

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Duke Energy Corporation, Duke Energy)	
Commercial Asset Management, Inc., and)	
Duke Energy Lee II, LLC)	Docket No. EL14-45-000
)	
v.)	
)	
PJM Interconnection, L.L.C. and PJM)	
Settlement, Inc.)	
)	

COMMENTS OF THE INDEPENDENT MARKET MONITOR FOR PJM

Pursuant to Rule 211 of the Commission’s Rules and Regulations,¹ Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor for PJM² (“Market Monitor”), submits these comments responding to the complaint and alternative request for waiver filed by Duke Energy Corporation, et al. (“Duke”) on May 2, 2014 (“May 2nd Filing”). In this proceeding, Duke seeks to shift costs of procuring gas for certain Generation Capacity Resources on January 28, 2014, to PJM customers. Duke is wrong on its interpretation of the indemnification provisions of the tariff, Duke is wrong on its assertions about a PJM directive and Duke is wrong on the bases for its waiver request. Granting the requested relief would be inconsistent with the proper assignment of risks in markets regulated through competition and inconsistent with the obligations assumed by Generation Capacity Resources. Duke is asking that market rules be waived because they had large negative consequences for Duke on one specific day. But such a waiver would

¹ 18 CFR § 385.211 (2011).

² Capitalized terms used herein and not otherwise defined have the meaning used in the PJM Open Access Transmission Tariff (“OATT”).

violate a basic precept of markets and open the door to an unlimited set of such requests. PJM customers are not, and should not be, a source of funds to offset market risks for suppliers. Accordingly, the May 2nd Filing should be dismissed, the complaint should be denied and the alternative request for waivers should be denied.

I. COMMENTS

A. Background

PJM operates a wholesale power market in which competition results in compensation to suppliers and payments by loads. FERC's decision to use competition in order to produce just and reasonable results meant that compensation would be left to the market, operating consistent with a set of rules defined in the tariff, rather than to regulatory decisions about individual unit's required returns or the specific costs of fuel.³ Since the inception of full market-based LMP markets in PJM on April 1, 1999, energy market and capacity market prices have been high and energy market and capacity market prices have been low. Suppliers have been aggrieved at times and load has been aggrieved at times.

In markets, generation suppliers assume sole responsibility for the risks and rewards of owning and operating generating units and all the decisions that come with owning and operating generating units. When costs decrease, suppliers' profits increase and when costs increase, suppliers' profits decrease. PJM market rules assign risks to those best situated to manage them. Suppliers are best situated to manage risks associated with the availability of resources to meet market and reliability obligations. Suppliers are best situated to manage

³ See, e.g., *Regional Transmission Organizations*, Order No. 2000, FERC Stats. & Regs. ¶ 31,089 (1999), , 89 FERC ¶ 61,285 (1999) (The Commission determined that competition is the best way to protect the public interest and ensure that electricity customers pay the lowest price possible.); *order on reh'g*, Order No. 2000-A, FERC Stats. & Regs. ¶ 31,092 (2000), *aff'd sub nom. Pub. Util. Dist. No. 1 of Snohomish County, Washington v. FERC*, 272 F.3d 607 (D.C. Cir. 2001).

energy and fuel price risks. Suppliers receive the benefits when the results are favorable; suppliers must accept the consequences when the results are unfavorable.

Duke owns the Lee Energy Facility.⁴ The Lee Energy Facility consists of eight 80-MW natural gas-fired, combustion turbines (the “Lee Units”), located in Lee County, Illinois, about 90 miles west of Chicago.⁵

Duke purchases gas from Natural Gas Pipeline Company of America, LLC (“NGPL”) for the Lee Units, subject to terms and conditions to which Duke and NGPL agreed and to NGPL’s Commission-regulated tariff.⁶ The Lee Units cannot run unless they receive natural gas from NGPL.

The issue in this case arises entirely from Duke’s decision to rely solely on the gas pipeline for fuel, from Duke’s decision about the type of gas supply to purchase, and from the inflexible operational requirements of the gas pipeline as defined in NGPL’s tariff. More than half of Duke’s claimed losses in this case are the direct result of Duke’s decision not to buy gas a few hours earlier. The issue in this case is not a result of PJM market rules. Duke made an economic decision to rely solely on interruptible service from NGPL as defined in the NGPL tariff. In its filing, Duke did not discuss any other options it may have had to fuel the Lee Units, including investing in back up fuel capability or purchasing firming gas products, but which it decided, for economic reasons, not to pursue. But Duke did make such economic decisions as part of its choices about how to participate in markets. It is inappropriate for Duke to ask PJM customers to hold it harmless from such decisions, from which Duke has benefitted. It is also unfair to Duke’s competitors, who may have made different choices about fuel supply.

⁴ May 2nd Complaint at 9.

⁵ *Id.* at 10.

⁶ May 2nd Complaint at 13–15 & n.32, Exhibit D-4 (Affidavit of Shannon R. Gronefeld) at P 10; Exhibit D-5 (Duke/NGPL Balancing Service Agreement).

The Lee Units are Generation Capacity Resources for the 2013/2014 Delivery Year, which runs from June 1, 2013 through May 30, 2014. As a result, the Lee Units are required to offer in the PJM Day-Ahead Energy Market every day and the Lee Units have an obligation to provide energy whenever it is needed for the duration of the Delivery Year.⁷ Duke manages all aspects of ensuring the Lee Units are ready to run, including procuring the necessary fuel. In managing fuel procurement risk, Duke may make money or lose money relative to expected costs. If Duke enjoys gains as a result of successful fuel cost management, it does not share the gains with PJM customers. If Duke suffers losses from fuel cost management, Duke does not share the losses with PJM customers. There is nothing in the facts of this case that supports a different approach. Duke should not be allowed to share its losses with PJM customers.

