143 FERC ¶ 61,233
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Philip D. Moeller, John R. Norris,
Cheryl A. LaFleur, and Tony Clark.

Dominion Energy Marketing, Inc.	Docket No. ER13-1291-000
ISO New England Inc.	EL13-72-000

ORDER GRANTING COST RECOVERY,
INSTITUTING SECTION 206 PROCEEDING,
AND ESTABLISHING REFUND EFFECTIVE DATE

(Issued June 14, 2013)

1. On April 15, 2013, pursuant to section 205 of the Federal Power Act (FPA)[1] and section III.A.15 of Appendix A to Market Rule 1 of the ISO New England Inc. (ISO-NE) Transmission, Markets, and Services Tariff (tariff), Dominion Energy Marketing, Inc. (Dominion) submitted a request seeking recovery of $336,095 in fuel costs, plus reasonable regulatory costs, for its Manchester Street Station Units,[2] which were mitigated under ISO-NE's Constrained Area Mitigation[3] and Reliability Commitment

[1] 16 U.S.C. § 824d (2006).

[2] Manchester Street Station (Manchester Street) is located in Providence, Rhode Island and consists of three combined-cycle generating units (Units 9, 10 and 11, referred to collectively as the Manchester Street Units), each having a current capacity supply obligation of approximately 140 MW. The Manchester Street Units are dual fuel capable and have oil storage tanks on site to provide a back-up fuel source.

[3] Under section III.A.5.5.2 of Appendix A, mitigation is applied to any resource that violates the Conduct Test and Impact Test for Constrained Area Energy and is determined to be within a constrained area.

Mitigation[4] processes. Additionally, Dominion requests the Commission direct ISO-NE to implement tariff changes before winter 2013-2014, which would ensure that resources that provide a critical reliability service at ISO-NE's request have a reasonable opportunity to recover costs associated with providing that service. As discussed below, we grant Dominion's fuel cost recovery request and grant subject to condition its request for regulatory costs. We will further institute a proceeding under section 206 of the FPA, in Docket No. EL13-72-000,[5] and require ISO-NE to submit tariff revisions to allow resources to submit a section 205 filing for cost recovery in circumstances where for reliability reasons a resource is dispatched: (1) beyond its day-ahead schedule, where there is no opportunity to refresh the offer price to reflect current costs; or (2) after the results of the day-ahead market schedule are published, where the resource did not receive a day-ahead market schedule. We will also establish a refund effective date.

I. **<u>Background</u>**

2. On February 8-10, 2013,[6] a significant snowfall resulted in the Manchester Street Units being one of the only generation resources capable of maintaining stability and voltage support in the Rhode Island (RI) and South East Massachusetts (SEMA) load zones, thus becoming critical to maintaining system reliability in that geographic region.[7]

3. ISO-NE dispatched the Manchester Street Units beyond their day-ahead energy market schedule and into the following operating day to support reliability on each of those days, February 8, 9, and 10. On Friday, February 8, after the deadline to nominate natural gas deliveries over the weekend on the pipeline serving Manchester Street, Algonquin Gas Transmission (Algonquin), ISO-NE notified the Manchester Street Units to continue to run beyond their day-ahead schedule. Additionally, while Manchester Street has dual fuel capability, ISO-NE directed that the Manchester Street Units continue

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[4] Under section III.A.5.5.5 mitigation is applied to any resource that violates the Conduct Test for Local Reliability Commitment Mitigation and is committed, or required to remain online, to provide one or more of the following: a) local first contingency protection or local second contingency protections; b) VAR or voltage support; or c) Special Constraint Resource Service.

[5] 16 U.S.C. §824e (2006).

[6] The dates in question occurred over a weekend, beginning on Friday, February 8.

