

146 FERC ¶ 61,078  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

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

PJM Interconnection, L.L.C.

Docket No. ER14-1145-000

ORDER GRANTING WAIVER

(Issued February 11, 2014)

1. PJM Interconnection, L.L.C. (PJM) filed a request for temporary waiver – from the date of a Commission order through March 31, 2014 – of provisions of the Amended and Restated Operating Agreement of PJM Interconnection, L.L.C. (Operating Agreement) and the PJM Open Access Transmission Tariff (Tariff) in response to unprecedented spikes in fuel costs caused by recurring extreme cold weather events. The requested waiver is to permit submissions of cost-based offers from Generation Capacity Resources into the PJM energy markets at prices that exceed the \$1,000/MWh offer-price cap.<sup>1</sup> PJM requests expedited relief. As discussed below, the Commission finds good cause to grant the requested waiver.

**I. Background and Details of the Filing**

2. On January 23, 2014, PJM filed concurrently two requests for waiver of section 1.10.1A(d) of Schedule 1 of the Operating Agreement and the equivalent section of Attachment K-Appendix to the Tariff,<sup>2</sup> in Docket Nos. ER14-1144-000 and ER14-1145-000. In Docket No. ER14-1144-000, PJM requested temporary waiver – from January 24, 2014 to March 31, 2014 – of these Tariff provisions to permit sellers that submit cost-based offers from Generation Capacity Resources into the PJM energy markets and whose costs exceed the applicable energy market clearing price to receive a

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<sup>1</sup> Capitalized terms used but not defined herein are intended to have the meaning given to such terms in the Operating Agreement and the PJM Open Access Transmission Tariff, as applicable.

<sup>2</sup> PJM Operating Agreement, Schedule 1, Section 1.10 - Scheduling (14.0.0); PJM Tariff, Attachment K Appendix, Section 1.10 Scheduling (14.0.0).

make-whole payment covering the difference between their costs and the clearing price. PJM requested expedited relief in Docket No. ER14-1144-000, and explained that this waiver request would be superseded by the relief requested here in Docket No. ER14-1145-000. On January 24, 2014, the Commission issued an order granting the requested waiver in Docket No. ER14-1144-000.<sup>3</sup>

3. In the instant filing, PJM explains that the Operating Agreement provides that resources that have been committed as capacity shall submit offers into the day-ahead energy market for the available capacity of their resources; however, section 1.10.1A(d) of Schedule 1 of the Operating Agreement also provides that offers in the day-ahead energy market shall not exceed an energy offer price of \$1,000/MWh. PJM explains that published natural gas prices at two key citygates in the PJM region recently averaged over \$120/MMbtu and included prices up to \$140/MMbtu. PJM states that these gas prices are unprecedented in the PJM region.<sup>4</sup> PJM states that these record-setting prices would equate to a marginal energy cost for a simple-cycle combustion turbine (CT) generator of approximately \$1,200/MWh. PJM also notes that, on January 21, 2014, it saw approximately 5,000 MWs of energy market offers in the day-ahead market at a price of \$999/MWh, implying that the costs for these resources were above the \$1,000/MWh but their offers were constrained by the offer cap. PJM states that this situation is untenable because it does not provide the affected generators an opportunity to recover their costs of generating the energy that they are required to offer into the PJM market.

4. Accordingly, PJM requests a waiver of section 1.10.1A(d) of Schedule 1 of the Operating Agreement, and the equivalent section of Attachment K-Appendix to the Tariff, effective from the date of a Commission order through March 31, 2014, to permit Generation Capacity Resource sellers that submit cost-based offers from Generation Capacity Resources into the PJM energy markets to do so at prices that exceed the \$1,000/MWh offer-price cap. PJM explains that this will ensure that not only generators submitting cost-based offers can recover their marginal costs of sales into PJM's energy market, but also that the price in that market will correctly reflect the marginal costs of those sellers when they are needed to serve PJM loads. PJM argues that this is consistent with Commission policy, which recognizes that “[p]ayments made only to individual

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<sup>3</sup> *PJM Interconnection, L.L.C.*, 146 FERC ¶ 61,041 (2014) (January 24, 2014 Order).