Generation Capacity Resources are required to be available at their rated capacity value unless on an approved scheduled outage or a forced outage.⁸ No scheduled or forced outage applied to the Lee Units on January 28th. Gas was available to the Lee Units for purchase by Duke for operating on January 28th, and Duke did purchase gas for the five units scheduled by PJM in the Day-Ahead Energy Market.⁹ Duke did the right thing in purchasing gas and, with respect to the five Lee Units at issue, acted consistent with its capacity obligations.

Energy offers are comprised of three components, start, incremental energy and no load.¹⁰ Gas costs that are incurred in the process of starting a unit may be included in the

⁷ See, e.g., OATT Attachment DD § 8.1; PJM Operating Agreement Schedule 1 § 1.10.1A(d).

⁸ See OATT Attachment DD § 8.1; PJM Reliability Assurance Agreement § 9.1(c).

⁹ May 2nd Complaint, Exhibit No. D-10 (Gas Invoices).

¹⁰ See PJM Operating Agreement Schedule 1 § 1.10.1A(d).

start component.¹¹ Daily cost-based offers include the actual incremental costs for each component, including the incremental cost of fuel. Daily price-based offers may include the cost-based start costs and the cost-based no load costs plus an incremental offer selected by the seller.¹² But if the seller does not elect to use cost-based start and no load components as part of its price-based offer, the seller must define the level of start and no load components twice a year and cannot change them during the following six month period for its price-based offer. These rules were introduced in order to limit the exercise of market power and prevent market manipulation by sellers in extreme market conditions.¹³

For the six-month period at issue here, October 1, 2013 through March 31, 2014, Duke elected to set the Lee Units' start up component of the price-based offers at \$1,200.¹⁴ Duke elected not to set its start component based on costs. Regardless, actual cost-based start costs on January 28 were not substantially larger than the price-based start costs. The selection of price-based start costs did not have a material impact on Duke's losses.

There is no reasonable interpretation of the rules defining start costs which would include the costs of gas required to operate a unit and generate power. Those costs belong in the incremental offers and in the no load offers, following the rules for each, and are recoverable only if a unit operates subject to specific rules.

On January 27, 2014 at 8:45 AM, PJM issued a Maximum Generation Alert for January 28th.¹⁵ The cost of gas to run the Lee Units for January 28th was expected to be \$37

¹¹ For cost-based start offers, this means the cost of gas incurred in the process of bringing the unit on-line. *See* PJM Manual 15 (Cost Development Guidelines) § 2.4.1 at 12.

¹² *See* PJM Operating Agreement Schedule 1 § 1.10.1A.

¹³ *See* PJM Operating Agreement Schedule 1 § 1.9.7(b).

¹⁴ May 2nd Complaint at 40, 44. Duke does not explain its rationale for selecting the \$1,200 value. Duke does state (at 44) that the amount "was not developed with the NGPL restrictions in mind."

¹⁵ May 2nd Complaint at 6.

per MMBtu.¹⁶ Duke's analysis indicated to Duke that the Lee Units would not run profitably on January 28, 2014 ("January 28th").¹⁷ As a result, on January 27 between 8:53 AM and 8:56 AM, Duke decided not to purchase gas at the available price of \$37 per MMBtu for January 28th, despite the fact that PJM had informed Duke that PJM would be calling maximum emergency generation into capacity on January 28th.¹⁸

At 8:56 AM, PJM informed Duke that they would "advise you to secure gas for your units" as they were expecting to dispatch the Lee Units on the following day.¹⁹ When Duke stated that it may secure gas for some of the Lee Units, PJM clarified that it wanted "all units available for tomorrow."²⁰ PJM informed Duke that the decision about whether to purchase gas was not an economic decision.²¹ A PJM dispatcher stated: "This is a reliability issue, so all units must be available."²²

In a call with PJM, PJM informed Duke that PJM was not aware of any tariff provisions that would permit Duke to be made whole for gas costs.²³

At some time prior to the noon offer deadline for the Day-Ahead Energy Market Duke purchased gas sufficient for five of the eight Lee Units.²⁴ These five units cleared in

¹⁶ May 2nd Complaint at 4.

¹⁷ May 2nd Complaint at 4-5.

¹⁸ May 2nd Complaint, Exhibit No. D-1 (Affidavit of Gregory H. Cecil) ("Cecil Affidavit") at para. 20.

¹⁹ May 2nd Complaint, Exhibit No. D-2.

²⁰ *Id.* at 3.

²¹ *Id.* at 4.

²² *Id.*

²³ *Id.*, Cecil Affidavit at para. 25.

²⁴ *Id.*, Cecil Affidavit at para. 26.

the Day-Ahead Energy Market for hours ending 0800 through 1200 and hours ending 1900 through 2100, a total of eight hours.²⁵

On January 28th, PJM did not call the Lee Units to operate in the real time market. Duke took various measures to mitigate its losses on the gas purchased, including self-scheduling two of these five Lee Units on January 28th and selling gas. Duke states that it lost \$9,843,621 as a result of purchasing gas to run on January 28th.²⁶

Even if PJM had called the five Lee Units that cleared the Day-Ahead Energy Market in the Real-Time Energy Market to run for the hours that they cleared, the Lee Units would have been paid the Day-Ahead Market clearing price and Duke would still have lost money on its gas purchases as a result of the gas pipeline's restrictive tariff provisions. It was not PJM's actions in not calling the units in real time that caused Duke to lose money on its gas position. Duke was paid the Day-Ahead Market price and in addition made money from buying out of their position in real time at the lower Real-Time Market prices. Duke self-scheduled two of the five units and was thus not eligible for uplift payments. But, regardless of self-scheduling, Duke was not eligible for uplift payments (balancing operating reserve payments) as a result of not being scheduled in real time, because Real-Time Energy Market prices were lower the Day-Ahead Energy Market prices and lower than the Lee Unit offers.