[7] Transmittal at 2. Dominion states that ISO-NE discussed a series of operational issues at its March 2013 Participants committee meeting which further explain the reliability issues encountered during February 8-10. *Id.* at 3.

running on natural gas rather than come off-line to switch to fuel oil because doing so would carry additional reliability risks for the ISO-NE system.[8]

4. Dominion further notes that Algonquin established Capacity Constraint Notices on February 8-10, 2013, which precluded customers from burning more natural gas than nominated (during the Thursday and Friday timely nomination cycles), which meant that while Algonquin agreed to provide the additional natural gas transmission service, Dominion would be exposed to tariff-defined imbalance penalties if Dominion was not able to procure "post cycle" natural gas.[9] Dominion states that this subjected Manchester Street to extremely high spot market natural gas prices.

5. Dominion was unable to reflect these higher natural gas prices in its supply offer because, as Dominion explains, under the ISO-NE tariff, the only opportunity for market participants to update their supply offers is after the close of the day-ahead energy market, through the reoffer period, which at the time of the storm was between 4:00 pm and 6:00 pm. Market participants are able to change the supply offer's financial parameters during this reoffer period to, for example, reflect the change in fuel price. Thus, the latest time that Manchester Street would have been able to change its supply offer and reference price was at 6:00 p.m. the day before the operating day – well before ISO-NE directed the Manchester Units to continue operating beyond their day-ahead schedules.[10]

6. Dominion further states that, on the morning of February 8, 2013, while the natural gas markets were liquid, there was not a reasonable expectation that Manchester Street Units would run beyond their day-ahead schedules over the February 8-10, 2013 weekend. According to Dominion, the approaching storm significantly decreased load expectations and raised the likelihood that ISO-NE would call a Minimum Generation Emergency. Indeed, consistent with its expectations, the Manchester Street units were awarded a day-ahead schedule of only a few evening hours. Moreover, Dominion states that it expected that it would be permitted to run on fuel oil if the Manchester Street Units were dispatched beyond their day-ahead energy market award. However, as noted above, late on all three days, after the last opportunity to nominate natural gas deliveries on the

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[8] The Manchester Street Units must be brought off-line to switch fuel sources due to environmental restrictions and operational procedures.

[9] "Post cycle" gas is the term Dominion uses to describe natural gas that is available after the last pipeline nomination cycle. While the pipeline has no obligation to do so, it sometimes permits generators to nominate post cycle natural gas.

[10] Transmittal at 3-4.

Algonquin pipeline (6:00 p.m.), ISO-NE requested that the Manchester Street units run beyond their day-ahead energy market schedule and to continue burning natural gas, rather than switch to fuel oil. In order to run through the night on natural gas, Dominion states that it needed to procure additional natural gas during the weekend and within the operating day at a significant premium over the cost of procuring natural gas during the timely nomination window the day before the operating day. [11] Dominion states that, as a result of being dispatched beyond the day-ahead awards and not being able to switch to fuel oil, i.e., by complying with ISO-NE's reliability directives, Dominion under-recovered its fuel costs by approximately $2.4 million.

II. <u>Cost Recovery Filing and Tariff Revision Proposal</u>

7. Section III.A.15 of Appendix A to the ISO-NE tariff currently allows a market participant to seek additional cost recovery under section 205 of the FPA, if, *as a result of mitigation* applied under Appendix A, it will not recover the fuel and variable operating and maintenance costs of a resource for all or part of one or more operating days. Specifically, section III.A.15.1 provides that:

> If either (a) *as a result of mitigation* applied to a Resource under this Appendix A for all or part of one or more Operating Days, or (b) in the absence of mitigation, despite having submitted a Supply Offer at the energy offer cap specified in Section III.1.10.1.A(d) of Market Rule 1, a Market Participant believes that it will not recover the fuel and variable operating and maintenance costs of the Resource for those Operating Days, the Market Participant may, within sixty days of the receipt of the first Invoice issued containing credits or charges for the applicable Operating Day, submit a filing to the Commission seeking recovery of those costs pursuant to Section 205 of the Federal Power Act. (Emphasis added).