<sup>4</sup> PJM Transmittal at 7.

resources and recovered in uplift fail to send clear market signals” and resource costs instead “should be reflected in transparent market prices whenever possible.”<sup>5</sup>

5. PJM explains that the substance of the proper determination of cost-based offers for a seller would not change – all that would change is that the calculation of the cost-based offers would not be cut off at \$1,000/MWh. PJM states that the seller’s marginal costs must be as determined and documented in accordance with the cost development guidelines and procedures in PJM’s Manual 15, and PJM will apply unchanged the Fuel Cost Guidelines in Manual 15.<sup>6</sup>

6. PJM argues that there is good cause to grant the requested waiver. PJM states that it is limited in scope, both in time period (the remainder of the winter season) and in nature (limited to Generation Capacity Resources that have legitimate costs over \$1,000/MWh). PJM explains that the waiver resolves a concrete problem, i.e., the conflict between the must-offer requirement and the offer cap precipitated by the recent elevated natural gas prices. PJM argues that no market participants can claim any legitimate harm because the PJM market has always been premised on seller recovery of marginal costs and on clearing prices based on marginal costs. Furthermore, PJM argues that sellers are entitled to the proposed cost recovery only for their cost-based offers that are cleared and that are therefore necessary to the reliable operation of the PJM region’s grid.

7. PJM requests Commission action by February 10, 2014.

## **II. Notice and Responsive Pleadings**

8. Notice of PJM’s filing was published in the *Federal Register*, 79 Fed. Reg. 5,397 (2014), with interventions and protests due on or before January 30, 2014. Timely motions to intervene were filed by Edison Mission Energy, Duke Energy Corporation, Delaware Public Service Commission, PJM Industrial Customer Coalition, Consolidated Edison Energy, Inc., America’s Natural Gas Alliance, Calpine Corporation, The Dayton Power and Light Company, American Electric Power Service Corporation, Macquarie Energy, LLC, Direct Energy Business, LLC and Hess Energy Marketing, LLC, Franklin Power, LLC, North Carolina Electric Membership Corporation, Old Dominion Electric Cooperative, PSEG Companies, Sapphire Power Finance LLC and Raven Power Finance

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<sup>5</sup> *Id.* at 8 (citing *PJM Interconnection, L.L.C.*, 139 FERC ¶ 61,057 at P 78, n.72, *reh’g denied*, 141 FERC ¶ 61,096 (2012) (*PJM*)).

<sup>6</sup> *Id.* at 7.

LLC. Motions to intervene and comments were filed by the PPL Parties;<sup>7</sup> Electric Power Supply Association (EPSA); PJM Power Providers Group (P3); Exelon Corporation (Exelon); DC Energy, LLC (DC Energy); Independent Market Monitor for PJM (PJM IMM); FirstEnergy Service Company (FirstEnergy); Retail Energy Supply Association (RESA). Duke Energy Ohio, Inc., AEP, and Dayton (collectively, AEP) filed joint comments. Motions to intervene and protests were filed by the Maryland Public Service Commission (Maryland PSC), NextEra Energy Power Marketing, LLC (NEPM), Public Power Association of New Jersey (PPANJ), American Municipal Power, Inc. (AMP), Washington Gas Energy Services, Inc. (WGES), Ethical Electric, Inc. (Ethical Electric), and the Consumer Representatives.<sup>8</sup>

9. On January 31, 2014, Champion Energy Services, LLC (CES) filed a motion to intervene out-of-time. On February 3, 2014, the Illinois Commerce Commission and NRG Companies filed motions to intervene out-of-time. On February 5, 2014, TAQA Gen X LLC and Dominion Resources Services, Inc. each filed a motion to intervene out-of-time. On February 7, 2014, Dynegy Kendall Energy, LLC, Ontelaunee Power Operating Company, and Dynegy Marketing and Trade, LLC (collectively, Dynegy) filed a motion to intervene out-of-time.

10. On February 3, 2014, PJM filed an answer to comments and protests. On February 4, 2014, NEPM filed an answer to PJM's answer. On February 5, 2014, RESA filed an answer to PJM's answer. On February 6, 2014, the Maryland PSC filed an answer to PJM's answer.

**A. Comments**

11. Several commenters provided supporting comments for PJM's waiver, arguing that fuel costs incurred by generators are more appropriately reflected in the market

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<sup>7</sup> For purposes of this proceeding, the PPL Parties are: PPL EnergyPlus, LLC; PPL Brunner Island, LLC; PPL Holtwood, LLC; PPL Ironwood, LLC; PPL Martins Creek, LLC; PPL Montour, LLC; PPL Susquehanna, LLC; Lower Mount Bethel Energy, LLC; PPL New Jersey Solar, LLC; PPL New Jersey Biogas, LLC; and PPL Renewable Energy, LLC.

<sup>8</sup> The Consumer Representatives are the PJM Industrial Customer Coalition, Consumer Advocate Division of West Virginia, Delaware Division of the Public Advocate, Illinois Citizens Utility Board, Indiana Office of Utility Consumer Counselor, Maryland Office of People's Counsel, New Jersey Division of Rate Counsel, Office of the People's Counsel of the District of Columbia, and Pennsylvania Office of Consumer Advocate.

clearing price, rather than being recovered through uplift payments.<sup>9</sup> Exelon contends that accounting for fuel costs through uplift would result in inaccurate market prices. Exelon argues that granting the waiver will allow actual market conditions to be reflected in the market price, appropriately reflecting the cost of producing energy, which is particularly important in a time of extreme cold weather events. Exelon states that the Commission should approve this waiver as soon as possible to not only ensure that generators are not required to operate at a loss, but to support accurate price formation and reliable operations going forward.