In summary, PJM did not direct Duke to purchase gas on January 27. Duke initiated a call on January 27 to determine if Duke really needed to follow its tariff obligations as a Generation Capacity Resource.²⁷ In effect, Duke was attempting to get PJM to commit to more certainty than PJM is ever in a position to provide. In response, PJM simply reminded Duke of its obligations as a capacity resource, advised Duke of emergency conditions on the

²⁵ *Id.*, Cecil Affidavit at para. 27.

²⁶ *Id.*, Cecil Affidavit at paras. 38-43.

²⁷ May 2nd Complaint, Cecil Affidavit at para. 20.

grid and advised Duke of PJM's concerns about reliability. Despite that information, Duke initially chose not to purchase gas at \$37 per MMBtu to support its required offers in the Day-Ahead Energy Market. PJM even felt the responsibility to call Duke back to reiterate its statements.²⁸ PJM's statements to Duke were consistent with PJM's responsibilities as an RTO and did not constitute a directive to purchase gas.

According to Duke's argument, PJM's emergency procedures constitute a directive to generators, and following such a directive means that generators are entitled to indemnification under Section 10.3. Under this interpretation, no generator would ever be responsible for its costs in a PJM emergency. Accepting this argument would unjustifiably and unreasonably impose a major shift of cost responsibility to PJM customers from PJM suppliers. Owners of generating units have not used this provision to shift costs in this manner, and they should not be permitted to do so now.

B. PJM Transmission Customers Are Not Responsible for Fuel Procurement for the Lee Units.

The sole basis for recovery under the PJM tariff cited by Duke is Section 10.3 of the OATT. Section 10.3 provides that the Transmission Customer must indemnify Generation Owners "acting in good faith to implement or comply with the directives of the Transmission Provider."²⁹ Duke has not shown that Section 10.3 applies to directives that

²⁸ May 2nd Complaint, Cecil Affidavit at para. 23.

²⁹ Section 10.3 of the OATT reads in its entirety:

The Transmission Customer shall at all times indemnify, defend, and save each Transmission Owner, the Transmission Provider, PJMSettlement, and each Generation Owner acting in good faith to implement or comply with the directives of the Transmission Provider, and their directors, managers, members, shareholders, officers and employees harmless from, any and all damages, losses, claims, including claims and actions relating to injury to or death of any person or damage to property, demands, suits, recoveries, costs and expenses, court costs, attorney fees, and all other obligations by or to third parties, arising out of or resulting from the Transmission Provider's, PJMSettlement's, a

relate to the operation of the markets, i.e. the rules for the PJM Interchange Energy Market, as opposed to open-access transmission service. Duke has not shown that PJM issued a directive or that Duke complied with one. Indemnification from “the Transmission Customer” is only available for Generation Owners following PJM “directives,” under the Tariff, which is defined as the “PJM Open-Access Transmission Tariff” (OATT).³⁰ Duke cites to provisions of Schedule 1 to the PJM Operating Agreement, not the OATT, for examples of “directives” that it followed.³¹

If a “directive” means an advisory statement, a request, or a call for another party to honor their obligations, then the Transmission Customer would be required to indemnify all costs Generation Owners incur (in good faith, and in the absence of negligence or intentional wrongdoing) in the course of responding to any and all PJM emergency instructions and advisories, including for example, Maximum Emergency Generation Alerts. This would be an absurd result, and it would be only one of many absurd results. It would be fundamentally unreasonable and unjust to interpret Section 10.3 to impose on the Transmission Customer the costs incurred by Generation Owners to comply with every PJM request or advised course of action. The Market Monitor is not aware that PJM has ever applied Section 10.3 to indemnify costs that were incurred for compliance with directives that the recipient has the discretion to ignore. No provision of the tariff allows

Transmission Owner’s, or a Generation Owner’s (acting in good faith to implement or comply with the directives of the Transmission Provider) performance of its obligations under this Tariff on behalf of the Transmission Customer, except in cases of negligence or intentional wrongdoing by such Transmission Owner, the Transmission Provider, or such Generation Owner acting in good faith to implement or comply with the directives of the Transmission Provider.

³⁰ OATT § 1.43A.

³¹ The various provisions for which Duke seeks waiver are also provisions of Schedule 1 to the PJM Operating Agreement.

PJM to issue “directives” as contemplated under Section 10.3 that concern fuel procurement.

PJM has specific rules in place to ensure that units do not run at a loss when PJM requests that they run. These operating reserve or uplift rules do not permit payments of the type requested by Duke.

PJM does not issue directives related to fuel procurement. PJM instead obtains commitments from Capacity Resources in return for being paid the Capacity Market clearing price to provide energy from their units when it is needed for the duration of each Delivery Year. Generation Capacity Resources must procure fuel as needed in order to be able to provide energy every day that it is needed. The owners of Generation Capacity Resources have the responsibility to ensure that they are ready and available. In addition to this basic obligation, the rules include performance incentives designed to encourage availability.

