144 FERC ¶ 61,162
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.

Lincoln Paper and Tissue, LLC Docket No. IN12-10-000

ORDER ASSESSING CIVIL PENALTY

(Issued August 29, 2013)

1. In this order, the Commission finds that Lincoln Paper and Tissue, LLC (Lincoln) has violated section 1c.2 of the Commission's regulations and section 222 of the Federal Power Act (FPA), which prohibit energy market manipulation.[1] In light of the seriousness of these violations and the lack of any effort by Lincoln to remedy its violations, we find that a civil penalty and disgorgement, plus interest, pursuant to section 316A of the FPA,[2] is appropriate.

I. Background

2. Lincoln is a paper mill in Lincoln, Maine. In 2007, Lincoln participated as an end-user demand response provider in ISO New England, Inc.'s (ISO-NE) Day-Ahead Load Response Program (DALRP).[3] Through the DALRP, ISO-NE compensated customers

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[1] 18 C.F.R. § 1c.2 (2013); 16 U.S.C. § 824v(a) (2006).

[2] 16 U.S.C. § 825o-1 (2006).

[3] An independent system operator (ISO) "is an independent company that assume[s] operational control—but not ownership—of the transmission facilities owned by its member utilities . . . . [and] provide[s] open access to the regional transmission system to all electricity generators at rates established in a single, unbundled, grid-wide tariff that applies to all eligible users in a non-discriminatory manner." *New England Power Generators Ass'n, Inc. v. FERC*, 707 F.3d 364, 367 n.1 (D.C. Cir. 2013) (quoting *Midwest ISO Transmission Owners v. FERC*, 373 F.3d 1361, 1364 (D.C. Cir. 2004)) (internal quotation marks omitted).

for certain load reductions, also called demand response, as measured against a baseline load (customer baseline)[4] established for each facility providing the demand reduction.

3. On April 17, 2012, the Commission's Office of Enforcement Staff (OE Staff) submitted to the Commission an Enforcement Staff Report and Recommendations (OE Staff Report) alleging that Lincoln had violated the Commission's Prohibition on Market Manipulation, 18 C.F.R. § 1c.2 (2013). The OE Staff Report alleged that Lincoln engaged in an intentional fraudulent scheme in connection with the DALRP, to artificially inflate its customer baseline to enable it to receive compensation for demand response without intending to provide the service or actually having to reduce load. The OE Staff Report described the fraudulent scheme as follows: Lincoln devised and implemented a plan to inflate its customer baseline by curtailing its use of on-site generation during its initial DALRP customer baseline period, and instead replacing that on-site energy with energy taken from the grid. This curtailment created an inflated customer baseline that did not reflect Lincoln's routine electricity consumption from the grid. After establishing its initial inflated customer baseline, Lincoln resumed its routine practice of operating its on-site generation to lower electric consumption from the grid. Lincoln then offered demand response into the DALRP on a daily basis, at a minimum offer price which would almost always be accepted by ISO-NE, thereby, under the terms of the DALRP, leaving in place its inflated customer baseline. Lincoln then received compensation for providing demand response because, when measured against its inflated baseline, Lincoln's routine use of its on-site generation appeared to have reduced its load. Lincoln's offers fraudulently communicated a willingness and ability to reduce load, even though it did not intend to reduce load and, in fact, did not reduce load. The OE Staff Report recommended that Lincoln be assessed a civil penalty of $4,400,000 and ordered to disgorge $379,016.03 in unlawful payments for engaging in the fraudulent scheme.

4. On July 17, 2012, the Commission issued an Order to Show Cause and Notice of Proposed Penalty.[5] The Commission directed Lincoln to file an answer within 30 days showing cause why it should not be found to have violated 18 C.F.R. § 1c.2 and 16 U.S.C. § 824v(a) in connection with Lincoln's participation in ISO-NE's DALRP. In addition, the Commission directed Lincoln to show cause why its alleged violation

[4] Per the ISO-NE DALRP manual in effect at the time, a customer baseline is calculated using "the average hourly load, rounded to the nearest kWh, for each of the 24 hours in a day." ISO New England Load Response Program Manual, Rev. 9 § 4.2.1 (effective Apr. 7, 2006) (Load Response Program Manual).

[5] *Lincoln Paper and Tissue, LLC*, 140 FERC ¶ 61,031, at P3 (2012) (Show Cause Order).

should not warrant the assessment of a civil penalty in the amount of $4,400,000, or a modification of that amount consistent with section 31(d)(4) of the FPA, and disgorgement of $379,016.03 in payments received as a result of its participation in ISO-NE's DALRP. The Commission also stated that Lincoln must, within 30 days, elect either an administrative hearing before an Administrative Law Judge at the Commission prior to the assessment of a penalty pursuant to section 31(d)(2) of the FPA or, if the Commission finds a violation, an immediate penalty assessment by the Commission under section 31(d)(3)(A) of the FPA.[6] The Show Cause Order further allowed OE Staff to file a reply within 30 days of the filing of Lincoln's answer.[7]

5. On August 14, 2012 Lincoln gave notice electing the procedures set forth in section 31(d)(3)(A) of the FPA and the Show Cause Order,[8] thereby electing an immediate penalty assessment if the Commission finds a violation. Lincoln filed its answer to the Show Cause Order on September 14, 2012 (Show Cause Answer). OE Staff filed a reply to the Lincoln's answer on November 13, 2012 (OE Staff Reply). Lincoln filed a Motion for Leave to Answer and Answer to OE Staff's Reply on November 28, 2012 (Lincoln November Reply). OE Staff submitted an opposition to Lincoln's November Reply on November 30, 2012 (OE Staff Opposition). Lincoln filed supplemental information on January 10, 2013 (Lincoln Supplemental Information). OE Staff submitted an answer to Lincoln's Supplemental Information on January 25, 2013 (OE Staff January Answer).

II. Discussion

A. Procedural Matters

6. 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 an answer unless otherwise ordered by the decisional authority. We will accept Lincoln's November Reply, OE Staff's Opposition, Lincoln's Supplemental Information, and OE Staff's January Answer because they provided information that assisted us in our decision-making process.

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[6] *See* 16 U.S.C. § 823b(d) (2006).

[7] On August 2, 2012, the Commission extended Lincoln's deadline to respond to the Show Cause Order to September 14, 2012. On September 26, 2012, the Commission extended OE's deadline to reply to Lincoln's Show Cause Answer to November 13, 2012.

[8] *See* Ordering Paragraph D to Show Cause Order.

B. Substantive Matters

7. Section 222(a) of the FPA makes it unlawful for any entity to use a deceptive or manipulative device in connection with the purchase or sale of electric energy or the transmission of electric energy subject to the Commission's jurisdiction.[9] Order No. 670 implemented this prohibition, adopting the Anti-Manipulation Rule. That rule, among other things, prohibits any entity from: (1) using a fraudulent device, scheme or artifice, or making a material misrepresentation or a material omission as to which there is a duty to speak under a Commission-filed tariff, Commission order, rule or regulation, or engaging in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity; (2) with the requisite scienter; (3) in connection with the purchase, sale or transmission of electric energy subject to the jurisdiction of the Commission.[10]

8. Pursuant to section 316A(b) of the FPA, the Commission may assess a civil penalty of up to $1 million per day, per violation against any person who violates Part II of the FPA (including section 222 of the FPA) or any rule or order thereunder.[11] In determining the amount of a proposed penalty, section 316A(b) requires the Commission to consider "the seriousness of the violation and the efforts of such person to remedy the violation in a timely manner."[12] Although the Penalty Guidelines are not mandatory, the Commission uses them and its policy statements on enforcement to guide its penalty analysis.[13]

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[9] 16 U.S.C. § 824v(a) (2006).

[10] 18 C.F.R. § 1c.2(a) (2013); *see Prohibition of Energy Market Manipulation*, Order No. 670, FERC Stats. & Regs. ¶ 31,202, at P 49 , *reh'g denied*, 114 FERC ¶ 61,300 (2006).

[11] 16 U.S.C. § 825o-1(b)(2006).

[12] *Id.*

[13] *See Enforcement of Statutes, Orders, Rules, and Regulations*, 132 FERC ¶ 61,216 (2010) (Penalty Guidelines Order); *Enforcement of Statutes, Orders, Rules, and Regulations*, 130 FERC ¶ 61,220, at PP 6, 26 (2010) (Initial Penalty Guidelines Order) (seriousness of violation and timely efforts to remedy a violation will continue to be significant factors under the Penalty Guidelines). The Commission also noted when issuing its Initial Penalty Guidelines Order that it will continue to rely on issues identified in its policy statements on enforcement, *Enforcement of Statutes, Regulations, and Orders*, 123 FERC ¶ 61,156, at PP 50-71 (2008), and *Enforcement of Statutes, Orders,*

(continued…)

9. As discussed below, we find that Lincoln violated section 1c.2 of the Commission's regulations and section 222(a) of the FPA by inflating its customer baseline in ISO-NE's DALRP and by subsequently accepting demand response payments without altering its operations to provide the required demand reduction. Further, we find that a civil penalty of $5,000,000 and disgorgement of $379,016.03, plus interest, is appropriate given the seriousness of Lincoln's violation and the harm caused by its conduct. As discussed below, in order to alleviate any concern about Lincoln's ability to pay the penalty, we will permit Lincoln, if it desires, to pay the penalty pursuant to an agreed upon payment plan with OE Staff, subject to Commission approval.

C. Commission Determination

1. Findings of Fact

a. ISO-NE's DALRP Framework

10. The Commission's regulations define demand response as "a reduction in the consumption of electric energy by customers from their expected consumption in response to an increase in the price of electric energy or to incentive payments designed to induce lower consumption of electric energy."[14] A demand response resource is a resource capable of providing demand response.[15]

11. From June 1, 2005[16] through the relevant period of OE Staff's investigation, the DALRP allowed compensation for demand response resources that "provide a reduction in their electricity consumption in the New England Control Area during peak demand

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Rules, and Regulations, 113 FERC ¶ 61,068, at PP 17-27 (2005), as well as its policy statement on compliance, *Compliance with Statutes, Regulations, and Orders*, 125 FERC ¶ 61,058 (2008), to measure the seriousness of violations and timely efforts to remedy violations. The Commission stressed that any conflict will be resolved in favor of the Penalty Guidelines. Initial Penalty Guidelines Order, 130 FERC ¶ 61,220 at P 63. The Penalty Guidelines are appended to the Penalty Guidelines Order.