12. EPSA contends that LMPs should reflect the marginal costs of sellers, especially at times when the market is stressed, agreeing with PJM's statements that the principle of basing market clearing prices on the costs of cleared sell offers is fundamental to PJM's market design. EPSA states that, as such, this principle should not be set aside, however briefly, and particularly not at times when seller costs are highest.<sup>10</sup>

13. Several commenters argue that parties would be financially harmed if fuel costs were accounted for through uplift, instead of through LMPs.<sup>11</sup> According to RESA, their members are able to hedge costs in the energy market, but unable to effectively hedge uplift costs. Thus, RESA states, "unless these increased fuel costs are reflected in the locational marginal pricing in the Day Ahead energy market, these costs will fall to retail suppliers who have no way of managing these costs or reflecting them in prices to customers aside from invoking contractual 'change in law/regulation' provisions if they exist."<sup>12</sup> PPL Parties state that accounting for high fuel costs through uplift unfairly and discriminatorily burdens market participants who planned in advance and hedged their positions.<sup>13</sup> DC Energy recommends that the Commission continue its policy of supporting efficient energy markets rather than relying on out-of-market uplift charges that compensate generators on a pay-as-bid model, and requests that the Commission

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<sup>9</sup> Exelon at 2-6, DC Energy at 1-3, PJM IMM at 1, PPL Parties at 4-8, P3 at 5-9, FirstEnergy at 2-4, AEP at 1, and EPSA at 3-7.

<sup>10</sup> EPSA at 3-4.

<sup>11</sup> RESA at 5, PPL Parties at 5, Exelon at 5, and P3 at 5 and 8-10.

<sup>12</sup> RESA at 3.

<sup>13</sup> PPL Parties at 5.

apply PJM's approach in this proceeding in the New York Independent System Operator waiver request proceeding in ER14-1138-000.<sup>14</sup>

14. FirstEnergy and P3 note that markets have changed since the introduction of the offer cap.<sup>15</sup> Specifically, P3 states that the price cap was never intended to be a permanent feature of the PJM market and that "the growth in demand response in PJM since 2002 suggests that there may be good cause to address whether an offer cap is even necessary in today's market."<sup>16</sup> Also, according to P3, it is critically important that the Commission act on the waiver request as quickly as possible because the current interim relief undermines fundamental tenants of the market and punishes market participants who will be asked to fund the uplift. P3 claims that failure to address this inequity will lead market participants to manage their uplift risk rather than responding to market signals, which will result in an upward price spiral.<sup>17</sup>

15. In order to facilitate accurate price formation, EPSA and PPL Parties suggest that the Commission direct PJM to work with market participants and other stakeholders on long-term, efficient investment decisions and price formation outcomes.<sup>18</sup>

16. The PJM IMM states that it supports PJM's request for waiver but recommends that an order approving the waiver request clarify that price-based offers should be permitted to exceed \$1,000/MWh only if they equal the cost-based offer.<sup>19</sup>

## **B. Protests**

17. Protestors argue that the Commission should deny PJM's requested waiver. NEPM and Maryland PSC state that truncating the Commission's 60-day review period for a section 205 filing, giving affected parties seven days to comment, is unjustified. Additionally, NEPM and AMP maintain that PJM has bypassed the stakeholder process, which they state is the appropriate forum to debate changes to the Operating Agreement.

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<sup>14</sup> DC Energy at 1-2.

<sup>15</sup> FirstEnergy at 2, and P3 at 2-5.

<sup>16</sup> P3 at 3-4.

<sup>17</sup> *Id.* at 7-9.

<sup>18</sup> EPSA at 3 and 8, PPL Parties at 9, Exelon at 4-5, RESA at 6-7 and AEP at 2.

<sup>19</sup> PJM IMM at 1.

18. Maryland PSC argues that PJM has not provided data identifying how much inefficient CT capacity it has on its system and how much other, more efficient gas-fired generators, are experiencing the alleged problem. In addition, the Consumer Representatives argue that PJM provides no evidence for the record high price levels it claims occurred.<sup>20</sup>

19. Several protestors argue that PJM has not met the requirements for a waiver because it is not limited in scope. AMP and Ethical Electric argue that it amounts to a fundamental market rule change, and NEPM, Maryland PSC, and PPANJ argue that it is broad, not narrow like the first request, and does not respond to any residual emergency condition. The Consumer Representatives argue that PJM has failed to meet its burden to show that the waiver is limited in scope because it has failed to show that the requested waiver is necessary for all regions of PJM. In addition, the Consumer Representatives argue that the waiver has significant and broad implications for customers' prices and for commercial transactions in the PJM region because: (1) any market clearing price that exceeds \$1,000/MWh will directly and significantly affect customers' prices, and (2) the regulatory and pricing risk associated with exceptions to the offer-price cap rule will increase the cost of hedging instruments long after March 31, 2014.

