UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Offer Caps in Markets Operated by Regional Transmission Organizations and Independent System Operators	Docket No. RM16-5-001

REQUEST FOR REHEARING AND CLARIFICATION OF THE TRANSMISSION ACCESS POLICY STUDY GROUP

Pursuant to Section 313 of the Federal Power Act, 16 U.S.C. § 825*l*, and Rule 713 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713, the Transmission Access Policy Study Group ("TAPS") seeks rehearing and clarification of Order No. 831, the Commission's November 17, 2016 Final Rule on Offer Caps in Markets Operated by Regional Transmission Organizations and Independent System Operators.[1]

SPECIFICATION OF ERRORS

1. The Commission erred by setting the level of the "hard cap" at $2,000/MWh for offers allowed to set the locational marginal prices ("LMP") instead of a lower number.
2. The Commission erred by exempting import offers above $1,000/MWh from the cost-verification requirement, especially if such offers are permitted to set the LMP (which the Final Rule leaves unclear).
3. If the Commission intended to allow regional transmission organizations ("RTOs") to include, when calculating cost-based incremental energy offers, an opportunity cost adder *in addition to* a $100/MWh adder for risk and uncertainty, then the Commission erred by doing so.

---

[1] *Offer Caps in Markets Operated by Regional Transmission Organizations and Independent System Operators*, Order No. 831, 81 Fed. Reg. 87,770 (Dec. 5, 2016), 157 FERC ¶ 61,115 (2016) ("Final Rule" or "Order No. 831").

STATEMENT OF ISSUES

1. Did the Commission err by setting the level of the "hard cap" at $2,000/MWh for offers allowed to set the LMP instead of a lower number? *Pac. Gas & Elec. Co. v. FERC*, 373 F.3d 1315 (D.C. Cir. 2004); *Canadian Ass'n of Petroleum Producers v. FERC*, 254 F.3d 289 (D.C. Cir. 2001).

2. Did the Commission err by exempting import offers above $1,000/MWh from the cost-verification requirement, especially if such offers are permitted to set the LMP (which the Final Rule leaves unclear)? *Ill. Commerce Comm'n v. FERC*, 576 F.3d 470 (7th Cir. 2009).

3. Did the Commission intend to allow RTOs to include, when calculating cost-based incremental energy offers, an opportunity cost adder *in addition to* a $100/MWh adder for risk and uncertainty? If so, did the Commission err by doing so? *Canadian Ass'n of Petroleum Producers v. FERC*, 254 F.3d 289 (D.C. Cir. 2001).

ARGUMENT

I. THE COMMISSION SHOULD SET THE "HARD CAP" BELOW $2,000/MWH.

The NOPR in this proceeding[2] proposed that any pre-verified cost-based incremental energy offer above $1,000/MWh could be used to calculate LMPs, but asked whether it would be necessary to impose a "hard cap" above which such cost-based incremental energy offers would be fully compensated, but would not be used to calculate LMPs.[3] The NOPR asked whether the level of the hard cap should be $2,000/MWh or another value.[4]

In its comments, TAPS urged the Commission to adopt a $1,500/MWh hard cap.[5] TAPS explained that a hard cap is a necessary safety valve to protect against extreme

---

[2] *Offer Caps in Markets Operated by Regional Transmission Organizations and Independent System Operators*, 81 Fed. Reg. 5951 (Feb. 4, 2016), FERC Stats. & Regs. ¶ 32,714 (2016) ("NOPR").

[3] Order No. 831, P 44.

