A. AMP’s Protest

10. AMP protests the proposal to limit the reinstatement rights of members that have been declared in default of their payment or collateral obligations to PJM. AMP states that, in principle, it does not oppose PJM’s objective; rather, AMP is concerned that the language of the rules proposed by PJM in proposed section 15.1.6 to the Operating Agreement is overly expansive. AMP states that its members are municipal electric systems that may face unanticipated budgeting constraints as a result of unforeseen circumstances that may hamper their ability to remit timely payments and post required collateral when due, which could lead to termination of the member’s membership rights in PJM and prohibit them from re-applying for membership in the future. Given the severity of permanent expulsion from PJM, AMP argues, the scope of the proposed rule should be limited to situations that are necessarily reflective of high-risk market activities. Broadly-written expulsion powers, AMP argues, does not represent a measured approach to managing the risk of default to pool members.

11. Further, AMP argues that the ambiguous language in proposed section 15.1.6 of the Operating Agreement makes it unclear how PJM will implement the provisions of that section. AMP explains that while PJM’s transmittal letter suggests that penalties would apply only to credit or payment-related issues, the plain language proposed appears to provide that a member’s failure to comply with any of its obligations under the

⁶ PJM Proposed section 15.1.6(d), Proposed Sixth Revised Sheet No. 50A.

Operating Agreement could trigger membership termination. AMP asserts that the “catch all” language in subsections (b) and (c) is at odds with the more specific language set forth in subsection (a) directed at collateral and payment defaults.

12. AMP also argues that it is not clear from the language in section 15.1.6 under what conditions reinstatement will be permitted. AMP expresses concern that reinstatement will be allowed only with respect to defaults for credit policy infractions, such as nonpayment or a failure to provide collateral when required. AMP asserts, however, that it is uncertain whether reinstatement would be permitted for defaults associated with non-credit policy issues. AMP requests that section 15.1.6(c) be revised to ensure that the conditions pursuant to which a member may lose its membership are narrowly tailored and explicitly identified in the Operating Agreement because there should be no doubt for PJM members as to the circumstances under which their membership may be terminated.

13. AMP also states that PJM fails to detail the ramifications of a membership being terminated. In particular, AMP states, PJM’s filing is silent with respect to the impact of terminating the membership of a retail load serving entity, transmission owner or generator owner, and as to who would become responsible for serving the former member’s load. AMP questions if PJM would have rights to call on a generator whose membership is terminated and if such a generator would still have a capacity must-offer requirement. AMP argues that PJM should be required to explain the effect of a member’s expulsion pursuant to section 15.1.6 of the Operating Agreement, including, *inter alia*, what actions PJM may take following such expulsion to mitigate the impact thereof and what remaining obligations, if any, the former member will be required to fulfill.

14. AMP states that the provisions addressing a former member’s rights to appeal for reinstatement are imprecise. AMP states that the Operating Agreement fails to specify who, as between PJM and the mediator or arbitrator selected to resolve the dispute pursuant to Schedule 5 to the Operating Agreement, will be responsible for determining whether the member has made the required demonstration as a condition to reinstatement. AMP asserts that if PJM has the discretion to determine whether the member has made the requisite showings, PJM’s so called “fail safe” provision is a misnomer as currently drafted. According to AMP, if the authority to determine a member’s eligibility to reapply for membership ultimately rests with PJM, then a member can have no assurance that it will be reinstated as a PJM member even if it believes that it has satisfied the section 15.1.6(d) three-prong test. AMP maintains that section 15.1.6(d) does not identify any criteria pursuant to which the former member’s responses and materials provided to satisfy the three-prong test would be evaluated and argues that it should be revised to clarify that any such responses and materials be evaluated according to objective criteria or standards.

15. Finally, AMP argues that PJM should carry the burden of proof in seeking to terminate a member's membership. According to AMP, section 15.1.6 does not require PJM to make any showing to the Commission before expelling a member from the RTO and that it would presumably be left to the dissatisfied expelled member to seek redress with the Commission via a complaint filed pursuant to section 206 of the Federal Power Act. Given the grave consequences for both the expelled and remaining members in the pool, AMP argues that PJM's proposal should be revised so as to require PJM to seek Commission approval pursuant to section 205 in order to terminate a member's membership in PJM.

B. PJM's Answer

16. PJM argues that its proposed reinstatement rules are reasonably fashioned to address serious defaults and minimize the risk of potential defaults to the PJM membership pool. PJM argues that, under its Operating Agreement, the concepts of "breach" and "default" are unique and separate. As PJM explains, any PJM member declared in "breach" of its obligations pursuant to the terms of section 15.1 of the Operating Agreement will have two full business days to cure the breach prior to being declared in "default" of its obligations to PJM.⁷ PJM states that a member who fails to timely post collateral to securitize its market position has effectively transferred the credit risk to the rest of the PJM membership. PJM argues that it is an important distinction that, under the proposed revision, exclusion from PJM membership does not follow from multiple "breaches", but from multiple actual declared "defaults" of obligations. Furthermore, PJM clarifies that, under its proposal, "it would take three distinct collateral defaults in a twelve-month period to ultimately result in a [member's] expulsion."⁸

17. In response to AMP's concerns that municipal entities may face unanticipated budgeting constraints that may inhibit their ability to make timely payments or post required collateral when due, PJM explains it is able to provide more credit to municipalities than a purely formulaic administration of the tariff would otherwise allow.⁹ PJM asserts that it is precluded from terminating municipalities' transmission service

⁷ PJM Operating Agreement, section 15.1.5, Default Notification and Remedy.

