

# Issues with PJM's Default Management Proposal

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# PJM's Request

- **PJM requests unlimited discretion to manage defaulted positions.**



# PJM's Request

- **PJM wants to have the discretion to pick the “prudent and practical” path from a number of options (“including but not limited to”) (September 17 MRC):**
  - **Closing out (presumably elimination, per MMU proposal)**
  - **Auctioning off portions of the portfolio across several regular auctions (similar to PJM’s pre December 2018 process)**
  - **Conduct one or more special FTR liquidation auctions.**

# PJM's Request

- **PJM states (September 17 MRC) that the goal of its discretionary approach would be to:**
  - **Minimize losses for non-defaulting participants**
  - **Limit significant price disruptions to the market**
  - **Taking into consideration: “Liquidity, Volatility, Size of the Portfolio, other market factors”**

# Unlimited Discretion is Not Appropriate

- **PJM does not propose rules defining how PJM would determine what is “prudent and practical” for any specific default event.**
- **The metrics for liquidity, volatility, size of the portfolio, other market factors have not been defined.**
- **The way in which such metrics would be evaluated and applied in the decision making process has not been defined.**
- **PJM has not explained how it would value different objectives if they conflict.**



# Unlimited Discretion

- **Without defined, reviewed and approved rules, there is no way to determine whether the decision making process used to pick an option or a set of options will:**
  - **Be prudent**
  - **Be practical**
  - **Recognize tradeoffs**
  - **Favor one set of participants**
  - **Be applied consistently**



# ISO/RTO Best Practices

- **Best practices in ISO/RTOs is to use a defined rule(s) approved by FERC.**
  - **Defaulted positions go to settlement is the most common rule.**
- **Best practices in ISO/RTOs is not to have discretion.**



# CCP Best Practices: Risk Management

- **Fundamental best practice in CCP industry (based on PJM discussion and industry papers ) is consistency.**
- **Consistent approach to risk management:**
  - **Onboarding criteria and creditworthiness standards**
  - **Effective risk controls and processes**
  - **Effective default management practices**
  - **Margining requirements**
- **PJM and the stakeholders are working on implementing consistent approach to risk management**
  - **Rule based, nondiscriminatory**

# CCP Discretion Not Applicable to PJM

- **PJM cite CCP12 paper as basis for CCP discretion in managing defaults across different products. The paper defines goals rather than actual practices.**
- **PJM concludes that PJM needs discretion in managing defaults for FTRs .**
- **PJM does not recognize the fundamental differences between CCPs and PJM.**
  - **CCP has its own assets at risk.**
  - **PJM does not.**

# PJM's Proposal Not Required for Margining

- **PJM's proposal does not create certainty.**
  - Does not eliminate volatility
  - Does not define the holding period
- **PJM's proposal is not required in order to discuss initial margining.**
- **To create certainty, rules governing a default management process need to be defined.**



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