[4] *Id.*

[5] Transmission Access Policy Study Group, Comments at 7-11 (Apr. 4, 2016), eLibrary No. 20160404-5220 ("TAPS Comments").

prices in anomalous conditions when markets are not operating normally—for example as a result of market manipulation or market power abuse, extraordinary circumstances or catastrophes, or dysfunction in markets for fuel or other inputs to electric generation.[6]

TAPS also explained that setting the hard cap at the right level is important to fulfilling the Commission's duty to set just and reasonable rates, and its purpose of "curb[ing] prices and enhance[ing] reliability in the wholesale electricity market."[7] If LMPs were to clear at the hard cap, the difference between a $1,500/MWh and $2,000/MWh hard cap could cause hundreds of millions of dollars to be transferred from homeowners, small businesses, and other electricity consumers to the fleet of electric generators, even if high marginal costs of generation are due to manipulation in fuel markets that the Commission cannot remedy or other market dysfunction. Even if LMPs never clear at the hard cap, the level of the hard cap will also impact other RTO pricing features, such as penalty factors, and so it is important that the hard cap is set at the correct level.[8]

The Final Rule adopted a hard cap of $2,000/MWh.[9] The Commission explained that "a resource may submit a cost-based incremental energy offer above $2,000/MWh, [but] the hard cap will prohibit the use of such offers above $2,000/MWh when

---

[6] As TAPS explained in its comments on the NOPR, the Commission has previously recognized that during the California Market Meltdown, manipulation of natural gas markets—including through transactions over which the Commission has no jurisdiction—had driven wholesale electricity prices in CAISO's single-price market above just and reasonable levels. TAPS Comments at 9 (citing *San Diego Gas & Elec. Co.*, 102 FERC ¶ 61,317, PP 56-61 (2003)).

[7] TAPS Comments at 10 & n.15 (citing *FERC v. Elec. Power Supply Ass'n*, 136 S. Ct. 760, 773 (2016)).

[8] Order No. 831, P 88.

[9] *Id.* P 77.

calculating LMPs."[10] The Commission provided "two primary reasons" for adopting a hard cap: (1) the cost-verification process may have imperfect information about resources' short-run marginal costs, in particular the expected cost of natural gas; and (2) a hard cap will be easier to integrate with other market constructs that place caps or upper bounds on various market elements (e.g., penalty factors associated with shortage pricing or violating transmission constraints).

Although the Commission was correct in determining that a hard cap is required to ensure just and reasonable rates, the Final Rule does not provide an adequate explanation for why it adopted $2,000/MWh, rather than a lower figure, as the level for the hard cap. The Commission indicated that the hard cap should be set at a level such that "resources may experience costs that approach but are unlikely to exceed" that level.[11] But $2,000/MWh does not satisfy that test, because there is insufficient evidence to show that "resources may experience costs that approach" $2,000/MWh.

Part I.A below shows the Commission cannot reasonably base its $2,000/MWh hard cap level on the $1,724/MWh offer made once by a single resource in PJM during the Polar Vortex as described in another proceeding. First, in that proceeding, PJM's characterization of that offer as cost-based was disputed by PJM's independent market monitor, and the Commission made no finding about the accuracy and details of PJM's claim. Second, the level of the hard cap should be based on evidence of a resource's highest *actual* cost, not highest *estimated* cost. Finally, even if estimated cost were an appropriate basis for setting the level of the hard cap, it is inappropriate to rely on an

---

[10] *Id.* Cost recovery for accepted offers above $2,000/MWh, or offers whose costs cannot be pre-verified, would be available through make-whole payments if the actual costs are verified after the fact.

[11] *Id.* P 90.

estimate that was verified using a methodology that is *not* compliant with the Final Rule's requirement that adders for difficult-to-quantify costs may not exceed $100/MWh.

Part I.B shows that the Commission erred in rejecting the $1,500/MWh hard cap proposed by TAPS, because there is no record evidence that any resource has had an actual cost that exceeded that value. And as explained in Part I.C, even if it were appropriate to rely on the claim that one resource did have a $1,724/MWh cost-based incremental energy offer during the Polar Vortex, that claim does not support a hard cap of greater than $1,800/MWh.