20. Protestors argue that the request does not address a concrete problem because the Commission already addressed any problem in the January 24, 2014 Order, which relieved the potential for generators in PJM to sell at a price below their marginal costs, and that no further emergency relief is needed. The Consumer Representatives argue that cleared Capacity Resources knew or should have known that they would be required to bid into the Day-Ahead Energy Market at \$1,000/MWh or less, had adequate time between submitting their offers and the time that natural gas prices spiked to hedge themselves against the possibility of increased natural gas costs, and those who did not enter into fuel delivery agreements to hedge their risk and decided instead to purchase natural gas on the spot market made a conscious business decision to do so. The Consumer Representatives assert that customers should not be forced to cover any extra costs associated with generators' failure to hedge against the risk of price fluctuations. Similarly, the Consumer Representatives argue that generators that had dual fuel capability were able to protect themselves from the spike in natural gas prices by switching to the much cheaper fuel oil source, and customers should not be charged increased prices for risks that generators consciously assumed by making the business

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<sup>20</sup> The Consumer Representatives state that, while there is evidence that prices in the Texas Eastern M-3 zone may have exceeded \$90/MMbtu, there is also evidence of trades at much lower prices for the same flow day. Consumer Representatives Protest at 5.

decision to not install dual fuel capability. Ethical Electric asserts that the cost for a seller to protect the price for the Generation Resource by purchasing call options for firm gas supply at a price level that enables the seller to meet the price cap is very inexpensive when the forward curve for natural gas is well under \$10 per MMBtu.

21. Finally, protestors argue that granting waiver will cause third-party harm because market participants rely on longstanding market rules and make contractual commitments based on those rules. Consumer Representatives argue that many market participants have already undertaken significant supply commitments to hedge against natural gas price exposure based upon the \$1,000/MWh cap, as NEPM represents that it has done. AMP, Maryland PSC, and Consumer Representatives argue that granting the waiver will result in wholesale and retail customers paying significantly more than the make-whole payments already authorized by the Commission, and Maryland PSC estimates that this could easily reach several hundred million dollars.<sup>21</sup> AMP explains that, while the uplift mechanism limits the amount allocated to the other market participants to the incremental amount of that generator's costs above the \$1,000/MWh cap, raising the market clearing price to reflect the extraordinary costs of the uneconomic generator will allow all generators who clear to get paid this higher LMP amount.

22. Maryland PSC argues that the price cap is established at a level that the Commission believes will, given the risk that market participants may exercise market power in each market, be sufficient to protect end users from unjust and unreasonable rates and is an essential component of PJM market design. Maryland PSC states that the Commission has permitted recovery of demonstrated costs by affected suppliers through an "above the offer" price ceiling but has directed that these higher, aberrant costs should not be permitted to establish market clearing prices to be paid to other generators not affected by the atypical cost pressures.<sup>22</sup> NEPM argues that, when prices are extremely high, like the circumstances caused by the "polar vortex," it is all the more important for market participants to be able to rely on a market rule that protects against unlimited price exposure and to not change that rule without a stakeholder process.

23. Consumer Representatives argue that, because the least efficient generators that chose not to hedge will set the market-clearing price, the incentives for other resources to optimize fuel delivery arrangements and operational efficiency are significantly reduced, if not eliminated, particularly for generation owners with multiple units that would

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<sup>21</sup> Maryland PSC Protest at 8.

<sup>22</sup> *Id.* at 6 (citing *ISO New England, Inc.*, 117 FERC ¶ 61,082, at PP 20-21 (2006) (*ISO-NE*); *Ca. Indep. Sys. Operator Corp.*, 101 FERC ¶ 61,061, at PP 15-17 (2002) (*CAISO*)).

benefit from higher market-clearing prices. Ethical Electric argues that the price cap incents utilities to hedge properly and that its elimination transfers the risk of natural gas price volatility from generators to market buyers. WGES argues that the door will be opened for potential gaming of offer prices by Generation Resources such that very high clearing prices will result and revenues for all of the energy delivered will be dramatically increased. WGES asserts that granting PJM's waiver request will result in sellers of natural gas supply to electric generators having no limits or restraints at all in their pricing, and generators will be willing to pay "whatever it takes" to buy high priced gas knowing they will be able to bid the equivalent electricity price into the PJM day-ahead energy market. PPANJ, Ethical Electric, and Consumer Representatives assert that the waiver will create tremendous market uncertainty and add a regulatory "risk premium" to contract prices.