Section III.A.15.2 provides that:

> Any Section 205 filing made pursuant to this section shall include: (i) the actual fuel and variable operating and maintenance costs for the Resource for the applicable Operating Days, with supporting data and calculations for those costs; (ii) an explanation of (a) why the actual costs of operating the Resource for the Operating Days exceeded the Reference Level costs or, (b) in the absence of mitigation, why the actual costs of operating the Resource for the Operating Days exceeded the costs as reflected in the Supply Offer

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[11] Dominion notes that natural gas markets lack liquidity on weekends, thus the spot market prices are higher. Transmittal at 4.

> at the energy offer cap; (iii) the Internal Market Monitor's [(IMM)] written explanation provided pursuant to Section III.A.15.3; and (iv) all requested regulatory costs in connection with the filing.

8. Dominion explains that the IMM mitigated Manchester Street's February 10 supply offers below the units' actual fuel costs but did not mitigate the Manchester Street Units' offers on February 8 or 9 because the supply offers were below the mitigation reference price.[12] Dominion states that its day-ahead supply offers for February 8 and 9 also were below the units' actual incurred fuel costs when they were dispatched in real-time beyond their day-ahead schedule.

9. Consistent with section III.A.5, Dominion requests fuel cost recovery of $336,095, plus reasonable regulatory costs, for its unrecovered costs incurred relating to only the February 10 operating day. Dominion states that, pursuant to ISO-NE's tariff, it previously submitted to the IMM its actual fuel costs and supporting material. The IMM issued a report supporting Dominion's request for additional cost recovery for February 10. Dominion states that it has complied with the section III.A.15 requirements for a cost recovery filing for the February 10 costs and that the IMM agrees that Dominion properly complied. However, the IMM concluded that Dominion did not satisfy the requirements for additional cost recovery for February 8 or 9 because, under the tariff, mitigation of supply offers is a necessary pre-condition for market participants to seek additional cost recovery when the actual costs of operating the resource are under-recovered.

10. Dominion further states that while it is not seeking here to recover its roughly $2 million in additional fuel costs for February 8 and 9, it requests that the Commission direct ISO-NE to implement tariff changes before winter 2013-2014 that would: (1) provide a mechanism for generation resources committed for reliability to recover their fuel costs incurred in meeting the reliability need without first having its supply offer mitigated and without submitting a section 205 filing to the Commission; and (2) allow resources to update their supply offers in real-time to reflect changes to their operating costs.[13]

11. Dominion challenges the tariff as forcing generators to incur the administrative burden and associated costs of making a section 205 filing every time they are unable to recover fuel costs, because, according to Dominion, the mitigation reference prices do not accurately reflect those costs. Dominion opines that under the tariff, ISO-NE cannot

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[12] *Id.* at 4.

[13] *Id.* at 7.

accommodate timely supply offers that reflect the true marginal costs of energy. Moreover, Dominion adds that the tariff provides a perverse incentive for generators to submit supply offers with the purpose of being mitigated, because mitigation is a prerequisite to recovering costs not reflected in supply offers. Absent mitigation, generators are in the position of incurring significant and unrecoverable fuel costs and potential pipeline penalties in order to meet ISO-NE's system reliability needs.[14]

12. Dominion states that ISO-NE acknowledged these shortcomings in a November 30, 2012 Energy Market Enhancements White Paper and currently is evaluating proposed market rule enhancements for implementation in late 2014, which will allow resources to modify their offers in real-time to reflect increases in fuel costs. Dominion asserts that ISO-NE must move forward with planned market rules changes now to ensure that resources that serve a critical reliability need have a reasonable opportunity to recover their fuel costs associated with meeting that need.

13. Dominion posits that its requested tariff revisions will help resolve a current disconnect between the New England electric and natural gas markets, and ensure that resources called upon to support system reliability are able to recover their costs and that the New England market design produces outcomes where the marginal price of electric energy accurately reflects the cost of the marginal resource.[15]

III. Notice of Filing and Responsive Pleadings

14. Notice of Dominion's filing was published in the *Federal Register*, 78 Fed. Reg. 24,191 (2013) with interventions and protests due on or before May 6, 2013. On May 6, 2013, New England Power Pool Participants Committee (NEPOOL) filed comments, and ISO-NE filed a motion to intervene and limited protest. On May 22, 2013, Dominion filed an answer.