A. The Commission's Selection of a $2,000/MWh Hard Cap is Not Supported by the Record.

The Commission adopted the $2,000/MWh hard cap based on its belief that "high natural gas prices during the Polar Vortex resulted in at least one resource with a cost-based incremental energy offer of $1,724/MWh."[12] The Commission predicted that "resources may experience costs that approach but are unlikely to exceed $2,000/MWh."[13]

In fact, the record in this proceeding does not contain substantial evidence that any resource has ever had a legitimate cost-based incremental offer of $1,724/MWh. The Final Rule cites the NOPR as evidence that the Polar Vortex resulted in a resource with a $1,724/MWh offer, but the NOPR did not make such a finding.[14] PJM did not assert in

---

[12] *Id.*

[13] *Id.* The Commission also noted that Potomac Economics "generally supported" the $2,000/MWh level. *Id.* However, Potomac Economics did not explain any reason why the $2,000/MWh level was justified, and moreover, it only supported that level for a "true hard cap" that would not allow for *any* costs above $2,000/MWh to be recovered, even through make-whole payments. Potomac Economics, Ltd., Comments at 8 (Apr. 4, 2016), eLibrary No. 20160405-5015. In contrast, the Final Rule allows for full cost recovery for all offers accepted.

[14] At footnote 199, Order No. 831 cites to paragraph 13 of the NOPR, which only states that the price of

its comments in this proceeding that any resource has had a cost-verified offer of $1,724/MWh.[15] Nor did PJM's Independent Market Monitor.[16]

Exelon, in this proceeding, claimed that "there was a legitimate offer in the energy market of $1,724/MWh in PJM in 2014,"[17] but that claim is not adequately supported. Exelon cites to PJM's December 15, 2014 filing in Docket No. EL15-31-000.[18] In that filing, PJM stated that after it had filed a request for waiver of the then-applicable $1,000/MWh offer price cap in January 2014, it invited market participants to "produce documentation to support what their validly incurred cost-based offers were, developed in accordance with the Cost Development Guidelines . . . in order to determine whether certain resources were eligible for make-whole payments."[19] PJM claimed that "the highest cost-based offer submitted by a Market Seller of a generation resource in accordance with PJM's Cost Development Guidelines was $1,724/MWh."[20]

The PJM Market Monitor, however, concluded that the $1,724/MWh cost-based offer cited by PJM was *not* a valid cost-based offer.[21] According to the Market Monitor,

---

natural gas in PJM during the Polar Vortex rose above $120/MMBtu, which led to resources having short-run marginal costs above $1,000/MWh. *Id.* P 13. The NOPR cites to *PJM Interconnection, L.L.C.*, 146 FERC ¶ 61,041, at P 2, *order on reh'g*, 149 FERC ¶ 61,059 (2014), which states that those record-setting natural gas prices would equate to a marginal energy cost for a simple-cycle combustion turbine generator of approximately $1,200/MWh.

[15] PJM Interconnection, L.L.C. and Southwest Power Pool, Inc., Joint Comments (Apr. 4, 2016), eLibrary No. 20160404-5288.

[16] Independent Market Monitor for PJM, Comments (Apr. 4, 2016), eLibrary No. 20160405-5027; Independent Market Monitor for PJM, Reply Comments (Apr. 19, 2016), eLibrary No. 20160420-5017.

[17] Exelon Corp., Comments at 9-10 (Apr. 4, 2016), eLibrary No. 20160404-5266.

[18] PJM Interconnection, L.L.C., Revisions to Open Access Transmission Tariff and Operating Agreement (Dec. 15, 2014), eLibrary No. 20141215-5253.

[19] *Id.* at 9 n.22.

[20] *Id.* at 8-9.