24. Consumer Representatives contend that the Commission should reject PJM's request for waiver because it constitutes impermissible retroactive ratemaking. Consumer Representatives argue that the proposal violates the doctrine that "a utility cannot retroactively increase the rate charged a customer to a level higher than the rate on file"<sup>23</sup> because it requires going back to the time the capacity resources cleared and retroactively changing the rules of the auction to the disadvantage of customers. Consumer Representatives assert that PJM effectively asks the Commission to write an "economic force majeure" into the Tariff after Capacity Resources cleared in an auction, took on the obligations of being a cleared Capacity Resource, and began receiving payment for those obligations.

25. If the Commission grants the request for waiver, PPANJ requests that the waiver be implemented subject to refund so that the efficacy of the rules change can be adjudicated and harmed parties can be made whole if the Commission ultimately decides the rule should not have been changed so precipitously.

26. Maryland PSC also requests that the Commission amend the January 24, 2014 Order in Docket No. ER14-1144-000 to (1) provide that Commission staff shall review generator cost requests made to PJM on a sample basis and review PJM decisions to allow "make whole" payments, and (2) direct the PJM IMM to prepare and file a report with Commission staff identifying all applications made for pricing above the \$1,000/MWh cap and explaining the basis upon which the price allowed was determined.

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<sup>23</sup> Consumer Representatives Protest at 10 (citing *Cities of Anaheim, et al. v. California Indep. Sys. Operator Corp.*, 102 FERC ¶ 61,274, at PP 40-41 (2003)).

### C. PJM's Answer

27. In its answer to protests, PJM argues that the waiver granted in Docket No. ER14-1144-000 does not moot the present waiver request, because the two waiver requests address different problems. The make-whole waiver request provided assurance to sellers that if they operate as dispatched by PJM, they would not be forced to sell below cost, and thereby helped avoid undercutting PJM's dispatch authority. The present waiver request asks the Commission to address the remaining adverse consequences - below-cost pricing that breaks the marginal cost pricing principle and imposition of unhedgeable costs on load.<sup>24</sup>

28. PJM also states that market prices can be hedged through forward contracts and other mechanisms, whereas uplift charges cannot. Therefore, the uplift approach advocated by protesters would misallocate generation costs from customers that did not hedge to customers that did hedge, according to PJM.<sup>25</sup>

29. PJM states that the practical effect of protesters process arguments, such as NEPM's statement that PJM should have submitted a 60-day notice filing instead of requesting expeditious relief, would mean there would not be relief until the end of winter.

30. PJM asserts that the fact that the offer-price cap has been in place for many years is not a sufficient reason to impose it despite demonstrably uneconomic pricing results, and protesters have provided no economically rational argument for denying the requested waiver. PJM contends that when the price cap was implemented the \$1,000/MWh value was five to seven times higher than the marginal cost of production, and the cap was intended as a "fail-safe market power mitigation provision" preventing sellers from raising market prices above the marginal cost—not the actual cost—of production.<sup>26</sup> PJM also argues that the mere fact that the offer price cap is long-standing does not bear on whether it should be waived because "*every* waiver request by definition seeks a departure from a current effective tariff provision that the Commission has previously accepted as just and reasonable."<sup>27</sup>

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<sup>24</sup> PJM Answer at 4-5.

<sup>25</sup> *Id.* at 5.

<sup>26</sup> *Id.* at 7.

<sup>27</sup> *Id.*

31. In response to concerns that the cost of spot market natural gas is not appropriately included in energy offers or clearing prices because sellers could have hedged their gas price exposure, PJM argues that whether or not these offers are based on spot market prices is not the issue. In fact, PJM argues, proof of such hedging strategy is not currently a precondition to including fuel costs in *any* energy market offer.<sup>28</sup> Similarly, PJM argues that the fact that Generation Capacity Resources receive capacity payments does not provide a reason to exclude elevated fuel costs from energy offers and clearing prices because capacity payments are not designed to recover variable costs like the cost of fuel. Lastly, PJM argues that its waiver request does not constitute retroactive ratemaking because PJM seeks to waive the offer-price cap only prospectively, and because the Commission has found that “upset[ing] the expectations of market participants ... is distinguishable from retroactive ratemaking.”<sup>29</sup>