[14] 18 C.F.R. § 35.28(b)(4) (2013).

[15] *Id.* § 35.28(b)(5).

[16] *See ISO New England, Inc.*, 123 FERC ¶ 61,021, at P 4 (April 4, 2008 Order), *order on reh'g*, 124 FERC ¶ 61,235 (2008) (September 11, 2008 Order).

periods."[17] ISO-NE calculated that reduction in electricity consumption taken from the grid by first establishing a customer baseline for each demand response resource, and then subtracting the demand response resource's actual metered load during the hours in which ISO-NE accepted the demand response resource's price-based bid.[18] DALRP market participants could offer their demand response resources at a minimum price of $50/MWh and a maximum price of $1,000/MWh. Each offer had to be at least 100 kW. Each accepted offer then would be paid the applicable day-ahead zonal price multiplied by the cleared day-ahead offer.[19]

12. ISO-NE's Load Response Program Manual required each DALRP participant to "be willing and capable of interrupting load within the parameters of the offer" and to "be able to interrupt Monday-Friday, on non-Demand Response Holidays between 7:00 AM - 6:00 PM."[20] Per the Load Response Program Manual, each resource had its own customer baseline, which was determined as "the average hourly load, rounded to the nearest kWh, for each of the 24 hours in a day."[21] For a new demand response resource, the Load Response Program Manual specified that its customer baseline was "calculated for each hour in [a] day based on meter data from the initial five business days after the asset [wa]s approved and hourly meter data beg[an] to be recorded."[22] Once an initial customer baseline was established, the customer baseline would be recalculated each day based on a weighted average of the previous day's customer baseline and the meter data for the present program day. However, for any day that a demand response offer was accepted, that day's customer baseline would be excluded from the rolling weighted average calculation of a demand response resource's customer baseline. Thus, a DALRP

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[17] ISO New England, Inc., FERC Electric Tariff No. 3, Section III – Market Rule 1 – Standard Market Design, Appendix E-Load Response Program, 2nd Rev Sheet No. 7902, § III.E.1.1. This order refers to ISO-NE's tariff in operation during the time period covered by OE Staff's investigation.

[18] April 4, 2008 Order, 123 FERC ¶ 61,021 at PP 4-5; *see also* Load Response Program Manual § 4.3.1.3.

[19] ISO New England, Inc., FERC Electric Tariff No. 3, Section III – Market Rule 1 – Standard Market Design, Appendix E-Load Response Program, 1st Rev Sheet No. 7906-7907, §§ III.E.2.2-III.E.2.3; Load Response Program Manual § 4.5.1.1.

[20] Load Response Program Manual § 2.2.1.

[21] *Id.* § 4.2.1.

[22] *Id.*

participant indefinitely could maintain its initial customer baseline by making daily offers that were accepted.[23]

13. Any ISO-NE market participant or demand response provider could enroll itself or an end-user in the DALRP.[24] ISO-NE would then pay or collect fees from the enrolling participant (the entity responsible for enrolling the demand asset) but was not responsible for disbursing any revenues to, or collecting fees from, a demand response provider. The enrolling participant would then be responsible for distributing or collecting such funds to the demand response provider.[25]

b. Lincoln Paper Mill

14. Lincoln is a paper mill in Lincoln, Maine with approximately 400 employees.[26] In 2007, and when fully operational, the mill's electricity consumption was approximately 20 MW, and did not fluctuate appreciably between day and night hours.[27] Lincoln obtained electricity from behind-the-meter, on-site generation and grid power purchases from Constellation NewEnergy, Inc. (Constellation).[28]

15. Lincoln's on-site generation consisted of two steam-powered turbine generators used to create steam for manufacturing and to generate electricity. The first was the

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[23] *Id.*

[24] *Id.* § 2.2.

[25] *Id.* § 4.5.4.

[26] Van Scotter Dep. 27:1-4, Dec. 15, 2008. Citations herein are to documents obtained and sworn testimony developed during OE Staff's nonpublic investigation. Citations to most documents refer to the entity supplying each document and the electronic or physical bates stamp (*e.g.*, LINC000001) and transcript references refer to the last name of the deponent, page, and line of the relevant transcript (*e.g.*, Van Scotter Dep. 27:1-4).

[27] LINC000688 and LINC000730; *accord* Brennan Dep. 35:7-9, Dec. 16, 2008; Van Scotter Dep. 30:5-20.

[28] Van Scotter Dep. 37:21-24; 38:2-10; Brennan Dep. 113:22-24.

Westinghouse generator, which had a nameplate capacity of 4 MW.[29] In December 2006 and January 2007, the Westinghouse generator was dismantled for repairs, costing over $300,000, to keep it operational until it could be replaced.[30] The second generator, theTG3 generator, which was meant to replace both the Westinghouse generator and another generator which had previously failed, had a nameplate capacity of 13.5 MW.[31] The TG3 generator began operational testing in November 2007, but performed poorly.[32] It began commercial operation on January 15, 2008, but was never commercially accepted.[33] It had an output of 7.5 to 9.1 MW.[34]

c. <u>Lincoln's Participation in the DALRP</u>

16. In July 2007, Lincoln enrolled in the DALRP with Constellation as its enrolling participant, which would retain 15 percent of all DALRP revenues.[35] Lincoln did not discuss setting its customer baseline with Constellation.[36] Lincoln's initial five-day customer baseline ran on July 25, 26, 27, 30, and 31, 2007. Per the Load Response Program Manual Lincoln did not include July 28 and 29, 2007 in this initial customer baseline because these two days were non-business days.[37] Shortly before 7:00 AM each day of the initial customer baseline, Lincoln's metered consumption of grid energy increased from approximately 16 MW to approximately 19 MW, where it would stay

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[29] Show Cause Answer at 7; Van Scotter Dep. 37:14-16. The Westinghouse generator provided both electricity for the mill to operate, and steam management for the plant's manufacturing process. Show Cause Answer at 7.

[30] Show Cause Answer at 8; Wissman Aff. at 7.

[31]Show Cause Answer at 11; Brennan Dep. 37:21-25.

[32] Show Cause Answer at 11; Van Scotter Dep. 45:17-18; Wissman Aff. at 9-10.

[33] Show Cause Answer at 29; Van Scotter Dep. 45:17-24.

[34] Show Cause Answer at 12; Wissman Aff. at 10.

[35] Show Cause Answer at 9.

[36] Show Cause Answer at 30; Response No. 20 of Constellation NewEnergy, Inc. to April 7, 2008 Data Request (May 9, 2008).

[37] Show Cause Answer at 9; Load Response Program Manual § 4.2.1.

until 6:00 PM, when it returned to approximately 16 MW.[38] The increase in Lincoln's purchases of grid energy during these hours was mainly attributable to Lincoln curtailing the Westinghouse generator by 3 MW, increasing energy purchases from ISO-NE.[39] During these hours, Lincoln replaced mill load usually met with Westinghouse generator output with energy purchased from the grid.[40] Lincoln's purchases of replacement grid energy during the five-day initial customer baseline period cost Lincoln approximately $10,000.[41]

17. ISO-NE used the metered load data reflected on the following chart to establish Lincoln's initial customer baseline:[42]

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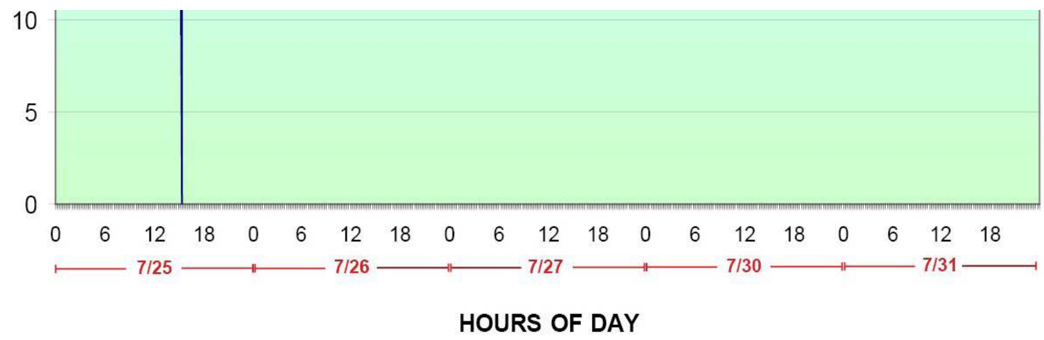
[38] OE Staff Report at 8; *See also* Show Cause Answer at n.28 (stating that during the baseline period Lincoln had an average increase in its purchase of energy from the grid of approximately 3 MW); May 5, 2011 Lincoln Letter to OE at 8 (stating that Lincoln ramped down its Westinghouse turbine by approximately 3 MW when setting its baseline).

[39] Van Scotter Dep. 109:25; 110:1-14.

[40] See Van Scotter Dep. 117:3-7.

[41] Van Scotter Dep. 117:8-15; May 5, 2011 Lincoln Letter to OE Staff at 8.

[42] OE Staff Report at 9 (citing December 7, 2011 ISO-NE Data Response).



18. On almost every non-holiday weekday between July 31, 2007[43] and early February 2008, Lincoln submitted DALRP load reduction offers for each DALRP program hour.[44] These offers were almost always submitted at the minimum DALRP offer price of $50/MWh.[45] Lincoln's offers of $50/MWh almost always cleared during this period because they were lower than locational marginal prices during DALRP hours in this period.[46] Lincoln earned DALRP revenues for each day it participated in the DALRP during this period. There were only seven days during this period on which Lincoln's bids were not accepted, five of which were caused by Lincoln missing the bid deadline.[47] In July 2007 and August 2007 Lincoln verified with Constellation that cleared daily offers into the DALRP would freeze its customer baseline.[48] Lincoln's customer baseline changed nine times during this period, decreasing from 19.39 MW on July 31, 2007 to 17.73 MW in February 2008, a difference of 1.66 MW.[49]

19. During the months of Lincoln's participation in the DALRP, Lincoln did not veer from its routine in order to provide demand response; Lincoln neither increased its on-site

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[43] Lincoln submitted its first offers for load reduction on July 31, 2007 for the next day. August 1, 2007 was Lincoln's first day of participation in the DALRP. LINC000511-516.

[44] *Id*.

[45] *Id*.