[21] Independent Market Monitor for PJM, Comments at 2 (Dec. 23, 2014), eLibrary No. 20141223-5109 ("Market Monitor Comments").

the highest, valid cost-based offer that it reviewed was less than $1,500/MWh.[22] PJM responded by asserting that the Market Monitor's analysis was based not on offers made in accordance with PJM's then-applicable Cost Development Guidelines, but rather "on an after-the-fact review of such offers' actual gas costs, imputed heat rates, and elimination of the 10% adder that all cost-based offers are eligible to receive."[23] The Market Monitor did not respond to PJM's claim, and the Commission ultimately accepted PJM's proposed $1,800/MWh cap without making any findings about whether the $1,724/MWh offer cited by PJM was a valid cost-based offer or whether any resource had an actual cost that even approached $1,724/MWh.[24]

Closer examination of the $1,724/MWh offer and the controversy regarding its validity highlights the inappropriateness of relying on that offer as the basis for the $2,000/MWh hard cap level. As described above, PJM states that it verified (using its 2013/2014 Cost Development Guidelines, which allowed for inclusion of opportunity costs and permitted a 10% adder for uncertainty) that a resource had an *estimated cost* of $1,724/MWh during the Polar Vortex. PJM also states that the Market Monitor reviewed the same resource's *actual cost* and concluded that it was less than $1,500/MWh. PJM apparently also participated in that review of actual cost;[25] and it did not dispute the accuracy of the Market Monitor's actual cost analysis.

---

[22] *Id.*

[23] PJM Interconnection, L.L.C., Motion for Leave to Answer and Limited Answer at 5 (Jan. 5, 2015), eLibrary No. 20150105-5135 ("PJM Answer").

[24] *PJM Interconnection, LLC*, 150 FERC ¶ 61,020 (2015).

[25] PJM Answer at 5.

The very large discrepancy between the verification of expected cost and the *ex post* verification of actual cost shows that the former was inaccurate (and far above marginal cost). It therefore should not be relied on to inform the level of the hard cap. Consistent with the Commission's objective of setting the hard cap at a level such that "resources may *experience* costs that approach but are unlikely to exceed" that level,[26] the Commission should determine the hard cap level based on actual *experienced* costs, not estimated expected costs.

In addition, even if it were appropriate for the Commission to use estimated expected costs to inform the level of the hard cap, it was inappropriate for it to rely on the $1,724/MWh offer, which was estimated using a methodology that is not compliant with the Final Rule. As noted above, PJM's filing in another proceeding described the $1,724/MWh offer as verified under the 2013/2014 Cost Development Guidelines, which allowed for an uncapped 10% adder above costs; under the Final Rule, any adder used in *ex ante* cost verification of estimated expected costs will be capped at $100/MWh,[27] and no such adder may be included in an *ex post* verification of actual costs.[28] It was an error for the Commission to set the hard cap level based on an offer that was, at best, validated only under a cost verification methodology that would be unlawful under the Final Rule.

---

[26] Order No. 831, P 90 (emphasis added).

[27] PJM implied that the $1,724/MWh offer included a 10% adder (as permitted by PJM's then-applicable rules). PJM Answer at 5. Thus, the "cost-based" offer before the adder would have been $1,567/MWh. Adding the Final Rule's maximum $100/MWh adder would restrict that cost-based offer to at most $1,667/MWh. PJM's Cost Development Guidelines also permit inclusion of opportunity costs in addition to the 10% adder. If, as requested in Part III below, the Commission also clarifies that opportunity cost adders are included within the $100/MWh cap required by Order No. 831, it is possible that the adjusted *ex ante* offer would be even lower.

[28] Order No. 831, P 207.

