



Commission filed a Notice of Extension of Time, extending the comment deadline to September 16, 2016. On December 7, 2015, P3 filed a doc-less Motion to Intervene in the above-captioned proceeding, and on December 11, 2015, P3 filed comments in support of PJM's initial filing. P3 generally supports PJM's August 16, 2016 Compliance Filing and asks the Commission to accept PJM's Compliance Filing by October 17, 2016, and direct PJM to make the modest revisions as detailed herein.

## **I. COMMENTS**

### **A. Importance of Hourly Offers and FERC's Efforts**

P3 again stresses the importance of supply offer flexibility in day-ahead and real-time markets and the need to introduce this flexibility to the PJM markets as expeditiously as possible. More granular energy offers will enhance price formation while sending price signals reflective of market conditions and allowing for efficient real-time dispatch. Market efficiency is enhanced when generators are permitted to adjust their offers to reflect the real time price of fuel, which can vary on an hourly basis. These hourly updates will allow PJM to dispatch resources that truly are the "least cost" resources available at that time, thereby benefitting consumers. Hourly updates also will provide resources in PJM an adequate opportunity to recover "last minute" fuel costs incurred to comply with its directives to ensure reliability during stressed system conditions. Current rules, which do not allow for updates of day-ahead offers that contain stale market information, may result in confiscatory rates where generators are paid far less than actual costs. The economics of this situation could jeopardize generators' ability to procure fuel in real-time and, as a result, threaten reliability.

P3 appreciates the Commission's continued support for market rule changes that allow generators to submit day-ahead offers that vary by hour and to update offers in real-time. As the Commission clearly concluded in the underlying June 9, 2015 Order,

our review of the record established through the Commission's recent technical conferences on price formation in organized energy and ancillary services markets demonstrates the importance of supply offer flexibility in day-ahead and real-time energy markets. In light of the potential for significant changes in costs between the time for submitting offers in the day-ahead market and real-time operation, ensuring market participants greater flexibility to structure and modify their offers in such markets will allow resources in PJM to better reflect their actual costs in their offers. Such flexibility will also support proper price formation and efficient real-time dispatch. Moreover, as commenters and panelists from the price-formation proceeding have noted, the ability to submit day-ahead offers that vary by hour and to update offers in real-time is especially critical in markets with demands for more flexible and responsive generation resources.<sup>4</sup>

Again, in its recent June 17, 2016 order, the Commission reaffirmed the importance of this issue stating, “[w]e find that it is critical for the Market Sellers of resources to make accurate and timely updates to their cost-based offers . . . .”<sup>5</sup> and directing, “PJM to include in its Tariff and Operating Agreement [ ] a requirement for market participants to submit fuel cost policies that are approved by PJM prior to submission of cost-based offers . . . .”<sup>6</sup>

P3 agrees that it is critical for Market Sellers to be allowed to make accurate and timely updates to their cost-based offers and asks the Commission to move expeditiously to bring this matter to a conclusion. Every winter that passes without hourly offer flexibility is a winter in

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<sup>4</sup> *PJM Interconnection, L.L.C.*, 151 FERC ¶ 61,206 at P 71 (2015).

<sup>5</sup> FERC Order 2016, at P 71.

<sup>6</sup> FERC Order 2016 at P 63.

which the market is less efficient, suppliers are exposed to inadequate cost recovery, and reliability is potentially comprised.