**D. NEPM’s Answer**

32. NEPM argues that PJM’s answer should be rejected and that it simply reargued its petition. NEPM contends that the Commission recently rejected requests that it order the New York Independent System Operator (NYISO) to waive or eliminate its \$1,000/MWh offer price cap.<sup>30</sup> NEPM also notes that the fact that the Midcontinent Independent System Operator (MISO) and NYISO will each have a \$1,000/MWh offer price cap in effect would artificially incent flows into PJM from MISO and NYISO during periods of extremely high gas prices, contrary to Commission precedent supporting consistency of offer price caps in interdependent markets.<sup>31</sup>

**E. RESA’s Answer**

33. In its answer, RESA argues that, contrary to protestors’ claims, the problem was not “fixed” by the granting of the prior waiver and likely will not be fixed until the flaws in the market that resulted in this problem are corrected, likely via the stakeholder process or a process before the Commission. RESA states that the status quo is untenable

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<sup>28</sup> *Id.* at 8.

<sup>29</sup> *Id.* at 8-9 (quoting *ISO New England, Inc.*, 145 FERC ¶ 61,095, at P 28 (2013) (internal quotations omitted)).

<sup>30</sup> *Id.* (citing *New York Independent System Operator, Inc.*, 146 FERC ¶ 61,061 (2014) (NYISO Order)).

<sup>31</sup> *Id.* (citing *Western Elec. Coordinating Council*, 133 FERC ¶ 61,026, at P 14 (2010)).

and its members will be directly harmed unless the waiver request is granted. RESA notes that the offer-price cap has always been artificial and just because it has not been adjusted or exceeded before does not mean that it never can be. RESA states that the waiver is necessary for market transparency, particularly because costs resulting from increased gas prices will be reflected in higher balancing operating reserve charges.

#### **F. Maryland PSC's Answer**

34. Responding to PJM's Answer, Maryland PSC states that reimbursing generators whose cost-based offers exceed the \$1,000/MWh offer price cap via uplift is superior to enabling those resources to set the market clearing price. Maryland PSC alleges that allowing generators whose costs are below the offer price cap to be paid a market clearing price above \$1,000/MWh would be unjust and unreasonable. Maryland PSC requests that the Commission open an evidentiary proceeding into the matter, arguing that there have been higher-than-normal forced outage rates this winter and that, therefore, the Commission cannot rule out that market manipulation is occurring. Finally, Maryland PSC states that it appears that Manual 15 allows a generator to recover costs based on the spot price of fuel, although its actual experienced fuel costs are based on a contract or hedge.<sup>32</sup> Maryland PSC "requests further clarification of the Commission's January 24 Order" by clarifying, "in any order issued in Docket No. ER14-1145-000 or by issuance of a Clarification Order in Docket No. ER14-1144-000, that uplift compensation is permitted only for the recovery of actual above-cap generation costs experienced as the result of natural gas price spikes prior to March 31, 2014."<sup>33</sup>

### **III. Discussion**

#### **A. Procedural Matters**

35. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,<sup>34</sup> the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

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<sup>32</sup> See, PJM Manual 15 – Cost Development Guidelines at Section 2.3.2.

<sup>33</sup> Maryland PSC Answer at 6.

<sup>34</sup> 18 C.F.R. § 385.214 (2013).

36. Pursuant to Rule 214(d) of the Commission's Rules of Practice and Procedure,<sup>35</sup> the Commission will grant CES's, Dominion Resources Services, Inc.'s, TAQA Gen X LLC's, Dynegy's, and the Illinois Commerce Commission's late-filed motions to intervene given their interest in the proceeding, the early stage of the proceeding, and the absence of undue prejudice or delay.

37. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2013), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept PJM's, NEPM's, RESA's, and the Maryland PSC's answers because they have provided information that assisted us in our decision-making process.

## **B. Substantive Matters**

38. The Commission finds good cause to grant the requested waiver of section 1.10.1A(d) of Schedule 1 of the Operating Agreement, and the equivalent section of Attachment K-Appendix to the Tariff, effective from the date of this order through March 31, 2014. The Commission has previously granted requests for waivers of tariffs in situations where, as relevant here: (1) the waiver is of limited scope; (2) a concrete problem must be remedied; and (3) the waiver does not have undesirable consequences, such as harming third parties.<sup>36</sup>

39. We find that PJM's requested waiver satisfies the aforementioned conditions. PJM's request is limited in scope in that it is limited to the period from the date of this order through March 31, 2014 and limits what types of resources can bid and how.<sup>37</sup> While protestors argue that the waiver amounts to a fundamental market rule change, the

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<sup>35</sup> 18 C.F.R. § 385.214(d) (2013).