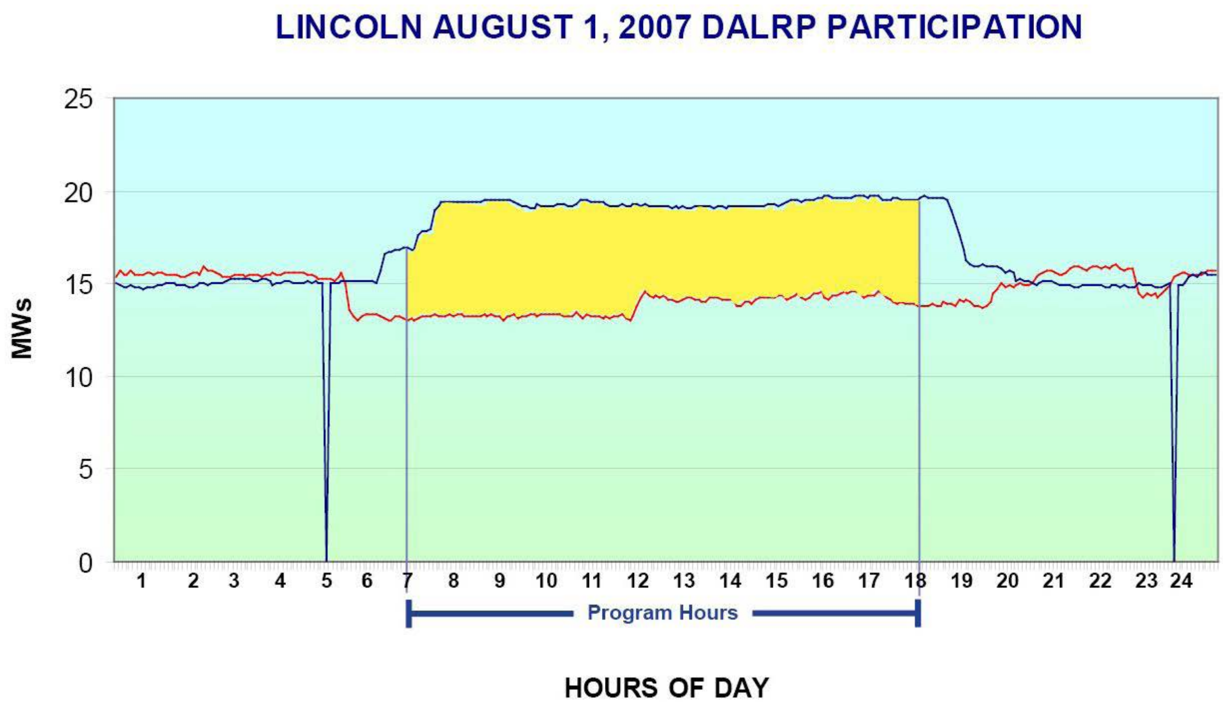
[46] *See* Van Scotter Dep. 127:9-13; May 5, 2011 Lincoln Letter to OE Staff at 7.

[47] LINC000511-516.

[48] LINC000008-009; LINC000228.

[49] LINC000511-516.

generation to reduce its demand from the grid nor reduced its electricity consumption. The following chart compares Lincoln's actual grid consumption (the line on the bottom) to Lincoln's established customer baseline (the line on the top) that was used by ISO-NE to calculate Lincoln's load reduction for the purposes of DALRP compensation (shaded area between two lines during program hours) on August 1, 2007, Lincoln's first day of DALRP participation):[50]



20. ISO-NE paid $5,015.36 for Lincoln's demand response reduction on August 1, 2007.[51] Lincoln reflected comparable differences between its customer baseline and grid consumption on almost every other day of its DALRP participation.[52] In total, ISO-NE paid $445,901.21 to Lincoln and Constellation for Lincoln's participation in the DALRP

[50] OE Staff Report at 11 (citing December 7, 2011 ISO-NE Data Response).

[51] December 7, 2011 ISO-NE Data Response.

[52] LINC000511-516.

between July 2007 and February 2008.[53] Lincoln was paid approximately 85 percent of this amount, $379,016.03.[54]

21. On November 29, 2007, Constellation advised Lincoln via email that "[d]istributed [g]eneration assets are not eligible to participate in the [DALRP] per the rules of ISO New England."[55] On January 23, 2008, Lincoln received a formal letter from Constellation, providing notice of Constellation's support for a new proposal by ISO-NE to modify the DALRP bidding rules, by "increas[ing] the minimum bid required under the Day-Ahead Program, which will result in customers' bids clearing less frequently and their baselines being adjusted more regularly."[56] Constellation stated that it was "concerned that some of [its] Day-Ahead Program customers may have increased their usage while ISO-NE was determining their baselines" and that bids based on these "inflated" baselines "may reflect a customer's normal usage rather than dispatchable load that the ISO-NE can depend upon for reliability purposes."[57]

22. On February 5, 2008, ISO-NE proposed tariff revisions changing the minimum price that demand response resources can offer into the market.[58] As a result, the minimum bid jumped from $50/MWh on February 8, 2008, to $121/MWh on February 11, 2008.[59] The last day that Lincoln's bid was accepted was February 7, 2008.[60] On April 4, 2008, the Commission accepted ISO-NE's DALRP changes, effective February 7, 2008, and announced that the Commission's Office of Enforcement

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[53] *See* CNE0023813.

[54] Constellation received $66,885.18, around 15%, of this amount. *See id*.

[55] LINC000025.

[56] LINC000236-237.

[57] *Id*.

[58] *See ISO New England Inc.*, Filing of Changes to Day-Ahead Load Response Program, Docket No. ER08-538-000 (Feb. 5, 2008)

[59] LINC000511-516.

[60] *Id*.

had begun a non-public investigation in February 2008 into whether any participants in the DALRP had violated the Commission's rules.[61]

2. Determination of Violation

a. Fraudulent Device, Scheme or Artifice

i. Show Cause Answer

23. Lincoln acknowledges setting its customer baseline by curtailing its Westinghouse generator by approximately 3 MW but argues its conduct was not fraudulent. On the issue of fraud, Lincoln argues that no guidance was available on how to set its customer baseline, the process was too complex, [62] and that it had no notice that it had set its customer baseline incorrectly. Lincoln argues that it received no advice from ISO-NE, Constellation, or FERC on how to set its customer baseline using its behind-the-meter generation.[63] Lincoln states that the concept of a baseline as it is now generally understood was not clear in 2007 and that Lincoln is now being punished for incorrectly guessing how its baseline should be set.[64] Lincoln argues that the Commission recognized the complexities in its 2008 orders accepting price modification to the DALRP and in statements therein by then-Commissioners Wellinghoff and Kelly.[65] In response to OE Staff's contention that the baseline period should have been reflective of Lincoln's normal operations, Lincoln argues that not until the 2008 orders did the Commission explicitly state that the baseline was "intended to estimate an asset's *normal* daily consumption pattern in the absence of demand response behavior."[66] Lincoln also

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[61] April 4, 2008 Order, 123 FERC ¶ 61,021 at P 50 n.49; *see also* September 11, 2008 Order, 124 FERC ¶ 61,235 at P 9.

[62] *Id*. at 16-18.

[63] Show Cause Answer at 15-16.

[64] *Id*. at 20.

[65] *Id*. at 16-17 (citing April 4, 2008 Order, 123 FERC ¶ 61,021 at P 29 (2008); April 4, 2008 Order, 123 FERC ¶ 61,021 (2008) (Kelly, Comm'r, concurring; Wellinghoff, Comm'r, concurring in part and dissenting in part); September 11, 2008 Order, 124 FERC ¶ 61,235 (2008) (Kelly, Comm'r, concurring; Wellinghoff, Comm'r, concurring in part and dissenting in part).

[66] *Id.* at 17 (citing September 11, 2008 Order, 124 FERC ¶ 61,235 at P 3) (emphasis added).

argues that no rule, order or tariff defined "normal" or the specific components of "normal" operations in setting a customer baseline.[67] Accordingly, Lincoln claims there was legitimate confusion regarding the program's requirements and that in these circumstances it is inappropriate to find fraud based solely on its changes to its operations during the customer baseline-setting period.

24. Lincoln further argues that ISO-NE's tariff did not expressly prohibit Lincoln's customer baseline-setting and DALRP bidding behaviors.[68] Lincoln states that the ISO-NE tariff did not exclude behind-the-meter generation from DALRP participation and was silent on how it should participate, and that thus Lincoln could not know its actions were wrong.[69] Lincoln argues it is inappropriate for OE Staff to now classify as fraudulent Lincoln's baseline-setting decisions without having provided prior fair notice of that interpretation.[70]

25. Lincoln also argues that neither Constellation nor ISO-NE, both of which had access to Lincoln's metering data and mill configuration information, informed Lincoln it had set its customer baseline incorrectly or asked it to reset its customer baseline.[71] Lincoln rejects OE Staff's contention that certain Constellation e-mails regarding customer baseline establishment and use of behind-the-meter generation constituted warnings of improper behavior that Lincoln ignored. Lincoln argues that, contrary to OE Staff's contention, the above-summarized November 29, 2007 e-mail from Constellation discussing distributed generation assets in the context of the DALRP was vague and did not provide a clear instruction that Lincoln should include the Westinghouse or TG3 in its customer baseline. Lincoln asserts that a January 23, 2008 formal letter from Constellation that expressed concerns that some customers "may have increased their usage while ISO-NE was determining their baselines," was generic and it was not clear whether the letter was directed at Lincoln's behavior. Lincoln states that it received no follow-up letter, and was never advised that it had improperly set its customer baseline.

26. Lincoln also asserts that it was entitled to receive payments because its Westinghouse generator was what Lincoln describes as a "pre-existing" demand response

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[67] *Id*. at 20.

[68] *Id*. at 20-21.

[69] *Id*.

[70] Lincoln Supplemental Information.