In short, the Commission's decision to set the hard cap at $2,000/MWh depended on the disputed claim—which was not resolved in this, or any other, record—that in one instance during the Polar Vortex a single resource in PJM had a cost-based offer of $1,724/MWh, based on then-applicable Cost Development Guidelines that significantly overstated actual costs and are not compliant with the cost verification requirements of the Final Rule. The Commission therefore erred by making a decision that was not based on substantial evidence.[29]

B. The Commission Should Set the Hard Cap at $1,500/MWh.

In its comments on the NOPR, TAPS proposed a $1,500/MWh hard cap, which was supported by a sound analytical approach discussed at the MISO Markets Subcommittee.[30] TAPS explained that a $1,500/MWh hard cap would accommodate cost-based bids from virtually every generator in the MISO footprint even when natural gas prices are 20 to 30 times higher than current average natural gas prices.[31]

The Commission declined to adopt the $1,500/MWh hard cap "because this level is demonstrably lower than cost-based incremental energy offers observed during the Polar Vortex."[32] But, as explained above, there is no credible evidence in this (or any other) proceeding that any resources actually had a legitimate cost-based incremental energy offer above $1,500/MWh. In fact, the PJM Market Monitor has explicitly said

---

[29] *Pac. Gas & Elec. Co. v. FERC*, 373 F.3d 1315, 1319 (D.C. Cir. 2004) ("FERC 'must be able to demonstrate that it has made a reasoned decision based upon substantial evidence in the record.'") (*quoting N. States Power Co. v. FERC*, 30 F.3d 177, 180 (D.C. Cir. 1994)).

[30] TAPS Comments at 10-11.

[31] *Id*.

[32] Order No. 831, P 92. The Commission also notes that the "PJM Market Monitor reported that on 54 occasions in early 2015, resources submitted cost-based incremental energy offers at prices above $1,000/MWh." *Id.* But that evidence does not support the Commission's decision to decline a $1,500/MWh hard cap.

that during the winter of 2014, the "highest valid cost-based offer reviewed by the Market Monitor was less than $1,500[/MWh]."[33]

The Commission rejection of TAPS' proposed $1,500/MWh hard cap was not based on substantial evidence.[34] Moreover, because the Commission dismissed the TAPS proposal, it failed to meaningfully address the evidence that TAPS presented on using an analytical approach to establish the hard offer cap.[35]

C. Alternatively, the Commission should set the hard cap no higher $1,800/MWh.

Even if the Commission could find, based on the record in this proceeding, that a single PJM resource really did have a legitimate cost-based incremental offer of $1,724/MWh, it would still not support the Commission's decision to set the hard cap at $2,000/MWh. The Commission indicated that the hard cap should be set at a level such that "resources may experience costs that approach but are unlikely to exceed" that level.[36] But the level the Commission selected is more than $275/MWh greater than the highest claimed cost-based incremental offer during the record-setting natural gas prices of the Polar Vortex. Thus, even if the $1,724/MWh offer were legitimately cost-based, that does not support a finding that resources will experience legitimate costs that "approach" $2,000/MWh.[37]

---

[33] Market Monitor Comments at 2.

[34] *See supra* note 29.

[35] *Canadian Ass'n of Petroleum Producers v. FERC*, 254 F.3d 289, 299 (D.C. Cir. 2001) (an agency's "failure to respond meaningfully" to objections raised by a party renders its decision arbitrary and capricious).

[36] Order No. 831, P 90.

[37] The Commission did adopt a $2,000/MWh hard cap for PJM in 2015. Its decision, however, was not based on evidence that resources will experience costs at that level, but rather on a compromise among the stakeholders in that region. *PJM Interconnection, L.L.C.*, 153 FERC ¶ 61,289, P 11 & n.9 (2015).

Rather, that information does not support a hard cap higher than $1,800/MWh. It is worth noting that PJM cited the $1,724/MWh offer in the context of a proceeding in which PJM was proposing a $1,800/MWh hard cap, which the Commission accepted as just and reasonable.[38] Moreover, in a report submitted by the PJM Market Monitor to the Commission examining offers submitted during PJM's temporary $1,800/MWh cap applicable from January 16 through March 31, 2015, the Market Monitor stated that there were "zero cost-based or price-based energy offers with incremental offers above $1,800 per MWh" during that period.[39]

In sum, the Final Rule rightly recognizes that a hard cap is needed to protect consumers from unreasonably high LMPs. It is just as important that the Commission set the hard cap at a reasonable level. Here, the Commission placed undue reliance on a claim that a single resource once had a cost-based offer of $1,724/MWh, without adequately considering the provenance of that figure or how it was derived, and despite evidence that the resource's actual cost was below $1,500/MWh. Thus, the Commission should rehear its adoption of a $2,000/MWh hard cap, and instead set the hard cap at $1,500/MWh as proposed by TAPS, or alternatively at a level no higher than $1,800/MWh.