<sup>36</sup> See, e.g., *New York Independent System Operator, Inc.*, 144 FERC ¶ 61,147, at P 8 (2013); *New York Independent System Operator, Inc.*, 139 FERC ¶ 61,108, at P 14 (2012); *PJM Interconnection, L.L.C.*, 137 FERC ¶ 61,184, at P 13 (2011); *ISO New England Inc.*, 134 FERC ¶ 61,182, at P 8 (2011); *California Independent System Operator Corp.*, 132 FERC ¶ 61,004, at P 10 (2010); *accord ISO New England Inc. – EnerNOC, Inc.*, 122 FERC ¶ 61,297 (2008); *Central Vermont Public Service Corp.*, 121 FERC ¶ 61,225 (2007); *Waterbury Generation LLC*, 120 FERC ¶ 61,007 (2007); *Auschnet Co.*, 122 FERC ¶ 61,045 (2008).

<sup>37</sup> PJM Transmittal at 7, n.10. Also, we agree with the PJM IMM that this means that price-based offers would be permitted to exceed \$1,000/MWh only if they equaled the cost-based offer.

waiver applies to a limited period of time and only applies to cost-based offers by Generation Capacity Resources whose marginal costs exceed \$1,000/MWh. While the Consumer Representatives argue that PJM has failed to show that the waiver request is necessary for all regions of PJM, making such a showing is not a prerequisite to granting a request for waiver.

40. PJM's request addresses a concrete problem by allowing Generation Capacity Resources to submit cost-based offers that fully reflect the marginal costs of those sellers. PJM explains that, during the recent period of winter weather, natural gas prices averaged over \$120/MMbtu, causing a large amount of generation being offered into, and clearing, PJM's energy market at prices likely below the generators' costs of producing that energy.<sup>38</sup> While the January 24, 2014 Order, by allowing marginal costs to be recovered as uplift, provided an immediate solution to the problem of Generation Capacity Resources not recovering their marginal costs due to recent spikes in fuel costs, that waiver request left open the issue that recovering such costs as uplift fails to reflect such costs (and risks) in transparent market prices. By limiting legitimate, cost-based bids to no more than \$1,000/MWh, the market produces artificially suppressed market prices and inefficient resource selection. By paying an uplift, PJM is in effect paying one price for energy dispatched through the market (e.g. \$1,000), and a second higher price (e.g. \$1,200) for the resource dispatched out-of-merit (while treating the latter in the dispatch stack as if it had a bid of \$1,000). This would not be consistent with longstanding Commission precedent. The Commission has previously found that "[p]ayments made only to individual resources and recovered in uplift fail to send clear market signals" and that those resource costs "should be reflected in transparent market prices whenever possible."<sup>39</sup> Accordingly, we find that the request for waiver addresses a concrete problem. Whether generators have entered into fuel delivery contracts or made other arrangements to hedge against the possibility of spikes in fuel prices does not change the

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<sup>38</sup> PJM Transmittal at 4-5.

<sup>39</sup> *PJM*, 139 FERC ¶ 61,057 at P 78, n.72. See, e.g., *PJM Interconnection, L.L.C.*, 117 FERC ¶ 61,331, at 62,876, n.101 (2006); see also *Town of Norwood v. FERC*, 962 F.2d 20, 23 (D.C. Cir. 1992) (upholding Commission marginal cost pricing order and describing academic support for marginal cost pricing). For example, if Generator A has short-run marginal costs of \$1,100/MWh, and Generator B has short-run marginal costs of \$1,200/MWh, but both can only submit bids of \$999/MWh, PJM might end up dispatching the less efficient Generator B and might not dispatch the more efficient Generator A. And, dispatched, both generators would operate at a loss. PJM states that it recently cleared 4,000 MW of offers at \$999/MWh – signaling that these resources had costs above \$1,000/MWh – and, thus, it has identified a concrete problem to resolve.

fact that the generators' marginal costs are not being reflected in transparent market prices.

41. Finally, although granting waiver may result in temporary increases of costs to load, we find that it is appropriate to allow generators to reflect their actual energy production costs, even if above \$1,000/MWh, in market prices. While protestors argue that third parties will be harmed because some have undertaken commitments to hedge against price exposure, we do not find that this renders it unreasonable for the marginal costs incurred by the generators to be reflected in prices. PJM's proposed waiver will ensure that marginal prices paid by consumers appropriately equal the incremental cost of servicing them, and efficient market signals—not constrained by a cap—should provide market participants with the information necessary to make informed business decisions, including hedging fuel risk. Lastly, as RESA and others indicate, retail suppliers are better able to hedge costs included in the energy market than those limited to uplift.