According to the facts of this case as presented by Duke, Duke took the steps that it decided were needed for the Lee Units to be ready on January 28th. Duke did not do what PJM advised. Duke procured gas for only five of the eight Lee Units. Duke did not purchase gas for the other three units despite PJM’s statements. Duke delayed buying gas for several hours after PJM issued its Maximum Emergency Generation Alert and despite the fact that extreme cold weather was expected, during which time the price of gas nearly doubled.

1. Duke Has Not Shown That Its Claim Is Consistent with the Design and Purpose of Section 10.3.

Duke has not demonstrated that it has invoked Section 10.3 for purposes consistent with its design and purpose.

Duke asks for relief that, if granted, could significantly alter risk and cost responsibilities of participants in PJM markets. The Market Monitor is not aware that Generation Owners have ever sought or received an indemnity under this provision. Granting Duke the relief that it requests would set a precedent for exploitation of this provision for purposes for which it was never intended.

Section 10.3 derives from the Pro Forma Tariff, which concerns open-access transmission service.³² Section 10.3 is limited to the performance of obligations under the Tariff, which is defined as the OATT.³³ PJM operates markets that are not covered under the Pro Forma Tariff, and Duke cites to the operation of those market rules to assert that it is entitled to relief.³⁴ Duke has not shown that the rules to which it cites are related to open-access transmission service and therefore cannot justify relief under Section 10.3.

Section 10.3 identifies the party responsible for indemnification as “[t]he Transmission Customer.” Section 10.3 contemplates claims that involve a specific Transmission Customer. Duke has not explained why a particular “Transmission Customer” or even Transmission Customers collectively should be responsible for the costs of purchasing gas to run the Lee Units on January 28th. The purchase of gas relates to the obligations of capacity resources as part of resource adequacy, for which Load-Serving Entities (LSEs) are expected to pay when they are charged for PJM’s costs of procuring capacity. Contrary to Duke’s characterization of “PJM load” and Transmission Customers as the same thing (at 27), these are different categories whose members, individually and collectively, have different relationships to PJM. One example is resource adequacy. The PJM market rules specifically assign responsibility for resource adequacy to LSEs.³⁵ Costs

³² Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, FERC Stats. & Regs. ¶ 31,036 (1996), Appendix D (Pro Forma Tariff § 10.2), order on reh’g, Order No. 888-A, FERC Stats. & Regs. ¶ 31,048, order on reh’g, Order No. 888-B, 81 FERC ¶ 61,248 (1997), order on reh’g, Order No. 888-C, 82 FERC ¶ 61,046 (1998), aff’d in relevant part sub nom. Transmission Access Policy Study Group v. FERC, 225 F.3d 667 (D.C. Cir. 2000), aff’d sub nom. New York v. FERC, 535 U.S. 1 (2002).

³³ See OATT § 1.43A.

³⁴ May 2nd Complaint at 32–33, citing PJM Operating Agreement § 1.10, Schedule 1 §§ 1.8.2(a), 1.7.4(f) and 1.7.11. Likewise, the provisions for which Duke requests waiver are all market rules unrelated to the Pro Forma Tariff, §§ 1.9.7(b)(i), 1.10.2(d) and 1.10.4(c).

³⁵ See PJM Reliability Assurance Agreement Among Load Serving Entities in the PJM Region.

associated with resource adequacy are not assigned properly to the Transmission Customer.

Duke has the burden to explain how Section 10.3 applies to its circumstances and why it is appropriate that the Transmission Customer indemnify it for the cost of gas purchased in order to be ready to run. Duke has not met its burden, and the Transmission Customer should not be required to pay an indemnity.

2. Indemnification Under Section 10.3 Does Not Concern Actions Taken in Response to PJM Directions Related to Fuel Procurement.

Section 10.3 concerns actions taken in response to PJM directives. The tariff does not provide, and PJM does not need, the authority to issue directives to Generation Owners to ensure that Capacity Resources are available to provide energy when needed. PJM procures capacity in advance, and relies on Capacity Resources selected in RPM Auctions and included FRR Capacity Plans to ensure resource adequacy.

Duke cites to “PJM Tariff Section 1.8.2(a)” as an example of a provision authorizing PJM to issue directives. Section 1.8.2(a) of the PJM Operating Agreement provides: “Market Participants shall comply with all determinations of the Office of the Interconnection on the selection, scheduling or dispatch of resources in the PJM Interchange Energy Market, or to meet the operational requirements of the PJM Region.” Section 1.8.2(a) of the OA does not authorize PJM to issue “directives” contemplated under Section 10.3 of the OATT. This provision does not authorize PJM to issue a directive that a Generation Owner purchase gas or make other fuel arrangements.

This provision is not relevant to Duke’s claim for an indemnity under Section 10.3. Section 10.3 applies to the “performance of obligations under the Tariff,” which is defined specifically to mean the OATT. Section 1.8.2 is a provision of Schedule I of the PJM Operating Agreement, not the Tariff.

The OATT includes a parallel cite to Section 1.8.2 in Attachment K–Appendix to the OATT. Duke apparently meant to cite to that provision because Duke could not cite to a provision of Schedule 1 that is plainly outside of the scope of Section 10.3. But such a cite

would have not affected the point. Attachment K–Appendix is not part of the OATT and subject to Section 10.3. Attachment K–Appendix explains its purpose: “The provisions of the Appendix incorporate into the Tariff for ease of reference the provisions of Schedule 1 of the Operating Agreement.” The inclusion of market rule provisions within the OATT, for convenience, is not a sufficient basis for inclusion of the market rules within the scope of the indemnity provided under Section 10.3 of the OATT. Extending the coverage of Section 10.3 is a highly significant expansion of the scope of that provision, and Duke has not shown or asserted that such an expansion is valid.