---

[38] *PJM Interconnection, LLC*, 150 FERC ¶ 61,020 (2015).

[39] Independent Market Monitor for PJM, Informational Filing at 4 (May 4, 2015), eLibrary No. 20150504-5255.

II. THE COMMISSION SHOULD NOT ALLOW AN IMPORT OFFER ABOVE $1,000/MWH TO SET THE LMP OR RECEIVE MAKE-WHOLE PAYMENTS UNLESS THE IMPORT OFFER HAS BEEN COST-VERIFIED.

The Commission proposed, in the NOPR, that imports would not be eligible to submit cost-based incremental energy offers above $1,000/MWh.[40] TAPS commented that RTOs should have the option of proposing a methodology that would allow an external resource to set the market clearing price above $1,000/MWh if the cost basis for its offer is verified by the importing RTO prior to market clearance.[41] TAPS also suggested that RTOs should also be allowed to propose a post-market-clearance cost-verification methodology to enable external resources to recover their actual costs from the importing RTO through out-of-market payment, in the event that LMPs in the importing region do not equal or exceed the external generator's actual costs reflected in its offer.

The Final Rule departs from the NOPR by permitting imports to make offers above $1,000/MWh.[42] The Commission also stated that it will not require that import transactions above $1,000/MWh be subject to the verification requirement prior to the market clearing process.[43] Exempting import offers above $1,000/MWh from the cost-verification requirements applicable to internal resources is unjust and unreasonable. And if the Commission intended to permit unverified import transactions above

---

[40] NOPR, P 63.

[41] TAPS Comments at 19-20.

[42] Order No. 831, PP 192-193. Imports will not, however, be permitted to make offers above $2,000/MWh. *Id.*

[43] *Id.*

$1,000/MWh to set LMPs,[44] exempting such transactions from pre-verification requirements is particularly unreasonable.

The Final Rule's exemption of imports from the cost-verification requirement is inconsistent with the Commission's core findings in the Final Rule. The Commission correctly found that "it would be inappropriate to raise the offer cap without imposing a verification requirement."[45] It likewise explained that cost verification is necessary because "market power concerns are heightened when a resource's short-run marginal costs exceed $1,000/MWh."[46] That is because such high prices may indicate that very few resources are available to provide additional supply.[47]

Although the Commission's findings on the need for cost verification were made for internal resources, cost verification is similarly important for imports. By waiving the cost verification requirement for imports, the Commission puts internal and external resources on unequal footing, and creates an exception that could swallow the rule. The Commission offers two reasons for creating this exception, neither of which is supportable.

First, the Commission's finding that *some* imports are not resource-specific, and thus can't be easily cost-verified, cannot support its exemption of *all* imports (including

---

[44] The Final Rule is ambiguous on whether import offers above $1,000/MWh will be eligible to set the LMP in the importing RTO. The Regulatory Text (to be codified at 18 C.F.R. § 35.28(g)(9)) unambiguously states that an offer may not be used to calculate LMP "[i]f a resource submits an incremental energy offer above $1,000/MWh and the costs underlying that offer cannot be verified before the market clearing process begins." And when discussing import offers (Order No. 831, PP 192-198), the Final Rule does not explicitly say that import offers above $1,000/MWh can set LMPs.

[45] *Id.* P 143.

[46] *Id.* P 139.