[71] Show Cause Answer at 18, 30-33.

resource. Lincoln explains that its generator generally helped reduce Lincoln's consumption of energy from the grid, and claims that the DALRP was designed to create "an additional financial benefit" in the form of "a payment for the amount of reduced load" to entities that were already providing demand response.[72] Lincoln contends that by curtailing its Westinghouse generator, Lincoln "communicated to ISO-NE what its typical, gross load would have been absent the pre-existing demand response," and did not misrepresent its load profile or ability to reduce energy consumption.[73] Lincoln asserts that Order No. 745[74] validates it view of the legitimacy of "pre-existing" demand response because Lincoln maintains that order provides for all demand response to be measured according to a baseline of zero and to be paid a full energy price. Lincoln reasons that it violated no ISO-NE tariff provision and merely did what it claims Order No. 745 now allows, and thus no fraud or penalty should apply.[75]

ii. OE Staff Report and Reply

27. OE Staff argues that Lincoln does not dispute the material facts of its conduct, only whether Lincoln's conduct constitutes fraud.[76] OE Staff asserts that the undisputed facts establish that Lincoln knowingly curtailed generation during the initial customer baseline period in order to obtain DALRP payments without altering its manufacturing behavior or energy usage. OE Staff states that Lincoln's actions in seeking demand response payments without ever providing or intending to provide any actual demand response was fraudulent.[77]

28. OE Staff assails Lincoln's explanations for its curtailment as internally inconsistent and unsupported by contemporaneous facts. OE Staff states that from April 2006 through July 2007 the Westinghouse generator experienced only five outages that

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[72] *Id.* at 22-23 (quoting *New England Power Pool and ISO New England Inc.*, 101 FERC ¶ 61,344, at PP 37-38 (2002)).

[73] *Id*. at 22.

[74] *Demand Response Compensation in Organized Wholesale Energy Markets*, Order No. 745, FERC Stats. & Regs. ¶ 31,322 (2011), *order on reh'g*, Order No. 745-A, 137 FERC ¶ 61,215 (2011).

[75] Show Cause Answer at 23-24.

[76] OE Staff Reply at 1.

[77] *Id*. at 2.

were not related to mill downtime or a scheduled overhaul and repair, and that once Lincoln began participating in the DALRP, the Westinghouse generator was out of service only three times from July 2007 through December 2007.[78] OE Staff argues that there is an inherent conflict between Lincoln's view that the ISO-NE Tariff's DALRP provisions were unclear and confusing and Lincoln's view that the tariff specifically contemplated an additional compensation for "pre-existing" demand response.[79]

29. OE Staff argues that the requirement to establish a customer baseline demonstrates that all behind-the-meter generation is not demand response – otherwise setting a customer baseline would be unnecessary.[80] OE Staff argues that it is "axiomatic" that demand response requires a "response" that results in an actual reduction of energy consumption from the grid compared to routine consumption.[81]

iii. Commission Determination

30. We find that Lincoln's conduct constitutes a fraudulent scheme or artifice, in violation of section 1c.2 of the Commission's regulations. The Commission has defined fraud in the context of section 1c.2 as including fraud's definition under the common law, i.e., any false statement, misrepresentation, or deceit. Fraud under section 1c.2 also includes "any action, transaction, or conspiracy for the purpose of impairing, obstructing or defeating a well-functioning market."[82] Fraud is a question of fact to be determined by all the circumstances of a case.[83] Lincoln devised and implemented a scheme to inflate its customer baseline and thereby be paid for demand response that it never intended to provide or actually provided. Under this scheme, for the DALRP program hours (7:00 AM to 6:00 PM) during the five-day initial customer baseline period (July 25, 26, 27, 30 and 31, 2007), Lincoln reduced its Westinghouse generator's operating level by approximately 3 MW from the level at which it otherwise would have operated given the

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[78] *Id*. at 16-17.

[79] *Id*. at n.5.

[80] *Id.* at 4.

[81] *Id.* at 4-6.

[82] Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 50 & n.103 (referencing *Dennis v. U.S.*, 384 U.S. 855, 861 (1966)).

[83] *Id*. P 50.

prevailing fuel and energy prices and mill energy requirements.[84] That departure from Lincoln's routine increased the amount of mill load served by energy from the grid and cost Lincoln approximately $10,000 over the five days in question.[85] Curtailing the Westinghouse generator in those hours – and only those hours – was uneconomic given Lincoln's ability and established practice of generating electricity from its Westinghouse generator at lower cost.[86] Therefore, we find that it served no legitimate purpose, but rather ensured the customer baseline did not reflect Lincoln's normal daily consumption pattern for energy taken from the grid.

31. This conduct resulted in the creation and the fraudulent communication to ISO-NE, of a higher, false customer baseline in those DALRP participation hours. After the initial five-day baseline period, Lincoln resumed routine operation of its Westinghouse generation during the hours of 7:00 AM to 6:00 PM.[87] Because of its inflated customer baseline, Lincoln portrayed a reduction from its inflated baseline simply by resuming routine use of its Westinghouse generator (which displaces energy taken from the grid) and thus enabled Lincoln to receive DALRP payments (calculated based on the difference between this inflated customer baseline and Lincoln's metered energy taken from the grid) without Lincoln having to alter its routine to provide any actual demand response.

32. We find that Lincoln perpetuated its inflated customer baseline by knowingly and fraudulently exploiting a DALRP provision that prevented a customer's baseline from adjusting on days when ISO-NE accepted its offer to provide demand response. In July and August 2007, Lincoln verified with Constellation that cleared daily offers into the DALRP would freeze the customer baseline.[88] Lincoln then made daily minimum

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[84] Show Cause Order at 8 (citing December 7, 2011 ISO-NE Data Response). *See* Show Cause Answer at 9 (stating that Lincoln curtailed the Westinghouse generator when setting the baseline); Van Scotter Dep. 99:16-25 (stating that the Westinghouse generator would probably not have been curtailed if Lincoln had not been participating in the DALRP); May 5, 2011 Lincoln Letter to OE at 8 (stating that Lincoln ramped down its Westinghouse turbine by approximately 3 MW when setting its baseline).

[85] Van Scotter Dep. 117:3-15; May 5, 2011 Lincoln Letter to OE Staff at 8.

[86] *See* Lincoln's May 5, 2011 Lincoln Letter to OE Staff at 7 (stating that pre-existing retail rates created incentives that meant Lincoln was running its Westinghouse unit near its maximum output in the time period just before the baseline was measured).

[87] *See* Brennan Dep. 182:23-183:21; Van Scotter Dep. 181:12-15.

[88] LINC000008-009; LINC000228.

DALRP offers knowing there was a high likelihood they would clear each day so that its customer baseline would not adjust, thereby ensuring that it would receive fraudulent payment for demand response that it appeared to provide only through its inflated customer baseline.[89]

33. We find that Lincoln's actions with respect to the DALRP defrauded ISO-NE at the expense of all ratepayers in the ISO-NE footprint. Lincoln's ongoing scheme caused electricity consumers in ISO-NE's footprint to pay $445,901.21 for demand response that never occurred. Of that amount, Lincoln received $379,016.03.[90]

34. Lincoln claims that complexities of the DALRP excuse its conduct; however, record evidence does not reflect that Lincoln misunderstood or was confused about the baseline procedure. To that end, no express prohibition on curtailing on-site generation during the initial customer baseline period in order to create a higher baseline was necessary. The DALRP process for calculating a customer baseline was straightforward. That process required no customer action other than to operate the customer's facilities as it routinely would. While Lincoln cherry-picks various statements in prior Commission orders to support its assertion that the DALRP was too complex to decipher, in 2002, the Commission clearly described the DALRP as a program that "would offer an additional financial benefit to customers for *reducing* their loads – a payment for the amount of the reduced load."[91] Although Lincoln claims ISO-NE and the Commission recognized the complexity of customer baseline methodologies in the 2008 DALRP modification orders, those references were to ISO-NE difficulties in designing accurate customer baseline methodologies ISO-wide, not to setting the baseline for particular customers.[92]

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[89] *See* LINC000228 (confirming Lincoln's understanding that the whole day is excluded from the baseline if the bid clears); LINC000511-516 (showing DALRP bids); Van Scotter Exh. No. 5 (stating that Lincoln wanted its bid to be $50 so that it clears); Van Scotter Dep. 127:9-13.

[90] *See* CNE0023813.

[91] *New England Power Pool*, 101 FERC ¶ 61,344 at P 38 (emphasis added).

[92] *See* April 4, 2008 Order, 123 FERC ¶ 61,266 at P 29 ("ISO-NE notes that Customer Baseline methodologies for demand response programs are complex, and that changes that could address the instant problem are by no means intuitive. Accordingly, ISO-NE maintains that changing the Customer Baseline methodology would not be a simple undertaking, and could consume from several months to more than a year to research, design, discuss, approve and implement such changes.").

35. Furthermore, even assuming, *arguendo*, that certain features of the DALRP such as the minimum offer price left the DALRP vulnerable to certain manipulation, that does not excuse the manipulation itself. Lincoln would not have benefitted to the extent it did without establishing and maintaining an artificially high customer baseline. Lincoln's scheme was not an inevitable result of the DALRP's structure at the time.

36. We also reject Lincoln's arguments that a finding of fraud must be premised on the violation of a tariff, rule, or regulation. An entity need not violate a tariff, rule or regulation to commit fraud.[93] Nor does a finding of fraud require advance notice specifically prohibiting the conduct concerned. Fraud is a matter of fact and requires evaluation of all the facts and circumstances of each case.[94] The Commission need not imagine and specifically proscribe in advance every example of fraudulent behavior. We find that Lincoln's fraudulent conduct violates section 1c.2 regardless of whether it violates a specific tariff provision.

37. Similarly, we reject Lincoln's defense that neither Constellation nor ISO-NE warned Lincoln that it had set its customer baseline incorrectly. Lincoln did not seek advice or assistance from Constellation or ISO-NE relevant to setting its baseline,[95] and, as stated above, an express warning against engaging in certain behavior (whether before or after the fact) is not a prerequisite to finding that the subject behavior constitutes fraud.

38. We reject Lincoln's claim that its inflated customer baseline was a legitimate interpretation of providing an "additional financial benefit" for reducing load. By reducing load, participants purchase less energy and receive compensation for their load reductions. The "additional financial benefit" was compensation for reducing load. Here, Lincoln did not reduce its load during its participation in the DALRP and thus it is not entitled to payment for demand response.

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[93] *See* Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 25 (noting that the Commission's rules against market manipulation apply to "all forms of fraud and manipulation that affect . . . electric energy transactions and activities the Commission is charged with protecting"); *see also In Re Make-Whole Payments and Related Bidding Strategies*, 144 FERC ¶ 61,068, at P 83 (2013) ("as Order No. 670 emphasizes, fraud is a question of fact to be determined by all the circumstances of a case, not by a mechanical rule limiting manipulation to tariff violations" (footnote omitted)).

[94] *See* Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 50.

[95] *See* Van Scotter Dep. 82:12-17, 97:16-24, 111:14-25.