Duke also cites to Section 1.7.4(f) of the PJM Tariff, Attachment K–Appendix, which states:

Each Market Participant shall operate, or shall cause to be operated, any generating resources owned or controlled by such Market Participant that are within the PJM Region or otherwise supplying energy to or through the PJM Region in a manner that is consistent with the standards, requirements or directions of the Office of the Interconnection and that will permit the Office of the Interconnection to perform its obligations under this Agreement; provided, however, no Market Participant shall be required to take any action that is inconsistent with Good Utility Practice or applicable law.

Section 1.7.4(f) does not explicitly authorize PJM to issue “directives” contemplated under Section 10.3. This provision does not authorize PJM to issue a directive that a Generation Owner purchase gas or make other fuel arrangements. This provision is not relevant to Duke’s claim for an indemnity under Section 10.3, because it is not a provision of the Tariff, but rather language included for convenience.

3. Generation Capacity Resources Such As the Lee Units Have an Obligation to Provide Energy When Needed.

Generation Capacity Resources such as the Lee Units have an obligation to provide energy when it is needed. PJM does not issue directives in order to ensure that Capacity Resources are available because Generation Resources are obligated to be ready to provide energy whenever it is needed. On January 27, 2014, PJM issued a Maximum Emergency

Generation Alert. PJM market rules explain, “The intent of the alerts is to keep all affected system personnel aware of the forecast and/or actual status of the PJM RTO... Alerts are issued in advance of a scheduled load period to allow sufficient time for members to prepare for anticipated initial capacity shortages.”³⁶

After PJM issued a Maximum Emergency Generation Alert to the members, Duke initiated direct individual contact with PJM dispatch.³⁷ Duke wanted to know whether PJM would call the Lee Units because Duke is the one responsible for providing energy from its units when it is needed.³⁸ PJM could not say whether it would call the Lee Units; the essence of its response was “be ready,” which is consistent with the intent of the alert.³⁹

Communications between PJM dispatchers and resource owners, such as those that occurred between PJM dispatchers and Duke on January 27, 2014, are a reminder of the obligations of resource owners and an indication of PJM’s expectations about system conditions. Such communications are not legally binding directives. Legally binding obligations to be available when needed for energy already apply to the Lee Units and other Generation Capacity Resources. The Lee Units, along with all other capacity resources, were and are already subject to the legally binding terms of the tariff.

All eight of the Lee Units are Generation Capacity Resources for the 2013/2014 Delivery Year. The Lee Units are paid to be ready throughout the year to provide energy when it is needed. The Lee Units have an obligation to provide the service for which they are paid every day.⁴⁰

³⁶ PJM Manual 13 § 2 at 16.

³⁷ May 2nd Complaint at 3–6.

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ *See, e.g.*, OATT Attachment DD § 8.1; PJM Operating Agreement Schedule 1 § 1.10.1A(d).

PJM and PJM customers are entitled to expect that Duke will procure fuel for all of the Lee Units so that they are ready to run when they are called. This leaves decisions about a resource's readiness in the hands of the owner, and the owner is entirely responsible for the attendant risks and rewards.

4. Duke Did Not Believe that PJM Had the Authority to Direct Duke to Purchase Gas.

PJM does not have the authority to order Duke to purchase gas. PJM did not order Duke to purchase gas. PJM did tell Duke that it expected to need the Lee Units on January 28th and reminded Duke that it was obligated to provide energy when it was needed for reliability. Duke did not comply with what PJM advised for three of the Lee Units.

Even if otherwise justified, which it is not, no indemnification is available to Duke under Section 10.3 if Duke was not following PJM's directives, and Duke did not follow what it asserts were PJM directives.

Duke cites to no provision of the tariff that authorizes PJM to direct Duke to procure fuel for the Lee Units. It would fundamentally change PJM's relationship with generation owners if Sections 1.8.2(a) and 1.7.4(f), and similar provisions addressing operational directives issued by PJM, were enforceable directives that also entitled generation owners to compensation for costs incurred in following such directives.

Duke did not follow PJM's advice. Duke's failure to follow the alleged PJM directive provides the best evidence that PJM did not direct Duke to purchase gas, that PJM did not have authority to direct Duke to purchase gas and that Duke did not believe that PJM had the authority to direct it to purchase gas. PJM dispatch advised Duke that "all units must be available" in response to Duke Managing Director Cecil's indication that he could make some units available. Duke did not procure fuel for three of the eight Lee Units, although all eight are Generation Capacity Resources.⁴¹ Duke's behavior directly contradicts its

⁴¹ May 2nd Complaint at 22.

argument on complaint that PJM has the authority to direct Duke to purchase gas and issued a binding directive that it do so.

About \$4.6 million of Duke's asserted losses are attributable to Duke's delay in purchasing the gas that would be needed to be ready. After PJM issued a Maximum Emergency Generation Alert, and after a phone call in which PJM stated "it was 99.9 percent that Lee would run," Duke declined to buy gas at \$37 per MMBtu.⁴² By the time Duke changed its mind, it had to buy at \$63 per MMBtu.⁴³ If Duke really thought PJM was directing it to purchase gas, it should have complied immediately. Immediate compliance would have avoided about \$4.6 million of the claimed loss.

5. Precedent Relied by Duke Does Not Support Its Claim for Relief.

Duke claims (at 35), "The Commission has permitted similar cost recovery in an analogous circumstance," citing *New England Power Pool, Inc. ("NEPOOL")*.⁴⁴ The facts and circumstances in *NEPOOL* are not analogous. On the contrary, there are material differences between the circumstances of the Lee Units on January 28th and the units involved in *NEPOOL*.