IV. Discussion

A. Procedural Issues

15. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2012), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

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[14] *Id.* at 10.

[15] *Id.* at 10-11.

16. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2012), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept Dominion's answer because it has provided information that assisted us in our decision-making process.

B. Comments and Protest

17. ISO-NE generally supports Dominion's request for additional cost recovery for February 10, in the amount of $336,095 plus Dominion's regulatory costs. NEPOOL takes no position on the amount but acknowledges Dominion's right under the tariff to submit a request for recovery of fuel costs and affirms that it is properly submitted under section 205 of the FPA.[16]

18. NEPOOL and ISO-NE oppose Dominion's request for a Commission order directing that ISO-NE change its tariff, stating that the request is procedurally improper in a section 205 proceeding. NEPOOL states that ISO-NE is the entity authorized to file changes to its tariff and market rules under section 205, and ISO-NE has not sought any changes in this proceeding. NEPOOL further states that a market participant's request to change market rules on file with the Commission is properly raised in a complaint under section 206 of the FPA. ISO-NE also contends that Dominion must meet the substantive burden of proof that would be required under a section 206 complaint, which Dominion has failed to do.

19. NEPOOL argues that Dominion's proposed changes should be addressed first in the stakeholder process and not in a Commission proceeding without the benefit of stakeholder consideration. Indeed, NEPOOL and ISO-NE state that the stakeholders are already considering some of Dominion's requested changes, including a proposal that allows for updating supply offers in real-time throughout the operating day.

20. ISO-NE further states that, even if the stakeholders and the Commission ultimately approve new hourly offer rules, substantial software changes would be necessary to implement them, so having those rules in place by winter 2013-2014, as Dominion requests, is impracticable. ISO-NE explains that the changes proposed in the stakeholder process will require, among other things, extensive modifications to database functions and information technology enhancements, as well as a number of revisions to other parts of the tariff, including Net Commitment Period Compensation (uplift). ISO-NE states that its implementation timetable for these changes is aggressive and reflects the high priority that ISO-NE and stakeholders have placed on the implementation of the hourly

[16] NEPOOL Comments at 1-2.

offer flexibility rules. ISO-NE confirms that it currently anticipates implementing certain hourly rule changes during the fourth quarter of 2014.

21. Regarding Dominion's request that the tariff be modified in the interim to provide a mechanism for generation resources committed for reliability to recover their actual fuel costs without having their supply offers mitigated, and without having to submit a section 205 filing with the Commission, ISO-NE argues that such a change is incompatible with competitive markets. Specifically, ISO-NE states that binding offers are fundamental to markets, and if offers are not binding, then the prices based on those offers are not reliable indicators of the cost of providing electricity. ISO-NE states that inaccurate prices would undermine both buyers' and sellers' confidence in the market.

22. ISO-NE also states that, to the extent Dominion seeks a tariff-based, out-of-market payment mechanism to recover fuel costs that are not reflected in generators' supply offers, such a mechanism also would undermine the accuracy of submitted offers. ISO-NE asserts that it would provide market participants with an incentive to submit low, non-competitive offers in instances where they anticipate a reliability event in order to increase their chance of being selected, with the expectation of receiving an out-of-market payment to recover their actual costs. ISO-NE notes that such an incentive would be especially problematic during times of natural gas pipeline constraints, when the natural gas market is less liquid and more volatile. ISO-NE explains that, under such circumstances, it is particularly important that resource offers and resulting prices reflect the best information available to each resource about fuel prices and availability, and the possibility of essentially riskless participation in the fuel markets would provide the greatest advantage to a resource selected to run for reliability. ISO-NE adds that the out-of-market payment mechanism would significantly erode the potential of the market clearing price to reflect the competitive cost of supplying energy, confer an unfair advantage to certain resources, and would subject consumers to significant uncertainty regarding energy prices.