⁸ PJM Answer at 5.

⁹ PJM Tariff, section 7.1A(b)(i); PJM Tariff, Attachment Q, section I.A.2.b; PJM Tariff, Attachment Q, Section I.B.2.b; PJM Tariff, Attachment Q, section II.

without first filing such a terminated request with the Commission,¹⁰ so AMP's concern that a municipality would inadvertently be subject to expulsion is unlikely.

18. PJM states that the proposed reinstatement limitation provisions in section 15.1.6 of the Operating Agreement are intended to apply to payment and collateral defaults only. According to PJM, the proposed reinstatement limitation provisions were drafted to parallel those Operating Agreement provisions related to breach notification and remedy,¹¹ which are applicable to member obligations broader than payment and/or creditworthiness standards. PJM states, however, that "the proposed provisions were not intended to be applicable to declaration of defaults outside the scope of payment and/or creditworthiness," and that "PJM would be open to amending the proposed language to accurately represent the intent of those provisions."¹²

19. PJM states that its proposed provisions allow it to enforce remedies consistent with authority already granted pursuant to the Tariff and Operating Agreement. PJM argues that its proposal should be read narrowly, because it is "implicit in the construction of Operating Agreement language that offered revisions should not ... conflict with [existing] rights ... found elsewhere in the Operating Agreement."¹³ Further, PJM claims that "it is clear that the reinstatement limitations do not bestow upon PJM an opportunity to create new termination rights."¹⁴ Rather, the proposal enhances existing provisions and clarifies the actions that PJM will take in reaction to repeated defaults, whereas the Tariff and Operating Agreement were silent before.

20. Finally, PJM addresses a member's right to appeal a PJM determination pursuant to the proposed provisions, asserting that these provisions are clear and concise. According to PJM, the proposal grants accused member recourse to the PJM dispute resolution process, an additional layer of process that would prevent relatively minor or

¹⁰ PJM Answer at 7-8. *See* PJM Operating Agreement at § 4.1(c) ("Any termination of this Agreement or withdrawal of any Member from the Agreement shall be filed with the FERC pursuant to section 205 of the Federal Power Act and shall become effective only upon the FERC's approval, acceptance without suspension, or, if suspended, the expiration of the suspension period before the FERC has issued an order on the merits of the filing.").

¹¹ Operating Agreement § 15.1.4.

¹² PJM Answer at 8.

¹³ PJM Answer at 9.

¹⁴ PJM Answer at 10.

incidental occurrences from ultimately resulting in expulsion. PJM states that, not only may an accused member dispute the decision using PJM's dispute resolution procedures but PJM also would be required to initiate a proceeding with the Commission to effectuate the termination. PJM states that its dispute resolution procedures make clear that "PJM is not the arbiter of any dispute brought by a member for dispute resolution."¹⁵ PJM argues that "discussion of the ramifications of a Member's expulsion in the context of the present filing is premature," because, for those terminations that are "subject to a filed proceeding with the Commission, PJM will be expected to address ... the consequences arising from the termination," at that time.¹⁶ Finally, PJM concedes that the language in its "three-pronged" criteria in Section 15.1.6(d) is imprecise, but states that the imprecision of the language is, by design, meant to allow for broader discretion on the part of the arbiter. PJM states that the language, as proposed, "gives the member the greatest possible chance that special circumstances should be considered."¹⁷

Discussion

21. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,¹⁸ the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2009), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept the answer filed by PJM because it has provided information that assisted the Commission in the decision-making process.

22. The Commission accepts PJM's proposed revisions to its credit policy, subject to conditions, to become effective, as requested, on January 1, 2010. As discussed below, the Commission directs PJM to make a compliance filing within 30 days of the date of this order. We will accept PJM's filing regarding termination and reinstatement subject to conditions. Under its existing tariff, a Member in default cannot participate in PJM's markets until the default is remedied. PJM has proposed a new provision that expands and extends its powers to terminate a Member that defaults multiple times, as well as providing more specific procedures for reinstatement. In general, we find this provision just and reasonable, subject to the condition discussed below.

¹⁵ PJM Answer at 11, citing PJM Operating Agreement Schedule 5, §3.2.

¹⁶ PJM Answer at 10-11.

¹⁷ PJM Answer at 12.

¹⁸ 18 C.F.R. § 385.214 (2008).