39. We further reject Lincoln's apparent argument that by running its Westinghouse generator, Lincoln already had been providing demand response prior to the initial baseline measurement period, and, therefore, it properly shut off the on-site generator to measure Lincoln's load absent that so-called "pre-existing demand response." In support, Lincoln erroneously cites Order No. 745, the Commission's final rule establishing the appropriate compensation level for demand response.[96] As an initial matter, Order No. 745 and its progeny were issued subsequent to the conduct at issue here and apply prospectively, not retroactively; the rulemaking proceeding is irrelevant to determining whether Lincoln engaged in prohibited conduct during any preceding period. In any case, Order No. 745 and its progeny did not categorically characterize use of behind-the-meter generation as demand response for any purpose, be it compensation or establishing customer baselines.[97] This point is illustrated by the Commission's acceptance of various ISO and regional transmission organization (RTO) compliance filings to Order No. 745, despite their divergent treatment of resources with behind-the-meter generation.[98] In fact, the Commission has rejected calls for standardized treatment of behind-the-meter generation in determining compensation or baselines, while noting that "demand reductions that are not genuine may be violations of the Commission's anti-manipulation rules."[99] Moreover, in relying on Order No. 745, Lincoln conflates two distinct issues: requisite compensation for demand response (which Order No. 745 addresses) with requisite criteria for establishing a resource-specific baseline (which Order No. 745 does not address). Even if resources facilitated by behind-the-meter generation are eligible to receive demand response compensation under a particular tariff, that does not mean that an individual resource that is likely to use (or has used) its behind-the-meter generation regardless of whether it receives (or has received) compensation may shut down the generator for purposes of establishing its baseline.

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[96] *See* Order No. 745, FERC Stats. & Regs. ¶ 31,322 .

[97] *See* Order No. 745-A, 137 FERC ¶ 61,215 at P 66; *ISO New England, Inc.*, 138 FERC ¶ 61,042, at P 76, *order on reh'g*, 139 FERC ¶ 61,116, at P 10 (2012).

[98] *See N.Y. Indep. Sys. Operator, Inc.*, 143 FERC ¶ 61,134, at P 101 (2013) (compensation for demand response precluded where facilitated by behind-the-meter generation); *ISO New England, Inc.*, 138 FERC ¶ 61,042, *order on reh'g*, 139 FERC ¶ 61,116 (2012) (compensation for demand response allowed where facilitated by behind-the-meter generation that results in net reduction to the grid).

[99] Order No. 745, FERC Stats. & Regs. ¶ 31,322 at P 954; Order No. 745-A, 137 FERC ¶ 61,215 at 66 & n. 123; *ISO New England, Inc.*, 139 FERC ¶ 61,116 at P 20 n.26.

b. Scienter

i. Show Cause Answer

40. Lincoln argues that its customer baseline reasonably reflected its expected future operation of on-site generation (and associated grid consumption) rather than an intent to deceive. Lincoln claims it did not view its Westinghouse generator as a reliable resource that would be part of its normal operations and therefore it was appropriate to curtail its unit during the initial customer baseline period.[100] In support, Lincoln identifies unit outages in the year prior to the initial customer baseline period and notes its decision to change its operations to allow the mill to continue production based solely on energy from the grid.[101]

41. Lincoln rejects OE Staff's argument that its regularly submitted $50/MWh bids were part of a scheme to maintain an inflated customer baseline. Lincoln argues that it simply wanted its bids to clear, just like any other bidder, and that it actually preferred low energy prices so that its energy costs would be lower.[102] Lincoln also argues that OE Staff incorrectly asserted that Lincoln's customer baseline remained unchanged, noting that its customer baseline adjusted on nine occasions by 1.66 MW over the course of its participation in the DALRP.[103]

42. Lincoln argues that OE Staff inappropriately seeks to establish intent by the act itself. Lincoln claims it believed its DALRP participation was appropriate and that therefore collecting payment based on that participation is not evidence of intent to manipulate the program.[104]

43. Lincoln further asserts it lacked scienter because it did not hide any of its actions from Constellation, which at all times knew its customer baseline level and had access to

[100] Show Cause Answer at 27-28.

[101] *Id.* at 28.

[102] *Id*. at 20-21.

[103] *Id*. at 21.

[104] *Id.* at 35.

its metering data, and that Constellation or ISO-NE could have readily determined how Lincoln set its customer baseline.[105]

44. Lincoln additionally disputes OE Staff's alternate scienter argument that Lincoln's behavior was reckless if not intentional. Lincoln rejects OE Staff's argument that Lincoln participated in prior demand response programs even though it had no load shedding procedures for DALRP participation. Lincoln contends that its lack of such procedures does not imply recklessness because the existing procedures were sufficient had Lincoln been required to shed load.[106] Lincoln argues that it attempted to change its energy consumption by undertaking various additional measures to alter its operations.

ii. OE Staff Report and Reply

45. OE Staff reiterates that Lincoln knowingly established and communicated to ISO-NE an inflated customer baseline that did not reflect Lincoln's genuine demand response capability and that Lincoln did not intend to alter its normal energy consumption or generation pattern.[107] OE Staff argues that Lincoln further submitted load reduction offers at the minimum values to perpetuate its inflated customer baseline.

46. With regard to Lincoln's lack of load shedding procedures, OE Staff notes that Lincoln had previously participated in ISO-NE demand response programs and had prepared detailed written procedures instructing how to shed load for those programs. OE Staff argues that the fact that Lincoln did not develop or implement any such procedures for its DALRP participation shows that it was reckless.[108]

iii. Commission Determination

47. We find that Lincoln had the requisite scienter when it engaged in a fraudulent scheme or artifice. Scienter is the second element of 18 C.F.R. § 1c.2.[109] For purposes of establishing scienter, Order No. 670 requires reckless, knowing, or intentional actions

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[105] *Id.* at 30-31.

[106] *Id.* at 36.

[107] OE Staff Report at 12.

[108] *Id.* at 13-14.

[109] Order No. 670, FERC Stats. & Regs. ¶ 31,202 at P 49.

taken in conjunction with a fraudulent scheme or artifice.[110] As we described above, Lincoln curtailed its generator during the initial customer baseline-setting period and submitted demand response bids almost every hour of every day during its participation in the DALRP.[111] Lincoln purchased approximately $10,000 of grid electricity rather than generating that energy using its generator at a lower cost, per its routine practices.[112] The record reflects no reason for this conduct other than to inflate Lincoln's customer baseline so that it could receive DALRP payments without having to reduce Lincoln's load taken from the grid during hours the relevant bids were accepted. As stated, we find that Lincoln understood the purpose of the customer baseline and how ISO-NE would calculate it for Lincoln. Lincoln thus recognized – and intended – that curtailing its generator during the initial customer baseline period would artificially inflate its customer baseline and thereby allow Lincoln to be paid for future DALRP participation without actually reducing load.

48. We find that Lincoln's submission of continuous minimum $50/MWh demand response offers is further evidence that Lincoln intended to enter into a fraudulent scheme that would prevent or delay changes to its customer baseline in order to continue to receive payments for non-existent demand response. Lincoln twice sought confirmation from Constellation that cleared daily offers into the DALRP would freeze its customer baseline.[113] We are unpersuaded by Lincoln's argument that it submitted its $50/MWh offers solely because it wanted its bids to clear. Having found that Lincoln first intentionally inflated its customer baseline, Lincoln would next have had to submit minimum offers to prevent that customer baseline from adjusting to ensure it continued to receive fraudulent DALRP payments. Lincoln's argument that its customer baseline did adjust on multiple occasions during its participation in the DALRP does not alter our conclusion that Lincoln acted with fraudulent intent. Lincoln's customer baseline changed because a small number of its offers were mistakenly submitted improperly and failed to clear.[114] Had they cleared, as we believe Lincoln intended, they would have prevented the customer baseline from adjusting.

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[110] *Id.* PP 52-53.

[111] Show Cause Answer at 9; LINC000511-516.

[112] Van Scotter Dep. 117:8-15; May 5, 2011 Lincoln Letter to OE Staff at 8.

[113] LINC000008-009; LINC000228.

[114] *See* LINC00511-516.

49. We reject Lincoln's claims that it curtailed its Westinghouse generator during the initial customer baseline period because it did not view the Westinghouse generator as a reliable resource that would be part of its normal operations. There is no contemporaneous evidence that Lincoln set its customer baseline the way it did due to these operational concerns. Indeed, Lincoln consistently relied on the Westinghouse generator before, during, and after the initial customer baseline period.[115] We find that Lincoln did not curtail its generation to ensure that its customer baseline reflected its expected operations, but rather to increase its DALRP payments.

50. We find no indication that Lincoln was confused about how to legitimately participate in the DALRP and instead find that Lincoln acted intentionally to inflate its customer baseline. Lincoln never sought assistance from Constellation or ISO-NE, and remained silent, failing to notify Constellation or ISO-NE that it had curtailed its on-site generator during the initial baseline measurement period, even after it received two Constellation correspondences suggesting potential abuses in customer baseline establishment.[116]

51. Because we have found that Lincoln possessed the requisite intent, we need not reach the issue of whether Lincoln's conduct here meets the scienter element through recklessness.

c. <u>In Connection with a Jurisdictional Transaction</u>

52. We find that Lincoln's fraudulent scheme was in connection with a jurisdictional transaction. The third element of establishing a violation of 18 C.F.R. § 1c.2 is determining whether the conduct in question was "in connection with" a transaction subject to the Commission's jurisdiction.[117] Section 201(b)(1) of the FPA bestows jurisdiction to the Commission over "the sale of electric energy at wholesale in interstate commerce."[118] Section 205(a) of the FPA confers jurisdiction to the Commission over "[a]ll rates and charges made, demanded or received by any public utility for or in connection with the . . . sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or

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[115] *See* Van Scotter Dep. 46:14-18; 47:1-5.

[116] LINC000025; LINC000236-237.

[117] 16 U.S.C. § 824v(a) (2006); 18 C.F.R. § 1c.2(a) (2013).