C. Answer

23. Dominion responds that the market rule changes it requests can be both directed by the Commission and accomplished through the ongoing stakeholder process. Dominion agrees that any market rule changes should be vetted in the existing stakeholder process, and Dominion deliberately elected not to file a section 206 complaint at this time to allow that process to move forward expeditiously. However, Dominion states that it strongly disagrees that the reforms outlined in its cost recovery filing should be delayed beyond winter 2013-2014, especially since, according to Dominion, ISO-NE identified the need to address generator offer flexibility almost 10

years ago.[17] Acknowledging that ISO-NE may not be able to implement a long-term solution prior to winter 2013-2014, Dominion seeks an interim mechanism for generation resources committed for reliability to recover their fuel costs incurred in meeting a reliability need without the necessity of having its supply offer first mitigated and without having to submit a section 205 filing. Dominion explains that there would be no market manipulation concerns with its proposal, considering that a market participant cannot accurately predict a reliability event and submit a non-competitive offer in anticipation of an event.

D. Determination

1. Dominion's Request for Cost Recovery

24. The Commission grants Dominion's fuel cost recovery request of $336,095, plus reasonable regulatory costs incurred in connection with this filing, subject to Dominion submitting a compliance filing detailing the actual regulatory costs.[18] Dominion followed the requirements of section III.A.15 of Appendix A to the tariff to obtain the cost recovery for additional costs incurred on February 10. According to the tariff, a resource's supply offer must be mitigated in order for the IMM to approve a cost recovery request. Dominion's supply offer for February 10 was mitigated and it submitted a cost recovery request to the IMM for the costs it incurred on February 8-10. As noted above, the IMM issued a report supporting Dominion's request for cost recovery for February 10 but finding that because mitigation is a necessary pre-condition for market participants to receive cost recovery under the tariff, Dominion did not satisfy the requirements for additional cost recovery for February 8 or 9. Once the IMM provides a written explanation to the market participant on its cost recovery request, and, within 60 days of that explanation, the market participant can exercise its right to submit a cost recovery filing to the Commission under section 205. It is undisputed that Dominion properly exercised that right here.

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[17] *See* "ISO New England's Management Response to the October 12, 2004 publication entitled Final Report on Electricity Supply Conditions in New England during the January 14-16, 2004 'Cold Snap,'" October 12, 2004, *available at* http://www.iso-ne.com/pubs/spcl_rpts/2004/iso_management_response_cold_snap.pdf, 14-16. *See also* Transmittal at 9.

[18] Dominion states that its regulatory costs will be based solely on fees and costs for outside and in-house counsel and will not include any costs associated with work performed by other employees of Dominion or its affiliates. *See* Transmittal at 7.

2. <u>Dominion's Request for Tariff Changes</u>

25. Pursuant to the Commission's authority under section 206 of the FPA, we find that ISO-NE's existing tariff, in particular section III.A.15 of Appendix A, is unjust, unreasonable, unduly discriminatory or preferential, because it does not provide resources an adequate opportunity to recover costs incurred to comply with ISO-NE directives to ensure reliability in instances when their supply offers were not mitigated. In situations such as the one Dominion experienced on February 8 and 9, despite complying with ISO-NE's directives to maintain reliability, resources could suffer significant financial loss in unrecovered costs.[19] The Commission finds that this outcome for resources called upon to respond to critical reliability needs is unjust and unreasonable.

26. Therefore, pursuant to our authority under section 206 of the FPA, we direct ISO-NE to submit tariff revisions which allow resources to submit a section 205 filing for cost recovery, including fuel and variable operation and maintenance costs for the resource, in circumstances where for reliability reasons a resource is dispatched: (1) beyond its day-ahead schedule, where there is no opportunity to refresh the offer price to reflect current costs; or (2) after the results of the day-ahead market schedule are published, where the resource did not receive a day-ahead market schedule. This provision will be in addition to the current provisions allowing cost recovery when a resource is mitigated or when a supply offer was submitted at the energy offer cap; therefore, a resource seeking cost recovery would follow the same cost recovery process for a bid that was mitigated or offered at the energy offer cap, i.e., submit the request to the IMM for analysis prior to submitting a section 205 filing to the Commission. We direct ISO-NE to submit these revisions in a compliance filing no later than 45 days from the date of this order.