[47] *Id.* P 144.

resource-specific imports) from the cost verification requirement.[48] A more reasonable solution would be to allow only resource-specific imports that are cost-verified in advance by the receiving RTO to set LMPs above $1,000/MWh. For other imports that cannot be cost-verified in advance, offers in excess of $1,000/MWh that have been cost-verified after-the-fact should be paid out-of-market.[49] Such a solution would promote the Commission's goals of improving transparency and efficiency. It would also ensure all imports have an opportunity to recover their costs, and thus would not discourage imports from offering energy to the importing RTO.[50]

Second, the Commission concludes that exempting imports from the cost-verification requirement is appropriate, because it would be difficult for an external resource to exercise market power in the importing RTO if the adjacent market is competitive.[51] Even if adjacent markets are competitive in the long-run because of the potential for entry and exit, that does not mean generators cannot exercise market power in the short-run under extreme conditions. Indeed, this reason is at odds with the Commission's finding that when short-run marginal costs exceed $1,000/MWh, "market power concerns are heightened . . . because short-run marginal costs in this range may indicate that very few resources are available to provide additional supply."[52]

---

[48] *Id.* P 195.

[49] A system import from another RTO whose "cost" is the LMP at the exporting RTO's border would likely not be pre-verified. However, the import offer, if accepted by the importing RTO, would be paid, after-the-fact through uplift, the lower of its "cost" or its offer, to the extent the seller's offer exceeded the importing RTO's LMP at the border.

[50] The Commission should also require RTOs, in their compliance filings, to ensure that market participants making above-$1000/MWh import offers do not (by setting the LMP or through after-the-fact out-of-market payments) recover more than their full costs nor receive any double-payment.

[51] *Id.* P 196.

[52] *Id.* P 144.

If imports are allowed to set LMPs in the importing RTO without being subject to price verification,[53] the opportunity and incentive for generators to exercise market power—and the adverse impacts on consumers—are even greater. For example, an owner of a fleet of generation both inside and outside an RTO (e.g., in a non-RTO region) would have a strong incentive to try to exercise market power by using the import exemption to end run the internal generation cost-verification requirement. Such an owner would not be able to exercise market power through its bidding strategy for its *internal* resources when short-run prices exceed $1,000/MWh, because all of those resources would be subject to cost verification. But it could use its *external* resources to make import offers in excess of $1,000/MWh that its internal resources would not be permitted to make. If the import resources were permitted to set the LMP, all of the internal resources owned by the market participant would reap infra-marginal rents. Not only would such a scheme be permissible under the Final Rule, it would also be difficult to monitor and detect such anticompetitive behavior, since the Final Rule does not require any cost information from external resources. This gap in the Commission's obligation to ensure just and reasonable rates is not addressed by the Commission's stated willingness to "consider" a separate Federal Power Act Section 205 filing proposing mitigation should the RTO elect to make such a filing.[54]

For those reasons, the Commission's decision to exempt import resources from the requirement that offers above $1,000/MWh be cost-verified was arbitrary.[55] On

---

[53] *See supra* note 44 (describing the ambiguity in whether imports can set LMPs).

[54] Order No. 831, P 197.

[55] *Ill. Commerce Comm'n v. FERC*, 576 F.3d 470, 477 (7th Cir. 2009) (explaining that a reviewing court cannot "uphold a regulatory decision that is not supported by substantial evidence on the record as a

rehearing, the Commission should bar import offers above $1,000/MWh from setting the LMP in the importing RTO unless the import offer has been cost-verified prior to market clearing, and that no make-whole payments should be made to imports unless the import offer has been cost-verified.

III. THE COMMISSION SHOULD NOT ALLOW RTOS TO INCLUDE AN OPPORTUNITY COST ADDER IN ADDITION TO AN ADDER FOR RISK AND UNCERTAINTY CAPPED AT $100/MWH.

A. The Commission Should Clarify That It Intended Opportunity Cost Adders To Be Included in its $100/MWh Cap on Cost Adders.