**B. Existing Rules Regarding Fuel Cost Policies Have Been Proven to be Unjust and Unreasonable**

Since the beginning of PJM's operations as an organized market in 1997, generation resource owners have been subject to the cost-based offer requirements in the PJM Operating Agreement "(OA)". P3 Members understand the need for fuel cost policies and have expended considerable effort to develop these policies in compliance with PJM's rules. All generation owners should have confidence that the rules should allow participants to make offers, to the greatest extent possible, based on their best estimate of their actual fuel costs. This goal is entirely consistent with the objectives that hourly offer updates are designed to meet. However, the current process for the development and approval of a fuel cost policy is no longer workable such that the tariff provisions regarding fuel cost policies can no longer be considered just and reasonable. As PJM has acknowledged, PJM's current governing documents are "virtually silent" regarding the appropriate standards to obtain approval of a fuel cost policy, as well as the roles of PJM and the IMM, which are both "critical issues."<sup>7</sup> This lack of clear rules has caused the approval process to become a cumbersome, lengthy and time-intensive negotiating process between the market supplier and the IMM. Multiple P3 members can confirm PJM's recitation that the negotiation process with the IMM over fuel cost policies has in some cases lasted over a year.<sup>8</sup> In the negotiation process, some P3 Members have experienced a panoply of "do-overs" and "try agains" with apparent changes in approval standards along the way and no clear path to

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<sup>7</sup> PJM Compliance Filing, at p 9.

<sup>8</sup> See PJM Compliance Filing at p. 12.

the completion of the process. For example, it would not be atypical for a generator to submit its policy to the IMM and receive three comments back. The generator addresses those comments only to receive comments back on three other sections that it believed were complete. In other instances the IMM has rejected policies that were deemed approved just months prior without providing a clear cause for the rejection. Without a standard of review that is understood and accepted by all parties, negotiations often reach a stalemate and, as a result, many generators are currently operating without an “IMM-approved” fuel cost policy. This is unacceptable for PJM and generators alike.

**C. PJM’s Proposed Fuel Cost Policy Tariff Provisions Represent a “Good Foundation”**

Given the importance of hourly pricing to the integrity of the overall market, it is imperative that the Commission not allow disagreements over fuel cost policies (concerning either process or substance) to become a road block to this long overdue reform to PJM’s cost-based offer rules. Equally important, however, both suppliers and consumers need confidence that the market has sufficient flexibility to address the needs of the system with the lowest price solution – particularly in times of market stress.

As written, the PJM proposal accomplishes that mission and should be accepted by the Commission with several modest revisions. While areas exist where clarification would be helpful and the lack of a finalized Manual 15 prevents an exhaustive review (especially with respect to the important issue of timing for review and approval), PJM’s proposed tariff changes build upon the Commission’s previous guidance regarding the relative roles of the IMM and PJM in reviewing and approving market participant offers, and offer a reasonable standard for review that recognizes challenges in determining anticipated fuel costs, especially in times of system stress.

P3 offers the following specific comments:

**1. The Standard of Review.**

As to the standard of review set forth in subsection (f), P3 generally supports the proposed Tariff provisions while again noting that the proposal references provisions yet to be developed in Manual 15, thus preventing a complete evaluation of the standard. The proposed language for standard of review seeks appropriate information that generators are capable of providing and sets forth a reasonable objective or purpose, i.e., for the Market Seller to demonstrate to PJM how it procures fuel.

PJM or the IMM (or the Commission) should not dictate a generator's fuel procurement practices. The purchasing of fuel for power generation is a complicated and thoughtful piece of any generator's business strategy. Fuel cost policies should reflect, and not dictate, a generator's business decisions with respect to fuel purchases. Moreover, these business decisions are the generators to make, not PJM or the IMM. P3 appreciates that PJM, the IMM and the Commission share a role in protecting the market from market power and market manipulation, and that fuel cost policies are a tool that each can use in fulfilling its responsibilities. To that end, fuel cost policies must be accurate and reflective of each generator's actual business practices.

In order for the market to have confidence that supply offers reflect prevailing market costs and the risks of each market participant, generators need confidence they can procure fuel under their approved fuel cost policy, especially during times of system stress. A fuel cost policy should recognize the unique fuel supply arrangements of each Market Seller and provide the latitude to define the best way to determine its fuel cost, as long as it can be supported thorough documentation. Market Sellers should not be required to use any particular template other than

their actual business practice as a condition to gaining approval of their fuel cost policy. P3 urges the Commission to confirm that the standard for review proposed by PJM allows for this flexibility. Specifically, P3 requests that the Commission condition any approval of PJM's proposal on a clarification that it is acceptable for a generator to provide PJM a clear understanding of how that generator intends to purchase fuel and then provide documentation that the fuel was purchased in that manner, whether the generator is purchasing gas via a contract or on the spot market. PJM and the IMM should not attempt to replicate the market or impose a formulaic evaluation on generators as such a task would prove nearly impossible and more likely lead to chaos during times of system stress. Ultimately, fuel cost policies should complement and not impede the proper functioning of the market.