In *NEPOOL*, certain units that Exelon had been running for "just over a month" failed to clear the day-ahead market due to the cost of natural gas included in those units' day-ahead offer.⁴⁵ Exelon was preparing to shut the units down when ISO-NE contacted Exelon and requested Exelon to continue running the units.⁴⁶ Exelon bought the fuel

⁴² *Id.*, Cecil Affidavit at paras. 19–21.

⁴³ *Id.*, Cecil Affidavit at para. 26.

⁴⁴ 107 FERC ¶ 61,183, *order on reh'g*, 108 FERC ¶ 61,207 (2004).

⁴⁵ *Id.* at P 3.

⁴⁶ *Id.*

required and continued to operate the units at ISO New England's direction.⁴⁷ Exelon was found ineligible for a make-whole payment only because over a month ago it had commenced operating the units based on self schedules.⁴⁸ It was widely agreed that the tariff failed to anticipate and account for circumstances where units that started based on self schedules end up running for a prolonged period. New England stakeholders identified the problem in the rules and voted to modify the applicable rules going forward.⁴⁹

Under the same facts applied to the PJM market rules, the Exelon units would have received make-whole payments, and proceedings for cost recovery and rule changes would not have been necessary.⁵⁰

There are also material differences between Section 10.3 of the OATT and the rule relied upon by ISO New England, Section 7.5(g) of the Restated NEPOOL Agreement.⁵¹ Section 10.3 provides for indemnification from the Transmission Customer to a Generation

⁴⁷ *Id.*

⁴⁸ *Id.* at P 4 (“...ISO-NE referenced section 2.1 of Market Rule 1, Appendix F, and NEPOOL Manual M-28, which provides that generation resources with Self-Scheduled hours during the minimum run time of their real-time commitment period (periods of continuous operation bounded by a start up and the earlier to occur of a shut down or unit trip) are not eligible to receive Operating Reserve payments.”)

⁴⁹ *Id.* at PP 5–6, 15.

⁵⁰ *See* PJM Operating Agreement Schedule 1 § 3.2.3 (All pool-scheduled resources are eligible to receive make whole payments (day-ahead or balancing operating reserve credits) if they follow the dispatch instructions. Self-scheduled resources are not eligible for operating reserve credits, but when a self-scheduled resource is instructed by the RTO to remain online it effectively becomes a pool-schedule resource.).

⁵¹ *See* NEPOOL at P 6 (Section 7.5(g) of the Restated NEPOOL Agreement states: “The Participants Committee shall have the duty and requisite authority to provide for the sharing by Participants, on such basis as the Participants Committee may deem appropriate, of payments and costs which are not otherwise reimbursed under this Agreement and which are incurred by Participants or under arrangements with Non-participants and approved or authorized by the Committee as necessary to meet or avoid short term deficiencies in the amount of resources available to meet the Pool’s reliability objectives.”).

Owner following PJM directives and who are otherwise eligible. In contrast Section 7.5(g) does not afford relief directly. Section 7.5(g) instead allows ISO New England's Participants Committee to vote to approve cost sharing and establish an ad hoc basis for such sharing among Participants the reimbursement of costs "to meet or avoid short term deficiencies in the amount of resources available to meet the Pool's reliability objectives."⁵² Section 7.5(g) provides for what is effectively a change to the otherwise applicable rules, with stakeholder support, for costs associated with resource adequacy, with no requirement that ISO New England issue a directive. In contrast, Section 10.3 concerns indemnification in specified circumstances, without regard to stakeholder support.

Unlike the Exelon units, the Lee Units cleared the day-ahead market. Unlike ISO New England's rules effective at the time, the PJM market rules allow make-whole payments under the circumstances. Unlike Exelon, Duke's units had an annual capacity commitment covering the relevant period. Unlike Exelon, stakeholders have not voted to grant Duke the requested relief. For these reasons, *NEPOOL* precedent does not support Duke's claim for relief. In contrast, *NEPOOL* exposes the deficiencies of the May 2nd Complaint.

C. The Standards to Grant a Waiver Request Are Not Met.

In the alternative, Duke seeks a waiver of the PJM market rules so that it can obtain payment for losses on its gas purchases on January 28th. Duke states the applicable standard for evaluating a waiver request: "(1) the waiver must be limited in scope; (2) the applicant must establish a concrete problem needing to be remedied; and (3) the waiver must have no unintended consequences, such as harm to third parties."⁵³ The request for waiver fails under each element of the applicable standard.

⁵² *Id.*

⁵³ May 2nd Complaint at 41, citing *PJM Interconnection, L.L.C.*, 146 FERC ¶ 61,078 at P 38 (2014); *New York Independent System Operator, Inc.*, 146 FERC ¶ 61,061 (2014). The standard is also set for in

Regardless, Duke would like PJM customers to pay it for gas it purchased but did not burn to serve them. The various provisions suggested for waiver are all in place for good reasons and waiving the rules for Duke would open the floodgates for others to ask for waivers when market decisions have negative consequences.

1. The Request Is Not Limited in Scope.

Duke's requested waiver is not limited in scope. Duke's request for waiver does not identify a discrete rule and request waiver of that rule and does not provide reasons why the rules should not apply in its particular circumstances. Duke really seeks waiver of whatever provisions prevent it from receiving a make-whole payment. There are many such provisions. They are all in place for good reasons. Provisions for make-whole payments appropriately limit when make-whole payments are appropriate, and they do not apply to Duke's circumstances. A waiver is not limited in scope when granting it requires broad revisions of the PJM market rules and incorporates significant changes to those market rules, as would Duke's request.