27. The Commission acknowledges ISO-NE's concerns that imposing a mechanism to allow generation resources committed for reliability purposes to recover their actual fuel costs incurred in meeting the reliability need could undermine the accuracy of submitted offers or incentivize market participants to submit low offers in anticipation of a reliability event in order to increase their chance of being selected or high offers in order to be mitigated and therefore eligible for cost recovery. However, the existing tariff already suffers from similar defects, encouraging resources to submit supply offers with the intent of being mitigated in order to assure cost recovery through the cost recovery mechanism. On balance, the Commission finds that it is appropriate to require that resources providing critical reliability services have a reasonable opportunity to recover costs associated with providing that service.

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[19] Some of Dominion's supply offers were based on natural gas as the fuel source while others were based on oil.

28. To provide guidance to ISO-NE as it prepares its compliance filing, the Commission expects that the parameters of the tariff provision(s) directed here will be sufficiently restrictive to discourage anticompetitive offering behavior but still allow for cost recovery in circumstances, for example, when a resource responds to a directive from ISO-NE to provide essential support to part of the system but has no reasonable opportunity to recover its costs. In other words, the tariff provision should ensure that a resource would be permitted to seek cost recovery, where, for instance, a resource submits an offer based on one fuel type but is required to run on another or cannot burn natural gas based on an Operation Flow Order restriction. These examples are not intended to be exhaustive and should not unduly limit the criteria ISO-NE develops for cost recovery under extraordinary circumstances. Our intention is for ISO-NE's tariff to provide enough flexibility to allow for cost recovery by resources that respond under extraordinary circumstances like those faced by the ISO-NE market on February 8 and 9.

29. The Commission also acknowledges that ISO-NE and its stakeholders are discussing comprehensive long-term changes to ISO-NE's market rules, which may address our concerns regarding the existing tariff. However, as ISO-NE admits, those changes will not be in effect for winter 2013-14, necessitating our action here. The Commission does not intend to prejudge any alternative approaches that might result from the stakeholder process, but, at the same time, recognizes the need to address critical reliability concerns in the near-term. We understand that the cost-recovery mechanism required herein may be replaced by a long-term solution resulting from the on-going stakeholder process.

30. In cases where, as here, the Commission institutes a proceeding under section 206, section 206(b) of the FPA requires that the Commission establish a refund effective date that is no earlier than publication of notice of the Commission's initiation of its proceeding in the *Federal Register*, and no later than five months subsequent to that date. We establish a refund date to be the earliest date possible in order to provide maximum protection to customers, i.e., the date that notice of initiation of the section 206 proceeding in Docket No. EL13-72-000 is published in the *Federal Register.*

<u>The Commission orders</u>:

(A) Dominion's request for fuel cost recovery, plus reasonable regulatory costs incurred in connection with this filing, is hereby granted, subject to a compliance filing detailing the actual regulatory costs, as discussed in the body of this order.

(B) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Commission by section 402(a) of the Department of Energy Organization Act and by the FPA, particularly section 206 thereof, and pursuant to the

Commission's Rules of Practice and Procedure and the regulations under the Federal Power Act (18 C.F.R., Chapter I), the Commission hereby institutes a proceeding in Docket No. EL13-72-000, as discussed in the body of this order.

(C) ISO-NE is hereby directed to submit a compliance filing revising section III.A.15 of Appendix A no later than 45 days from the date of this order, as discussed in the body of this order.

(D) The Secretary shall promptly publish in the Federal Register a notice of the Commission's initiation of the proceeding ordered in Ordering Paragraph (B) above, under section 206 of the FPA.

(E) The refund effective date established pursuant to section 206(b) of the Federal Act will be the date of publication in the *Federal Register* of the notice discussed in Ordering Paragraph (D) above.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.