[118] 16 U.S.C. § 824(b)(1) (2006).

charges."[119] There is well-established court precedent with respect to Commission jurisdiction over practices that directly or significantly affect rates under the FPA.[120] A demand response resource that may not be a public utility nonetheless may choose to participate in ISO-administered organized wholesale energy markets, therefore making it a market participant. The Commission has repeatedly found that market rules governing such participation by demand response resources in an organized wholesale energy market constitute practices that directly affect rates in those jurisdictional markets and therefore are subject to the Commission's jurisdiction under section 205(a) and (c) of the FPA.[121] Here, ISO-NE's markets are within the Commission's jurisdiction, as is ISO-NE's Commission-approved DALRP.[122] Therefore, we find Lincoln's fraudulent scheme to be conducted in connection with a jurisdictional transaction.

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[119] *Id.* § 824d(a) (2006).

[120] *See Conn. Dep't of Pub. Util. Control v. FERC*, 569 F.3d 477, 484 (D.C. Cir. 2009) ("[w]here capacity decisions about an interconnected bulk power system affect FERC-jurisdictional transmission rates for that system without directly implicating generation facilities, they come within the Commission's authority" as a practice affecting rates under FPA); *Miss. Industries v. FERC*, 808 F.2d 1525, 1542 (D.C. Cir. 1987) (while capacity allocation costs "do not fix wholesale rates, their terms do directly and significantly affect the wholesale rates at which the operating companies exchange energy"); *City of Cleveland v. FERC*, 773 F.2d 1368, 1376 (D.C. Cir. 1985) ("there is an infinitude of practices affecting rates and services"); *Groton v. FERC*, 587 F.2d 1296, 1302 (D.C. Cir. 1978) (capacity deficiency charge, just as the capacity adjustment charge "must be deemed to be within the Commission's jurisdiction because it too represents a charge for the power and service the overloaded participant receives or it is at least a rule or practice affecting the charge for these services").

[121] *See* Order No. 745-A, 137 FERC ¶ 61,215 at PP 20-35; *EnergyConnect, Inc.*, 130 FERC ¶ 61,031, at PP 27-32 (2010) (Commission has jurisdiction to regulate certain aspects of demand response and ISO market rules governing demand response as practices significantly affecting rates in organized wholesale electric markets).

[122] *See, e.g.*, September 11, 2008 Order, 124 FERC ¶ 61,235 at P 25 (approving revision to ISO-NE DALRP as just and reasonable); April 4, 2008 Order, 123 FERC ¶ 61,021 at PP 63-65 (approving revision to ISO-NE DALRP as just and reasonable); *New England Power Pool & ISO New England, Inc.*, 111 FERC ¶ 61,064 (2005) (approving ISO-NE demand response programs and related tariff provisions).

III. Civil Penalty Determination

53. Having concluded that Lincoln, in connection with the purchase or sale of electricity, knowingly devised and participated in a scheme to manipulate the wholesale power markets in violation of section 222(a) of the FPA and section 1c.2 of the Commission's regulations, we now must determine the appropriate remedies to assess. The OE Staff Report recommends that we assess civil penalties and disgorgement against Lincoln. After assessing the legal and factual issues, including those raised by the Lincoln, and "tak[ing] into consideration the seriousness of the violation and the efforts of such person to remedy the violation in a timely manner,"[123] we agree with OE Staff's recommendation and assess penalties and disgorgement.

54. Pursuant to section 316A of the FPA, the Commission may assess a civil penalty of up to $1 million per day, per violation against any person who violates Part II of the FPA (including section 222 0f the FPA) or any rule or order thereunder.[124] In determining the amount of a proposed penalty, section 316A(b) requires the Commission to consider "the seriousness of the violation and the efforts of such person to remedy the violation in a timely manner."[125] Although the Penalty Guidelines are not mandatory, the Commission uses them, and its policy statements on enforcement, to guide its analysis.[126]

55. The Penalty Guidelines assess the seriousness of particular violations by determining a Base Violation Level based on the type of violation involved. The Penalty Guidelines then adjust the Base Violation Level by considering the gain to the organization or the loss caused by the violation, and either the amount of energy involved in the violation or the duration of the violation, whichever is greater. The resulting violation level indicates a base penalty amount that is then adjusted using a culpability score multiplier to establish a penalty range. The Penalty Guidelines consider a variety of factors relating to a violator's culpability to determine the overall culpability score. The culpability score factors include evaluations of the efforts of the violator to remedy its violation. After establishing a penalty range, the Commission examines the specific facts of each case to determine where the ultimate penalty should fall within or, in appropriate circumstances, outside the indicated civil penalty range. Where facts warrant, the Commission retains discretion to deviate from the Penalty Guidelines range,

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[123] 16 U.S.C. § 825o-1(b) (2006).

[124] *Id*.

[125] *Id*.

[126] *See supra* note 13.

but has cautioned that it "do[es] not intend to depart from the Penalty Guidelines regularly."[127]

A. Show Cause Answer

56. Lincoln argues that OE Staff misapplied the Commission's Penalty Guidelines to produce an inflated $4,400,000 penalty and an incorrect disgorgement of $379,016.03.[128] Instead, Lincoln urges no civil penalty and if any, a reduced disgorgement of $235,259.47.

57. Lincoln asserts that OE Staff overstates the amount of market harm because OE Staff used the full amount paid by ISO-NE for Lincoln's demand response participation ($445,901.21). Lincoln seeks two subtractions from OE Staff's figure. First, Lincoln argues that $154,701.92 of its compensation was attributable to Lincoln's hourly load reductions that were even below the customer baseline level OE Staff asserts is proper in this case.[129] Thus, Lincoln argues these payments were for actual demand response not includable in harm because the load reduction exceeded the 3 MW by which OE Staff claims Lincoln fraudulently increased its customer baseline.[130] Second, Lincoln argues OE Staff's market harm figure should not include the 15 percent of ISO-NE DALRP payments kept by Constellation. Lincoln accordingly reduces the market harm figure to $235,259.47.[131]

58. Additionally, Lincoln generally asserts it did not harm ISO-NE customers. Lincoln claims those customers benefitted by Lincoln's continued operation of the Westinghouse generator (outside of the baseline measurement period) to displace power that Lincoln otherwise would have taken from the grid. Without market harm, Lincoln asserts that the Penalty Guidelines limit its base penalty to its alleged pecuniary gain (Lincoln's reduced market harm figure of $235,259.47).[132]

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[127] Initial Penalty Guidelines Order, 130 FERC ¶ 61,220 at P 32.

[128] Show Cause Answer at 37-44 (citing Penalty Guidelines).

[129] *See* Show Cause Answer at Exhibit JW-2(column J) (listing payments attributable to Lincoln's hourly load reductions above 3 MW).

[130] *Id.* at 38.

[131] *Id.* at 38-39.

[132] *Id.* at 39 (citing Penalty Guidelines § 1C2.2(a)).

59. Lincoln further disputes OE Staff's use of a durational enhancement for a violation lasting more than 50 but less than 250 days.[133] Lincoln states OE Staff's violation level already was based on the cumulative monetary harm to ISO-NE customers that increased in value for each of Lincoln's daily offers. Lincoln argues that an additional duration enhancement based on the days of the violation improperly double counts duration in the Base Violation Level.[134]

60. Lincoln requests the Commission not apply a culpability score enhancement under section 1C2.3(b) of the Penalty Guidelines for the involvement in the violation by its President and Chief Executive Officer (CEO), Keith Van Scotter, and others whom Lincoln concedes meet the definition of "high-level personnel" or "substantial authority" personnel.[135] Lincoln claims this culpability score enhancement's purpose – encouraging FERC-regulated companies to acquaint themselves and comply with Commission rules – is inappropriately applied to a small non-energy company such as Lincoln that did not routinely engage in Commission-regulated matters and lacked expertise in Commission issues.[136]

61. Lastly, Lincoln contends OE Staff's proposed penalty inadequately considers Lincoln's inability to pay a penalty, even one as low as the $188,208 - $376,415 Lincoln advocates.[137] In support, Lincoln presents the affidavit of John Wisser, Lincoln's Chief Financial Officer, which Lincoln asserts contains updated financial information indicating an inability to pay the proposed penalty.[138] Accordingly, Lincoln requests its penalty be reduced to the low end of or below Lincoln's suggested penalty range.

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[133] *Id.* at 42 (citing Show Cause Order, 140 FERC ¶ 61,031 at 61,117; *Rumford Paper Co.*, 140 FERC ¶ 61,030 (2012) (LaFleur, Comm'r, concurring)).

[134] *Id.* at 43.

[135] *Id.* at 40.

[136] *Id.*

[137] Lincoln suggests this penalty range is appropriate when the Penalty Guidelines are applied consistently with its above arguments.

[138] In the trailing twelve month period ending July 31, 2012, Lincoln states it had net sales of $147,294,581 and generated $5,726,882 of Earnings Before Interest, Taxes, Depreciation, and Amortization. From this, Lincoln states it had minimum principal and interest payments totaling $5,109,820.62 and sustaining capital investments of $3,311,500, resulting in negative cash flow of $2,694,438.62. Lincoln's liabilities

(continued…)

B. OE Staff Report and Reply

62. OE Staff argues that Lincoln's violation warrants assessment of the proposed $4,400,000 civil penalty and the full, unadjusted $379,016.03 of disgorgement. OE Staff states that the market harm is $445,901.21, which is the amount actually paid by ISO-NE. [139] OE Staff rejects Lincoln's argument that it legitimately received payment for any demand response in excess of 3 MW, characterizing Lincoln's behavior while in the DALRP as continually intending only to perpetuate its initial customer baseline fraud and not to provide any demand response.[140]

63. In support of a duration enhancement,[141] OE Staff states that Lincoln's behavior was not limited to a single incident of fraud but rather was a "conscious, continuing deception of ISO-NE by submitting daily offers that promised to reduce load that Lincoln had no intention of reducing."[142] OE Staff similarly rejects Lincoln's requested deviation from the culpability enhancement for "high level personnel" and persons with "substantial authority" based on its status as a non-traditional energy company. OE Staff notes that Lincoln concedes that its President and CEO qualifies as high-level personnel and argues that the Commission should not deviate from the Penalty Guidelines in that regard.[143]

64. OE Staff further asserts that the Commission should reconsider awarding Lincoln cooperation credit based on two instances evidencing less than full cooperation.[144] OE

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include a $25.2 million debt. Lincoln's cash position on July 31, 2012, was $4.3 million (net of book overdraft), with $10.7 million of accounts payables and accrued expenses, including $1.8 million of payables which are beyond terms. On July 31, 2012, Lincoln owed $4.4 million on its revolving credit facility and had another $0.3 million blocked by a reserve for an outstanding letter of credit.