While the tariff provision proposed by PJM seem to reflect this objective, there remains a general subjectivity to the standard of review that could prove challenging to implement. Manual 15 could help reduce this subjectivity and provide greater certainty to suppliers and consumers, but, again, PJM stakeholders do not have the ability to evaluate a finalized Manual at this time.<sup>9</sup>

**a. Illiquid Market Conditions**

Subsection (iv) of the standard of review proposed by PJM allows for the Market Seller to use the actual means that the Seller uses to price fuel in situations where applicable indices are not sufficiently liquid. In proposing this language, PJM acknowledges that Market Sellers should be able to rely on fuel cost policies that reflect the actual means used to price fuel. PJM provides the example of “documented quotes for the procurement of natural gas” as one

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<sup>9</sup> To date, there have been several PJM stakeholder discussions regarding potential revisions to Manual 15; however, there is no final agreement on revised Manual 15 language and a stakeholder or PJM board vote has yet to be scheduled.

alternative on which Market Sellers can rely where applicable indices are not sufficiently liquid. P3 appreciates PJM's acknowledgement that there are times, particularly with respect to the procurement of intraday gas, that indices are not available and the market is illiquid. However, this illiquidity may also prevent Sellers from obtaining a documented quote for natural gas. If left without a benchmark, a Seller should be permitted to rely on gas supply trader estimates to develop bids. To date, in the experience of some P3 Members, the IMM has not permitted the use of such estimates in fuel cost policies. Estimates are developed using trader experience and knowledge and can be documented for market sellers, PJM, and the IMM as necessary. It is therefore important that the example of "documented quotes" proposed by PJM does not become the *de facto* standard. P3 respectfully requests that the Commission condition any acceptance of PJM's proposal on a clarification that a Seller's fuel cost policy may rely on information other than documented quotes when such quotes are not available. It is very important for alternative means for pricing natural gas during illiquid market conditions are established prior to the actual occurrence of these conditions. Moreover, granting the requested clarification would ensure that PJM's tariff requires fuel cost policies to document the method used for a Seller to construct offers without mandating the particular methodology to be used.

**b. "Consistent With Or Superior To" Standard**

P3 wholeheartedly endorses the language of subsection (g) that allows a generator to establish a fuel cost policy that is based on an alternative methodology to document its fuel costs that is "consistent with or superior to" the standard of review proposed by PJM in subsection (f). Building this flexibility is crucial to long term success of these tariff provisions. Allowing the generator, PJM and the IMM the latitude to consider consistent or superior means of accomplishing the goals of fuel cost policies has merit and should be codified.



**c. Referrals to Enforcement**

PJM proposes that when PJM approves a generator’s fuel cost policy and the IMM disagrees, such disagreement would be referred to the Office of Enforcement.<sup>10</sup> P3 does not dispute the ability of the IMM to refer matters related to tariff violations and suspected wrongdoing such as alleged exercises of market power and market manipulation to the Office of Enforcement. However, under the proposal, the Office of Enforcement may be asked to moderate disputes between PJM and the IMM relating to matters such as PJM’s approval of the generator’s fuel cost policy. The Commission should reject the tariff provisions that would insert the Commission’s Office of Enforcement as an arbiter of disagreements between PJM and the IMM over the approval of a generator’s fuel cost policies. Resolution of such disputes between an RTO and its market monitor are not consistent with the role of the Office of Enforcement but instead are the province of the Commission and its Office of Administrative Law Judges to address in response to a complaint when appropriate, or for its Alternative Dispute Resolution (“ADR”) process to resolve outside of a formal process. In particular, an ADR process led by a FERC Administrative Law Judge (“ALJ”) may be appropriate to resolve disputes between PJM and the IMM. An ALJ-led mediation process will preserve confidentiality of the highly sensitive commercial information contained in a fuel cost policy and would focus more appropriately on the approval of a specific fuel cost policy related to a specific generator.