Market Participants must manage their risks all of the time. There is nothing extraordinary about continuing to assign to Duke responsibility for managing its risks under the circumstances on January 28th. Peak days are not the norm, but they are expected to happen, and participants are expected to manage the risks when they happen. Market rules are not waived during cold weather or hot weather. Many other resource owners also had to manage risks on January 28th in decisions made on or just before January 28th and in decisions made long before January 28th. Some did so more successfully than others. PJM customers are not required to shoulder the consequences of unsuccessful risk management. PJM customers do not receive the benefits when risks are successfully managed.

Indicated CAISO Suppliers, 146 FERC ¶ 61,183 at P 20 (2014) (Waiver of market rules to permit make-whole payments for gas purchase related losses denied because the request was not limited in scope.).

Duke specifies the provisions that require waiver to grant the requested relief, including Sections 1.9.7(b)(i) and 1.10.2(d), which limit recovery of “start-up costs,” “to an *ex ante* figure that was a previously-submitted amount (in this case \$1,200 – a tiny fraction of the actual costs given the market conditions and pipeline restrictions on the day in question) [emphasis in the original]”; and Section 1.10.4(c), which prohibits “self-scheduled resources seeking to recover start-up fees.” Duke’s gas costs are not start costs under any possible interpretation of market rules or of the way units operate. All of these market rules are in place for sound reasons. The rules are designed to incent market participants to manage their risks well, to prevent the exercise of market power and manipulation and to provide make-whole payments when it is appropriate to provide them.

a. The Commission Has Rejected Waivers in Similar Circumstances Where Suppliers Requested Significant Changes to Market Rules in Order to Create Eligibility for Make-Whole Payments.

The Commission recently rejected a waiver in similar circumstances because the requested waiver was not limited in scope. On March 14, 2014, the Commission denied a request for waiver of the market rules of the California Independent System Operator, Inc. (“CAISO) from certain market suppliers who sought an order that would require CAISO to “reimburse generators for the cost of natural gas procured in response to CAISO dispatch directives,” including “the cost of disposing of natural gas when CAISO later elects not to dispatch units for which natural gas was procured.”⁵⁴ The Commission found that the request was “overly broad in scope and did not meet the Commission’s requirements for a tariff waiver.” Consistent with this precedent, Duke’s request for waiver of PJM market rules should also be denied.

The Commission found (at P 22): “Specifically, Suppliers’ request does not identify specific provisions of the CAISO tariff for which they seek waiver. Rather, Suppliers’

⁵⁴ 146 FERC ¶ 61,183 at P 1.

waiver request seeks broad revisions of the CAISO tariff that appears to incorporate significant changes to the CAISO current market rules.” Duke corrects the technical oversight by specifying various provisions that prevent it from receiving a make-whole payment, but in so doing, confirms the Commission’s substantive concern that granting the requested relief would require a broad change to the applicable market rules, not just discrete change to a stand-alone provision.

b. The Market Consequences of Duke’s Decisions About the Basis for Start Up Offers Appropriately Belong with Duke.

One provision that Duke requests be waived is Section 1.9.7(b) of the PJM Operating Agreement. Section 1.9.7(b) requires that participants elect whether to use a cost-based or price-based calculation for start costs for specified six month periods.⁵⁵ Duke elected price-based start costs for the Lee Units, and those units were capped at the elected level on January 28th.

Duke explains:

Duke elected to use a market-based (or price-based) start-up cost for the relevant six-month period (October 1 through March 31), and so was required to use the pre-determined number of \$1,200, rather than its actual start-up costs in this particular instance of approximately \$9.8 million (net). But this \$1,200 amount was not developed with the NGPL restrictions in mind.

⁵⁵ Section 1.9.7(b) of the PJM Operating Agreement provides: “Market Sellers authorized to request market-based start-up and no-load fees may choose to submit such fees on either a market or a cost basis. Market Sellers must elect to submit both start-up and no-load fees on either a market basis or a cost basis and any such election shall be submitted on or before March 31 for the period of April 1 through September 30, and on or before September 30 for the period October 1 through March 31. The election of market-based or cost-based start-up and no-load fees shall remain in effect without change throughout the applicable periods.” Section 1.9.7(b)(i) provides further: “The Office of the Interconnection shall reject any request for start-up and no-load fees in a Market Seller’s Offer Data that does not conform to the Market Seller’s specification on file with the Office of the Interconnection.”

PJM market rules to protect against market power and manipulation require participants to elect price- based or cost-based start cost offers for six-month periods.⁵⁶ By electing to use a pre-determined number, \$1,200, Duke chose not to include current gas costs in the start and no load components of its offer. Duke could have elected a cost-based start offer component. But even if they had, Duke could have included only those gas costs associated with actually starting the unit in its cost-based start costs. Such cost-based start costs would have been greater than Duke's price-based start costs by only a small amount. As a result, this issue is an insignificant part of why Duke lost money on its gas purchases.

Duke's cost-based start costs could not have included the asserted \$9.8 million of gas costs because there were costs incurred to operate the unit and generate energy and do not meet the definition of start costs.

The request to receive \$9.8 million is not actually a request for a waiver of the start cost rule, but is a request for a new rule allowing generation owners to charge customers for all fuel costs purchased in anticipation of operating. This would constitute a dramatic change in market rules and an associated, inappropriate shift in the costs and risks of the market to customers.

c. Start Up Costs Are the Costs Actually Incurred In Order to Start a Unit.