[139] OE Staff Reply at 14 (citing Penalty Guidelines at Application Note 2A(i) to § 2B1.1).

[140] *Id.* at 16.

[141] *Id.* (citing Penalty Guidelines, § 2B1.1(b)(2)).

[142] *Id.* at 16-17.

[143] *Id.* at 16.

[144] *Id.* at 21.

Staff states it served a February 2011 data request on Lincoln calling for certain financial information, including future projections. Although this data request's instructions required supplementation of responses,[145] OE Staff notes that Lincoln never did so yet still submitted new financial information as part of its Show Cause Answer.[146] OE Staff further claims that Lincoln refused OE Staff's post-Show Cause Answer request to supplement Lincoln's February 2011 data response with its new financial data and narrative responses.[147] OE Staff also notes that it discovered after the Show Cause Answer that Lincoln had not supplemented an earlier response to an April 2008 OE Staff data request for which Lincoln later had discovered more than 200 pages of additional responsive e-mails, one of which it cited in the Show Cause Answer.[148] OE Staff claims Lincoln initially resisted supplementing its earlier response and then resisted producing the responsive e-mails in native form with searchable metadata.[149] OE Staff further asserts that once Lincoln did agree to provide the e-mails with searchable metadata it made only an incomplete production over a two-week period (October 24 to November 8, 2012) and offered to provide the balance of the production on the due date for OE Staff's Reply.[150] As a result, OE Staff asserts it could not reasonably analyze this metadata before its November 13, 2012 Reply.[151]

65. OE Staff also argues that Lincoln has failed to demonstrate that a reduction in the civil penalty is necessary to avoid jeopardizing the continued viability of the company. OE Staff notes that it considered Lincoln's continued financial viability on multiple occasions and that Lincoln's financial situation is sufficiently healthy to permit Lincoln to pay the proposed civil penalty, particularly if paid over a period of years on a payment

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[145] OE Staff's data request instructions to Lincoln specified: "Each data request is continuing in nature and requires supplemental responses as soon as further information is located or obtained that is responsive to the request." *Id.* at 21.

[146] *Id.* OE Staff notes that some of Lincoln's submitted new financial information dates from April 2012, five months before the Show Cause Answer. *Id.*

[147] *Id.* at 22.

[148] *Id.* As with the February 2011 data request, the April 2008 data request also was continuing in nature and required supplementation. *Id.*

[149] *Id.* at 22.

[150] *Id.* at 23.

[151] *Id.*

plan as permitted by the Penalty Guidelines.[152] OE Staff further states that Lincoln's currently claimed financial position should take into account significant profit distributions made to Lincoln's owners in 2009 and 2010, which according to OE Staff, indicate an ability to pay the proposed civil penalty.[153]

C. **<u>Commission Determination</u>**

1. **<u>Seriousness of the Violation</u>**

66. We discuss the factors in the Penalty Guidelines and Policy Statements on Enforcement that are relevant to the seriousness of Lincoln's violation below, to the extent applicable. These factors establish that Lincoln's violations were serious and warrant a penalty.

67. *Manipulation, Deceit, Fraud, and Recklessness or Indifference to Results of Actions.* As noted above in Section II, Lincoln's scheme violated section 1c.2 of the Commission's regulations and falls under section 2B1.1 of the Penalty Guidelines (Fraud, Anti-Competitive Conduct and Other Rule, Tariff and Order Violations). This violation begins with a Base Violation Level of 6, as required by section 2B1.1(a) of the Penalty Guidelines.

68. *Harm Caused by the Violation*. The Penalty Guidelines measure a violation's seriousness in part by examining the gain or loss caused. Application Note 2A to Penalty Guidelines § 2B1.1 specifies that "loss" is the greater of "actual loss or intended loss." Application Note 2A (i) then defines "actual loss" as "the reasonably foreseeable pecuniary harm that resulted from the violation." Here, Lincoln's violations resulted in ISO-NE (on behalf of its customers) paying Lincoln and Constellation $445,901.21 across more than six months in 2007 and 2008 for non-existent demand response resulting from Lincoln's artificially inflated baseline. We agree with OE Staff that all of these DALRP payments attributable to Lincoln's program participation (including the payments to Constellation) were reasonably foreseeable and are properly part of the "actual loss." We also agree with OE Staff that market harm should not be reduced by the ISO-NE DALRP payments for hourly reductions in excess of 3 MW. Non-intentional hourly variations in Lincoln's load that left it more than 3 MW below its fraudulently established customer baseline do not warrant payments here where, from the outset,

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[152] *Id.* at 18-20.

[153] *Id.* (citing Penalty Guidelines at § 1C3.2). OE Staff also contends Lincoln's failure to update its financial information prior to its filing calls into question Lincoln's eligibility for a cooperation credit under section 1c2.3(g)(2) of the Penalty Guidelines.

Lincoln's entire DALRP participation was based on fraud. We also reject Lincoln's view that its continued operation of its Westinghouse generator provided a legitimate benefit to ISO-NE customers that would support a finding of no market harm. Lincoln harmed ISO-NE and its customers through the payments that ISO-NE made for demand response that Lincoln did not provide. Accordingly, $445,901.21 is the appropriate market harm figure under section 2B1.1(b)(1) of the Penalty Guidelines, increasing Lincoln's Base Violation Level of 6 points by an additional 14 points.

69. *Isolated Instance or Recurring Problem, Systematic and Persistent Wrongdoing, and Duration.* Lincoln persistently and systematically provided fraudulent offers to ISO-NE for more than six months. Lincoln's violation began during the five days in which it established its initial customer baseline and extended for each day during the period Lincoln made daily offers at a level designed to perpetuate its initial artificial customer baseline. We agree with OE Staff that Lincoln's conduct warrants enhancement of the violation level provided under section 2B1.2(E) of the Penalty Guidelines for a violation continuing for more than 50 days but less than 250 days. This increases Lincoln's Base Violation Level by an additional 4 points.

70. *Violation Level.* Based on the above, we find Lincoln's final violation level is 24 (calculated as the Base Violation Level of 6 points for fraud plus the above-described increases of 14 points for harm and 4 points for duration). A violation level of 24 indicates a base penalty of $2,100,000 under the Penalty Guidelines.

2. <u>Mitigating Factors Relating to Culpability</u>

71. *Involvement in or Tolerance of Violations.* Section 1c2.3(a) requires a base culpability score of 5, which is increased if high-level personnel or substantial authority personnel participated in or tolerated the violation under section 1C2.3(b). Here, the individuals involved in Lincoln's baseline-setting scheme meet the Penalty Guideline's definition of high-level personnel or substantial authority personnel. We reject Lincoln's request for a deviation from this increase merely because it is a non-energy company; such a distinction is irrelevant to culpability. Lincoln concedes that its senior managers orchestrated and participated in setting the baseline, which we have found to be part of a fraudulent scheme, and it is appropriate that their involvement increase Lincoln's penalty. Section1c2.3(b)(3) requires an additional 3 points if the organization had 200 or more employees and an individual within high-level personnel of the organization participated in the violation. Based on Lincoln's size of approximately 400 employees and the involvement of high-level and substantial authority personnel, we find that Lincoln's culpability score should be increased by 3 points pursuant to section 1C2.3(b)(3) of the Penalty Guidelines.

72. *Prior History, Violation of Commission Order, and Obstruction of Justice.* Under section 1C2.3(c)-(e) of the Penalty Guidelines, the Commission can increase the culpability score if the organization involved has a prior history of violations, violates a

Commission order, or engages in obstruction of justice. Because none of these concerns arise here no increase in the culpability score is required for any of these factors.

73. *Commitment to Compliance and Actions Taken to Correct Violation.* Under section 1C2.3(f) of the Penalty Guidelines, the Commission may reduce the base 5 point culpability score by up to 3 points to take into account the nature and extent of an entity's internal compliance measures in existence at the time of the violation. Lincoln had no chief compliance officer or similar individual specifically tasked with ensuring that Lincoln complied with regulatory requirements; Lincoln provided no training or formal written guidance to personnel responsible for managing Lincoln's participating in the DALRP aside from Constellation sales materials and ISO-NE manuals; and Lincoln's management provided employees tasked with DALRP participation no specific energy compliance policies. Under these circumstances, we find that no compliance program credit is warranted.

74. *Cooperation.* Under section 1C2.3(g)(2) of the Penalty Guidelines, the Commission may reduce the base culpability score by 1 point if an organization cooperated in the investigation. To qualify for a reduction under subsection (g)(2), cooperation must be both timely and thorough. "To be timely, the cooperation must begin essentially at the same time as the organization is notified by the Commission or Commission staff of an investigation. To be thorough, the cooperation should include the disclosure of all pertinent information known by the organization." [154] The record reflects that Lincoln failed to supplement its initial data responses as instructed in OE Staff's 2011 data requests. Instead, almost a year later, Lincoln submitted significantly changed financial information in its 2012 answer to the Show Cause Order. Additionally, Lincoln delayed production of approximately 200 emails that should have been provided in response to an April 2008 OE Staff data request and only after multiple requests by OE Staff finally produced the information in a useable format.[155] We find that Lincoln's cooperation was neither timely nor thorough and, accordingly, we do not reduce Lincoln's culpability score for cooperation.

75. *Self-Reporting*. Under section 1C2.3(g)(1) of the Penalty Guidelines, the Commission may reduce the base culpability score by 2 points if an organization self-reports a violation. Lincoln made no report, and instead ISO-NE discovered and referred its conduct. No credit is warranted for self-reporting. We find no reduction in the culpability score is warranted.

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[154] *See* Application Note 11 to Penalty Guidelines § 1C2.3(g).

[155] OE Staff Reply at 21-23.

76. *Culpability Score.* We find Lincoln's final culpability score is 8 points (base score of 5 points increased by 3 points for senior manager involvement considering Lincoln's size). A culpability score of 8 indicates a multiplier of 1.6 to 3.2 which is then applied to the base penalty of $2,100,000 to produce a penalty range of from $3,360,000 to $6,720,000 under the Penalty Guidelines.