The Office of Enforcement was structured to investigate potential rule violations – not resolve disputes between PJM and the IMM or adjudicate whether specific rates (of which the Fuel Cost Policies are a component) are just and reasonable under Section 205 of the Federal Power Act. Indeed, the Office of Enforcement itself has indicated that its focus is on matters

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<sup>10</sup> PJM Compliance Filing at p. 34.

relating to fraud and market manipulation, serious Reliability Standard violations, anticompetitive conduct and conduct that threatens the transparency of markets.<sup>11</sup> A difference of opinion between PJM and its IMM on one individual generator's fuel cost policy falls far from this province of issues. This view is consistent with the provisions of the PJM Tariff, which, at Attachment M, currently delineates the types of issues that the IMM may refer to the Office of Enforcement. Issues eligible for referral include potential Market Violations or other untoward behavior of a Market Participant or PJM that may require investigation.<sup>12</sup> A "Market Violation" as defined in the tariff "means a tariff violation, violation of a Commission-approved order, rule or regulation, market manipulation, or inappropriate dispatch that creates substantial concerns regarding unnecessary market inefficiencies, as defined in 18 C.F.R. § 35.28(b)(8)."<sup>13</sup> The IMM's difference of opinion with PJM over a fuel cost policy approval does not fall into any of these categories.

Not only does the PJM proposal represent a departure from the rights set forth in Attachment M of the Tariff to refer suspected instances of wrongdoing and not mere differences of opinion with the RTO on market implementation issues, but also, as a policy matter, the FERC's Office of Enforcement should not be the first line of defense to resolve disagreements between PJM and its IMM. If instead, PJM proposes to rely on the Office of Enforcement as a referee every time a difference of opinion with the IMM arises, this inappropriate overuse of the Office of Enforcement will squander resources that are intended for other purposes. The Commission already has determined that, as between PJM and the IMM, PJM is the ultimate

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<sup>11</sup> See, e.g., *2015 Report on Enforcement*, Docket No. AD07-13-009 at 2 (Nov. 19, 2015).

<sup>12</sup> PJM Tariff, Attachment M, IV.I, 1.

<sup>13</sup> PJM Tariff, Attachment M, II, h-1, Definitions.

arbiter of the reasonableness of a Market Seller's fuel cost policy.<sup>14</sup> PJM should not now seek to add another unnecessary layer of review, especially one with open-ended time frames for resolution.

## **2. The Review Process.**

As stated above, the existing process to submit, review and approve generator fuel cost policies has proven to be unjust and unreasonable due, in part, to the lack of a clear definition of the roles for PJM and the IMM. PJM has proposed a process that focuses on collaboration between PJM and the IMM while respecting the roles of each entity. In many ways, PJM's proposed process is nearly identical to the RPM offer cap review process accepted by the Commission in 2009 as consistent with both Order No. 719 and the PJM/MMU Settlement Agreement.<sup>15</sup> While for the most part PJM's instant proposal is acceptable, there are several aspects that the Commission should not approve as proposed.

Looking at the specific language of the PJM proposal, subsection (e) requires any generator that wants to submit a non-zero cost based offer to submit a fuel cost policy to PJM and the IMM 45 days in advance of the date upon it wishes to offer consistent with the fuel cost policy. The IMM's review will be consistent with that previously approved by the Commission in conjunction with Attachment M of the PJM Tariff. PJM is required to consult with the IMM and to consider any "input and advice timely" received from the IMM. Upon completion of its evaluation, PJM is required to inform the generator of its decision to approve or reject the policy

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<sup>14</sup> PJM Interconnection, L.L.C., 155 FERC 61,282 at P 63; PJM Interconnection, L.L.C. 153 FERC 61,289 at P 47. As PJM stated in its filing, "the Commission made explicitly clear that it is PJM and not the IMM, that approves Fuel Cost Policies". PJM Filing at n.22.