23. As an initial matter, we find PJM's proposed revision to peak market activity to account for loss of short-term load contracts and its proposed revision to allow up to ten early payments for members with unsecured credit reasonable and will accept them.

24. Contrary to AMP's assertions, we also find that PJM has proposed reasonable provisions to minimize the risk of loss from defaulting parties. PJM's proposal provides incentives to avoid defaults by having tiered reinstatement rights for members that have been in collateral and/or payment default, with possible expulsion as a last resort for those parties who continue to pose increased risks and costs on PJM and its members. It is reasonable for PJM to deny a member the ability to repeatedly default and cure without any repercussions, because, as PJM explains, such behavior results in increased administrative costs and inefficiencies for PJM and indicates increased financial risk exposure for PJM's membership.

25. Further, as explained by PJM, there are existing provisions in PJM's Tariff and Operating Agreement that allow a municipality to finance weekly bills in the event they are unable to make payments when due because of unanticipated budget constraints, and there are alternative unsecured credit provisions that reduce the likelihood of municipal payment or collateral defaults.¹⁹ In addition, PJM is precluded from terminating transmission service for Members without first filing for termination with the Commission.²⁰ Accordingly, the Commission believes that AMP's concerns about the possibility of expulsion of one of its municipalities is adequately addressed by these tariff provisions and the requirement that the Commission approve any termination of transmission service to municipalities.

26. We will accept PJM's filing regarding termination and reinstatement subject to conditions. Under its existing tariff, a member in default cannot participate in PJM's markets until the default is remedied. PJM has proposed a new provision that expands and extends its powers to terminate a Member that defaults multiple times, as well as

¹⁹ See PJM Tariff § 7.1A(b)(i) (assisting municipalities in financing weekly bills in the event of unanticipated budget constraints); PJM Tariff, Attachment Q § I.A.2.b; § I.B.2.b and § II (directing PJM to consider alternative measures when assessing the creditworthiness of municipalities).

²⁰ PJM Operating Agreement § 4.1(c) ("Any termination of this Agreement or withdrawal of any Member from the Agreement shall be filed with the FERC pursuant to section 205 of the Federal Power Act and shall become effective only upon the FERC's approval, acceptance without suspension, or, if suspended, the expiration of the suspension period before the FERC has issued an order on the merits of the filing.").

providing more specific procedures for reinstatement. In general we find this provision just and reasonable, subject to the condition discussed below.

27. AMP questions PJM's rights under subsections (b) and (c) to terminate a member in default for failing to adhere to any obligations of the Operating Agreement, arguing that this conflicts with PJM's intent to make those provisions applicable only to payment and/or collateral defaults. PJM's use of the phrase "shall be terminated" in subsection (c) also appears to be inconsistent with other sections of the Operating Agreement which, as PJM acknowledges in its answer, require PJM to seek Commission approval to effectuate a termination. In its answer, PJM offered to amend this proposed language to represent the intent of those provisions.²¹ We accept PJM's reinstatement provisions, conditioned on its filing within 30 days of the date of this order to clarify that such reinstatement provisions only apply to payment and collateral defaults, and that PJM cannot terminate membership without making a Federal Power Act section 205 filing with the Commission.

28. AMP states that PJM's filing is silent with respect to the impact of terminating the membership of a retail load serving entity, transmission owner or generator owner, and as to who would become responsible for serving the former member's load. We find that determining who is responsible for serving retail load in the event of a default goes beyond the scope of this proceeding and instead needs to be addressed in the first instances by the relevant entity (and state and local regulatory authorities as appropriate).

29. AMP states that the provisions addressing a former member's right to appeal for reinstatement are imprecise. AMP states that the Operating Agreement fails to specify who, as between PJM and the mediator or arbitrator selected to resolve the dispute pursuant to Schedule 5 to the Operating Agreement, will be responsible for determining whether the member has made the required demonstration as a condition to reinstatement. We do not find the provision ambiguous. Under the provision, the arbitrator would have the authority to make the final determination as to whether any of the three reasons provided in the tariff justify reinstatement.²²

30. Finally, AMP argues that PJM should carry the burden of proof in seeking to terminate a member's membership. According to AMP, section 15.1.6 does not require PJM to make any showing to the Commission before expelling a member from the RTO

²¹ PJM Answer at 8.

²² These three conditions are: (a) that it has otherwise consistently complied with its obligations under [the Operating] Agreement and the PJM Tariff; and (b) the failure to comply was not material, and; (c) the failure to comply was due in large part to conditions that were not in the common course of business.

and that it would presumably be left to the dissatisfied, expelled member to seek redress with the Commission via a complaint filed pursuant to section 206 of the Federal Power Act. We disagree. As PJM recognizes, under its tariff, it must file under section 205 of the FPA to terminate a member and the burden of proof in that proceeding therefore lies with PJM.

The Commission orders:

(A) PJM's proposed tariff revisions are hereby accepted, subject to condition, as discussed in the body of this order, to become effective, as requested, on January 1, 2010.

(B) PJM is hereby directed to make a compliance filing within 30 days of the date of this order, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.