3. Appropriate Penalty and Disgorgement

77. Based on the foregoing factors, the pleadings in this case, and the OE Staff Report, the Commission finds that a civil penalty of $5,000,000 and a disgorgement of $379,016.03, plus interest, is fair and reasonable under the circumstances. This civil penalty amount is within the Penalty Guidelines range resulting from the foregoing analysis ($3,360,000 to $6,720,000) from which we have made no deviations. Although the Staff Report and Show Cause Order originally sought a $4,400,000 civil penalty, that civil penalty was in the middle of the Penalty Guidelines range that was calculated based on awarding Lincoln one point for cooperation credit ($2,940,000 to $5,880,000). Our decision to deny that cooperation credit increased the penalty range by $420,000 to $840,000 (an increase of 0.2 to 0.4 in the culpability score penalty multiplier applied to the $2,100,000 base penalty). Accordingly, we have increased the proposed $4,400,000 civil penalty by $600,000 to $5,000,000 to keep the resulting penalty in the middle of the recalculated Penalty Guidelines range reflecting the removal of any credit for cooperation.

78. We note that in concluding that $5,000,000 is a fair and reasonable civil penalty we have taken into consideration Lincoln's current financial condition. Our Penalty Guidelines establish that a reduction based on inability to pay is applicable only where the Commission finds that the organization is not able and, even with the use of a reasonable installment schedule, is not likely to become able, to pay the minimum payment required by the Penalty Guidelines. Those standards also require that any reduction from the otherwise applicable penalty amount be "no more than necessary to avoid substantially jeopardizing the continued viability of the organization."[156] Measured by this standard, we agree with OE Staff that Lincoln can pay a civil penalty without substantially jeopardizing its continued operation. Moreover, we agree with OE Staff that a payment plan can alleviate any concern about Lincoln's inability to pay a penalty. Therefore, we direct Lincoln to either (a) pay the $5,000,000 civil penalty and disgorgement of $379,016.03, plus interest, within 60 days of the date of this order, or (b) within 30 days of this order, submit for Commission approval a payment plan agreed to by Lincoln and OE Staff.

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[156] *See* Penalty Guidelines, § 1C3.2 and Application Note 1 to Penalty Guidelines § 1C3.2.

79. If Lincoln does not agree to a payment plan with OE Staff within 30 days or does not pay the $5,000,000 civil penalty and disgorgement of $379,016.03, plus interest, within 60 days of the date of this order, then the Commission will commence an action in a United States district court for an order affirming the penalty, in which the district court may review the assessment of the civil penalty *de novo*.[157]

80. Finally, this order will not be subject to rehearing.

The Commission orders:

(A) Lincoln is hereby directed to pay to the United States Treasury by a wire transfer a civil penalty in the sum of $5,000,000 and to pay disgorgement of $379,016.03, plus interest, to ISO-NE, as discussed in the body of this order.

(B) Lincoln is hereby directed to either:

(1) pay the $5,000,000 civil penalty to the United States Treasury and disgorgement of $379,016.03, plus interest, to ISO-NE, within 60 days of the date of this order; or

(2) within 30 days of the date of this order, submit for Commission approval a payment plan agreed to by Lincoln and OE Staff, as discussed in the body of this order.

By the Commission. Commissioner LaFleur is dissenting in part with a separate statement attached.

Kimberly D. Bose,
Secretary.

[157] 16 U.S.C. § 823b(d)(3)(B) (2006).

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Lincoln Paper and Tissue, LLC   Docket No. IN12-10-000

(Issued August 29, 2013)

LaFLEUR, Commissioner, *dissenting in part*:

Under the Federal Power Act, the Commission has the authority and responsibility to identify and punish fraud in wholesale markets. This includes cases where the fraud is perpetuated by industrial entities that participate in wholesale demand response programs. Grid operators increasingly rely on demand resources to meet customers' energy, capacity, and ancillary services needs. If a demand resource devises a scheme to receive payments without reducing demand, customers will not only suffer the monetary loss caused by the theft, they may also face threats to reliability as grid operators find themselves unable to rely on expected reductions in demand.

I join the majority in finding that Lincoln Paper and Tissue, LLC (Lincoln) engaged in fraud by devising a scheme to collect payments for demand response that it neither provided nor intended to provide, and that Lincoln must now be made to disgorge its profits and pay a civil penalty. However, I part company with the majority on the narrow point of how that civil penalty should be calculated.

When the Commission exercises its civil penalty authority, it must do so with care and due regard for the circumstances of the particular violation. At a minimum, it must explain in each case why adherence to the Penalty Guidelines is appropriate.[1] In some situations, the Commission may have to depart from the Guidelines and assess a civil penalty that is more tailored to the circumstances at hand.[2]

This case presents such an instance. As I explain below, strictly following the formula

[1] *Enforcement of Statutes, Orders, Rules, and Regulations*, 132 FERC ¶ 61,216 at P 211 (2010) (Penalty Guidelines) ("This is a policy statement. Consistent with the APA, when the Commission applies the Penalty Guidelines in orders, we will present why it is appropriate to apply the Penalty Guidelines and will justify their application in the particular circumstances at hand.").

[2] *Id*. P 32 ("Generally, we recognize that the Penalty Guidelines may not always account for the specific facts and circumstances of every case. This is an inevitable feature of a guidelines-based approach to determining penalties. It may be appropriate to depart from applying the Penalty Guidelines where they do not account for significant circumstances surrounding a violation, which is why we include the flexibility to depart as necessary.").

set forth in the Penalty Guidelines results in Lincoln's penalty being increased twice based on the duration of its fraud. Therefore, I respectfully dissent from this aspect of today's order.

I. Structure of the Penalty Guidelines

In cases that do not involve a natural person, the Commission selects and imposes a civil penalty from a range calculated according to the Penalty Guidelines. The range is the product of two factors: a base penalty and minimum and maximum multipliers that correspond to an entity's culpability score. The double counting in this proceeding occurred in calculating the base penalty, and more particularly, in calculating the violation level that yields the base penalty.[3]

The Penalty Guidelines assign a base violation level to each type of prohibited conduct. They then enumerate adders relevant to the conduct at issue and direct the Commission to increase the base violation level by a prescribed number of points for each adder. Fraud has a base violation level of 6 and in this case can be increased by two adders: (1) a magnitude adder that accounts for the monetary loss caused by the fraud, and (2) a separate adder that accounts for how long the fraud persisted. In this case, Lincoln's fraud cost customers $445,901.21 and persisted for more than 50 days, but less than 250 days. These correspond to a 14 point adder for magnitude and 4 point adder for duration.

Once the adders are applied, the Penalty Guidelines direct the Commission to a table that prescribes the dollar amount associated with each final violation level. This dollar amount is the base penalty applied to the relevant multipliers.

II. The Majority's Application of the Penalty Guidelines Double Counts Duration

In calculating Lincoln's civil penalty, the majority increases the base violation level by both the magnitude and duration adders. While this approach adheres to the letter of the Penalty Guidelines, it has the effect of increasing Lincoln's penalty twice based on the duration of its fraud. As a consequence, the majority's penalty range is three times higher than it would be if duration were not double counted.

In this case, the total monetary loss caused by the fraud is a direct function of how long the fraud persisted. On almost every weekday for seven months Lincoln submitted fraudulent demand response offers for each hour of the Day-Ahead Load Response Program and these offers almost always cleared. The $445,901.21 customers lost as a result of Lincoln's scheme is directly correlated to how long the scheme persisted because customers lost money virtually

[3] The base penalty is the greatest of three variables: (1) the pecuniary gain to the entity under investigation; (2) the pecuniary loss caused by the alleged violation; or (3) the dollar amount corresponding to the entity's violation level. In this case, the greatest amount is the cumulative dollar amount corresponding to Lincoln's violation level.

every weekday for seven months. Had Lincoln's fraud occurred over a shorter period of time, the loss to customers—and the magnitude adder required by the Penalty Guidelines—would have been diminished accordingly.

I agree that Lincoln's civil penalty should reflect the magnitude of its fraud. My objection is that the majority increases the base violation level a second time to account for the fraud's duration without recognizing that, in this case, the magnitude adder already reflects duration. While applying a separate duration adder may be appropriate in some circumstances, I do not believe that it is appropriate here because it does not capture the impact of Lincoln's fraud in a way not already captured by the Penalty Guidelines.

Because the Guidelines have a logarithmic structure, the adders applied to the initial base violation level can have a significant effect on the size of the base penalty, and by extension, on the parameters of the penalty range and final civil penalty. Lincoln's violation level with both the magnitude and duration adders is 24, which corresponds to a base penalty of $2,100,000. When this base penalty is multiplied by the applicable minimum and maximum multipliers,[4] the result is a penalty range of $3,360,000 to $6,720,000. The $5,000,000 civil penalty assessed by the majority is within this range. In contrast, Lincoln's violation level without the duration adder is 20. This corresponds to a base penalty of $650,000 and a penalty range of $1,040,000 to $2,080,000.

III. <u>The Commission May Use Discretion to Depart From the Penalty Guidelines</u>

By its own terms, the policy statement promulgating the Penalty Guidelines does not purport to limit or displace the Commission's inherent enforcement discretion.[5] Instead, it specifically affirms the Commission's freedom to follow or depart from the Guidelines.[6] Additionally, unlike a rulemaking, a policy statement requires the Commission to justify its use with each application.[7] When the Commission cannot explain why it is appropriate to strictly adhere to the Penalty Guidelines, it cannot rely on them.

The majority has not justified relying on the Penalty Guidelines to increase Lincoln's base level penalty by both the magnitude and duration adders. Therefore, I would have applied

[4] The applicable multipliers are 1.6 and 3.2. *See Lincoln Paper and Tissue, LLC*, 144 FERC ¶ 61,162 at P 76 (2013).

[5] Penalty Guidelines, 132 FERC ¶ 61,216 at P 32 ("As we emphasize throughout the Revised Policy Statement, our decision to adopt a guidelines-based approach does not restrict the discretion that we have always exercised and will continue to exercise in order to make an individualized assessment based on the facts presented in a given case.").

[6] *Id*. P 31 ("The Commission can also depart from the Penalty Guidelines in the absence of a staff recommendation or contrary to staff's recommendation."); *supra* n. 2.

[7] *See supra* n. 1.

the Guidelines without the duration adder and assessed a civil penalty of $2,080,000, the top of the resulting range.

IV. Conclusion

While I voted for the Penalty Guidelines and support their continued use, I expect there are issues in their application that will come to light only with experience. I believe we have encountered such an issue in this case. For the reasons discussed above, the Commission should have exercised its discretion and applied the Penalty Guidelines without the duration adder.

Accordingly, I respectfully dissent from this aspect of today's order.

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Cheryl A. LaFleur
Commissioner