<sup>15</sup> *PJM Interconnection, L.L.C.*, 129 FERC ¶ 61,250 (2009).

in writing, with a copy to the IMM. If the fuel cost policy is rejected, a written explanation must be provided.<sup>16</sup>

PJM's proposal clearly provides a role for the IMM consistent with that previously approved by the Commission in conjunction with the establishment of Attachment M. In that case, the Commission found that PJM was required under Order No. 719 to propose revisions that did not permit the IMM to participate in the administration of PJM's tariff or conduct prospective mitigation, except that the IMM was permitted to provide inputs to PJM -- the entity responsible for making the final determination with respect to RPM offer caps.<sup>17</sup> The proposal is also clear that PJM has the ultimate authority to approve or reject the policy after considering the input of the IMM. Thus, the fuel cost policy review process proposed by PJM is largely consistent with the process previously accepted by the Commission for RPM offer caps.

P3 notes that the proposed tariff language contains no time parameters on PJM's review other than the 45 day requirement, which is an important shortcoming of the proposal that the Commission should require PJM to address in the Tariff or in Manual 15. The Commission should require PJM to include in Manual 15 a timeline for processing the fuel cost policy with similar milestones to that provided with respect to RPM offer caps in Section 6.6(b) of Attachment DD of the Tariff.<sup>18</sup> Additional guidance with respect to the timing of the review process will help ensure that administrative backlogs do not conscript a generator to submitting only offers at \$0/MWh. Moreover, amendments to fuel cost policies may require expedited

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<sup>16</sup> PJM Compliance Filing at p 19.

<sup>17</sup> *PJM Interconnection, L.L.C.*, 129 FERC ¶ 61,250 at P 148 (2009).

<sup>18</sup> See PJM OATT, Attachment DD, Section 6.6(b)(milestones include submittal due date, period for IMM review, date for notifying PJM of a disagreement, deadline for PJM's response, and provisions/deadlines in the event of a lack of response by the IMM).

review in response to a change in conditions. Manual 15 or the Tariff should also provide for such expedited review in limited circumstances.

### **3. Penalties For Non-Compliance.**

The Commission should be mindful that the regulatory goal of fuel cost policies is compliance, not penalties. It should be a shared goal of the Commission, PJM, the IMM and generators that penalties are never assessed. In that regard, generators should be encouraged to have open lines of communication with PJM, the IMM and the Commission – particularly in times of system stress. Moving forward, consideration should be given to a just and timely review process or other compliance focused mechanisms that can provide suppliers and consumers’ confidence that offers reflect prevailing market conditions.

In specific regard to the proposed penalties in subsection (l), P3 is willing to support the proposed penalty structure with one important caveat. As currently written, generators that do not have an approved fuel cost policy are prohibited from offering anything other than \$0/MWh. However, under proposed subsection (l), this generator that is forced to offer in at \$0/MWh would also be exposed to penalties despite the clear fact that the generator could not be motivated to exercise market power with its \$0/MWh offer. Penalties should only be imposed on generators that violate their approved fuel cost policies – not on those that are operating without an approved fuel cost policy. The motivation to offer something other than \$0/MWh should be sufficient to induce a generator to obtain approval for its fuel cost policy. Accordingly, PJM should be required to remove the reference to “the Market Seller does not have a PJM-approved Fuel Cost Policy” in proposed subsection (l).

## II. CONCLUSION

For the foregoing reasons, P3 respectfully requests that the Commission consider its comments and accept PJM's August 16, 2016 Compliance Filing conditioned upon modest revisions detailed herein in an order issued no later than October 17, 2016.

Respectfully submitted,

On behalf of the PJM Power Providers Group

By: /s/ Glen Thomas

Glen Thomas

Diane Slifer

GT Power Group

101 Lindenwood Drive, Suite 225

Malvern, PA 19355

gthomas@gtpowergroup.com

610-768-8080

Dated: September 16, 2016

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 Washington, D.C., this 16th day of September, 2016.

On behalf of the PJM Power Providers Group

By: /s/ Glen Thomas \_\_\_\_\_

Glen Thomas

GT Power Group

101 Lindenwood Drive, Suite 225

Malvern, PA 19355

gthomas@gtpowergroup.com

610-768-8080