Another provision that Duke requests be waived is Section 1.10.2(d) of the PJM Operating Agreement. Section 1.10.2(d) caps make-whole payments for start and no load based on the "actual costs incurred" to a cost-based cap on start up costs. Duke seeks to waive the provision to include \$9,843,621 of uncovered gas costs on January 28th. It is appropriate to cap start costs at the actual cost of starting a unit. A cap is needed to prevent the exercise of market power and manipulation.

⁵⁶ PJM Operating Agreement Schedule 1 § 1.10.1A(d).

Duke's actual gas costs associated with actually starting the unit would have been greater than Duke's price-based start costs by only a small amount. As a result, this issue is an insignificant part of why Duke lost money on its gas purchases.

Duke's cost-based start costs could not have included the asserted \$9.8 million of gas costs because there were costs incurred to operate the unit and generate energy and do not meet the definition of start costs.

The request to receive \$9.8 million is not actually a request for a waiver of the start cost rule, but is a request for a new rule allowing generation owners to charge customers for all fuel costs purchased in anticipation of operating. This would constitute a dramatic change in market rules and an associated, inappropriate shift in the costs and risks of the market to customers.

d. The Market Consequences for Duke's Self Scheduling Appropriately Belong with Duke.

Another provision that Duke requests be waived is Section 1.10.4(c) of Schedule 1 to the PJM Operating Agreement. Section 1.10.4(c) provides that "[a] resource that has been self-scheduled shall not receive payments or credits for start-up or no-load fees." Duke self-scheduled two of the Lee Units in real-time.⁵⁷

PJM did not dispatch the Lee Units in real time. The PJM market rules allow resources to self-schedule.⁵⁸ Duke determined that self scheduling the Lee Units would mitigate Duke's losses. The rules governing uplift payments do not permit uplift payments when units are self scheduled, with the exception of lost opportunity cost credits. Duke has not provided any reason why such rules should be waived. Duke chose to self schedule and it is appropriate that Duke bear both the risks and rewards of that choice.

⁵⁷ May 2nd Complaint at 45.

⁵⁸ See PJM Operating Agreement Schedule 1 § 1.10.3.

Duke's decision to self schedule did not affect uplift payments. The Lee Units would not have been eligible for uplift payments (balancing operating reserves) even if they had not self scheduled. There is nothing in the uplift rules that would support the payment of the claimed \$9.8 million to Duke.

2. The Request Does Not Establish a Concrete Problem with the PJM Market Rules That Needs to Be Remedied.

Duke has not identified a concrete problem with the PJM market rules for which it seeks waiver. Each of the provisions that Duke seeks to change operates as it is intended to operate, and no changes to provisions are needed. No changes to these rules have been proposed.

Duke has identified some issues that Duke needs to address, but those issues do not involve any problems with the PJM market rules. Duke may need to reevaluate how it manages risks under the current rules, including its semiannual elections for the basis for start up offers and its protections against fuel price volatility. Duke may need to rethink the way it procures fuel, or to raise with the Commission the issue of whether the terms and conditions included in NGPL's tariff are just and reasonable.

The answer to Duke's problems on January 28th is not to shift the costs and risks of similar future events to PJM customers. PJM customers are not situated to manage the risks of owning and operating Generation Capacity Resources. The risks and rewards of such decisions appropriately lie with the owners of Capacity Resources.

3. The Request Cannot Be Granted Without Harm to Third Parties.

Duke's request clearly does not meet the third requirement for a waiver. Waiving the rules for Duke's benefit means harming third parties. Duke's requested waiver would require customers to pay Duke's gas costs.

D. Any Relief Awarded Duke Should Be Conditional on Process for Calculating and Verifying the Correct Amount.

If, contrary to the Market Monitor's arguments raised here, the Transmission Customer is required to indemnify Duke or the market rules are waived so that Duke can

receive a make-whole payment, then the Commission should reserve the decision on the specific amount of indemnification or market-whole payment. In that event, a separate process would be needed to calculate and verify Duke's costs and to otherwise ensure proper application of whatever principles the Commission determines to apply. The current record is not adequate for this purpose. For example, it is not known whether Duke had any contracts that provided revenue to the Lee Units. For example, it is not clear why Duke should receive credit for \$63 per MMBTU gas when it had \$37 per MMBTU gas available. The Market Monitor is ready to assist with such calculation and verification, if necessary

II. CONCLUSION

The Market Monitor respectfully requests that the Commission afford due consideration to these comments as the Commission resolves the issues raised in this proceeding.

Respectfully submitted,



Jeffrey W. Mayes

Joseph E. Bowring
Independent Market Monitor for PJM
President
Monitoring Analytics, LLC
2621 Van Buren Avenue, Suite 160
Valley Forge Corporate Center
Eagleville, Pennsylvania 19403
(610) 271-8051
joseph.bowring@monitoringanalytics.com

General Counsel
Monitoring Analytics, LLC
2621 Van Buren Avenue, Suite 160
Valley Forge Corporate Center
Eagleville, Pennsylvania 19403
(610) 271-8053
jeffrey.mayes@monitoringanalytics.com

Dated: May 27, 2014

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Eagleville, Pennsylvania,
this 27th day of May, 2014.



Jeffrey W. Mayes
General Counsel
Monitoring Analytics, LLC
2621 Van Buren Avenue, Suite 160
Valley Forge Corporate Center
Eagleville, Pennsylvania 19403
(610) 271-8053
jeffrey.mayes@monitoringanalytics.com