42. With respect to arguments by protestors that market participants rely on longstanding and essential market rules like the \$1,000/MWh offer price cap and the price cap is established at a level that will protect end users from the exercise of market power, granting PJM's proposed waiver does not permit the exercise of market power. The waiver allows a bid above \$1,000/MWh only when the supplier can document that it reflects its marginal cost. Market clearing prices derived from PJM's security constrained bid-based economic dispatch, where all bids have been appropriately mitigated for market power, yield competitive prices that all sellers should receive. Generators with marginal costs greater than \$1,000/MWh and that clear the market are, in fact, economic—not uneconomic, as some parties allege. The market clearing price under these conditions—even if it is higher than before—is a just and reasonable price that does not reflect the exercise of market power. Marginal cost bidding is competitive bidding. We did not anticipate that, when the \$1,000/MWh bid cap was adopted, it would prevent marginal cost bidding. Presently, however, the \$1,000/MWh bid cap is preventing competitive marginal cost bids and resulting competitive prices that are needed to balance supply and demand.

43. Granting waiver also does not permit gaming, contrary to the argument by WGES, because it is based on documented costs subject to review by the PJM IMM and determined in accordance with the Cost Development Guidelines in Manual 15.<sup>40</sup> With respect to the Maryland PSC's concerns regarding potential market manipulation due to allegedly higher-than-average forced outage rates within PJM, the Commission will continue to closely monitor conditions that have precipitated the need for PJM's waiver.

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<sup>40</sup> If market manipulation does occur, it would be subject to the Commission's enforcement authority.

44. Cases cited by Maryland PSC for the proposition that the Commission previously did not allow marginal costs to be reflected in market clearing prices are inapposite. In *ISO-NE*, the Commission accepted a section 205 filing proposing to remove a price cap during emergency weather conditions and allowing generating resources to make after-the-fact claims for extraordinary fuel expenses.<sup>41</sup> The Commission made no finding that only after-the-fact uplift is appropriate or that reflecting such costs in clearing prices would be unjust and unreasonable. Similarly, in *CAISO*, the Commission found that an uplift recovery arrangement was appropriate, but did not indicate that allowing costs to be reflected in clearing prices would, as a general matter, be unjust and unreasonable.<sup>42</sup>

45. We disagree with NEPM and AMP that the requested waiver should not be granted in order to reserve the issue for the PJM stakeholder process. PJM states that it will address revisions to the Operating Agreement with stakeholders,<sup>43</sup> but in the meantime we find that the current situation requires immediate relief.

46. We disagree with Consumer Representatives that granting PJM's request for waiver would constitute impermissible retroactive ratemaking. The waiver is effective prospectively, as of the date of this order, and therefore does not retroactively change the rules as Consumer Representatives claim, because the waiver, in effect, only affects the clearing prices in the energy market, while retaining the obligation of the capacity generation resources to bid into the day-ahead energy market. Further, the instant filing put market participants on notice regarding a possible rule change.

47. We do not find it appropriate to grant PPANJ's request that the waiver be implemented subject to refund, as the market will have already been run based on the generators' costs. We also find Maryland PSC's request that the Commission amend its findings in Docket No. ER14-1144-000 and DC Energy's request to align the methodology proposed in Docket No. ER14-1138-000 with the proposal in this docket to be outside the scope of this proceeding.<sup>44</sup> With respect to Maryland PSC's request for clarification of the January 24, 2014 Order's findings regarding compensation of energy market offer bids through an uplift charge, uplift compensation is at issue in Docket No. ER14-1144-000 but is not at issue in this filing.

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<sup>41</sup> *ISO-NE*, 117 FERC ¶ 61,082 at PP 20-21.

<sup>42</sup> *CAISO*, 101 FERC ¶ 61,061 at PP 15-17.

<sup>43</sup> PJM Transmittal at 1.

<sup>44</sup> The Commission issued an order in Docket No. ER14-1138-000 on January 31, 2014. NYISO Order, 146 FERC ¶ 61,061.

48. To the extent that NEPM argues that the Commission rejected requests that it order NYISO to waive or eliminate its \$1,000/MWh price cap, the NYISO order is distinguished from the instant case because NYISO did not request that the marginal costs be reflected in clearing prices. In addition, precedent cited by NEPM<sup>45</sup> does not make a finding that neighboring Regional Transmission Organizations must have offer price caps.

49. Finally, we note that under the PJM Tariff, the PJM IMM reviews all cost-based offers to verify the documented costs submitted. Given the unique nature of PJM's request, we direct the PJM IMM to submit an informational filing within 30 days of the expiration of the requested waiver that identifies: (1) the number of hours when clearing prices exceed \$1,000 as a result of this waiver; (2) the associated prices by zone; and (3) total energy costs.

The Commission orders:

PJM's request for waiver of section 1.10.1A(d) of Schedule 1 of the Operating Agreement, and the equivalent section of Attachment K-Appendix to the Tariff from the date of the issuance of this order to March 31, 2014, is hereby granted, as discussed in the body of this order.

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.

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<sup>45</sup> *Western Elec. Coordinating Council*, 133 FERC ¶ 61,026 at P 14.