In the NOPR, the Commission asked whether RTOs or market monitors "may need additional information to ensure that all short-run marginal cost components that are difficult to quantify, *such as certain opportunity costs*, are accurately reflected in a resource's cost-based incremental energy offer."[56] After noting that PJM allows resources to include a 10% adder for such costs, the Commission asked whether it is appropriate for RTOs to include an adder above cost in cost-based incremental energy offers.[57]

The Final Rule concluded that "if an RTO/ISO chooses to retain an adder above cost or proposes to include a new adder above cost in cost-based incremental energy offers above $1,000/MWh, such adders may not exceed $100/MWh."[58] The Commission did not specifically state whether the Final Rule's $100/MWh cap on adders above cost

---

whole").

[56] NOPR, P 59 (emphasis added).

[57] *Id.*; *see also* Order No. 831, P 9 (paraphrasing the NOPR's question as whether "additional information [is needed] to ensure that all short-run marginal cost components, such as risk *or opportunity costs that are often difficult to quantify*, are accurately reflected in a resource's cost-based incremental energy offer, and whether an adder is appropriate") (emphasis added).

[58] Order No. 831, P 207.

includes any opportunity costs. Nor did the Commission make any explicit determination about whether RTOs can allow opportunity costs when developing their pre-verification methodology.

To avoid ambiguity, and to ensure that RTOs do not propose cost-verification methodologies that allow for opportunity costs *in addition to* the $100/MWh adder for cost-based offers above $1,000/MWh, the Commission should clarify that if an RTO allows adders, the maximum total amount of such adders, including both opportunity costs and any other difficult-to-quantify costs, cannot exceed $100/MWh.

B. Alternatively, the Commission Should Grant Rehearing to Prohibit the Total Value of Adders, Including Opportunity Cost Adders, in Offers Above $1,000/MWh From Exceeding $100/MWh.

If the Commission intended to allow RTOs to propose cost-verification methodologies that allow for opportunity costs, in addition to a maximum $100/MWh adder for risk and uncertainty, the Commission should grant rehearing.

As TAPS explained in its comments on the NOPR,[59] opportunity cost should not be allowed at the extreme price levels at issue in this proceeding. The Commission has previously explained:[60]

> An opportunity cost exists if a unit must be run . . . for a transmission constraint and if that unit has only a significantly limited number of available annual run hours (a hydro unit or a unit with environmental run-time limits). The opportunity cost associated with providing 'must run' output is the value associated with the lost opportunity to produce energy during a higher valued time period within the year.

---

[59] TAPS Comments at 17-18.

[60] *PJM Interconnection, L.L.C.*, 126 FERC ¶ 61,145, P 28 n.34 (2009).

When prices are above $1,000/MWh, however, there can be no reasonable expectation that prices will go even higher during later time periods. While inclusion of opportunity cost may be appropriate when prices are low to allow generators and the market to make the best use of a limited resource by preventing its premature depletion, that is no longer a concern when prices are already above $1,000/MWh. During such conditions, it makes no sense to save such resources for a "rainy day"; it is already pouring, and the RTO should be directing all available units to run.

The Final Rule did not address those arguments. To the extent that it intended to allow for opportunity cost in addition to an up-to-$100/MWh adder for uncertainty, the Commission erred and should grant rehearing.[61] On rehearing, the Commission should find that if an RTO allows adders, the maximum total amount of such adders, including both opportunity costs and any other difficult to quantify costs, cannot exceed $100/MWh.

---

[61] *Canadian Ass'n of Petroleum Producers v. FERC*, 254 F.3d 289, 299 (D.C. Cir. 2001) (an agency's "failure to respond meaningfully" to objections raised by a party renders its decision arbitrary and capricious).

CONCLUSION

For the foregoing reasons, the Commission should correct the errors in Order No. 831 by granting rehearing or clarification as requested above.

Respectfully submitted,

/s/ Cynthia S. Bogorad

Cynthia S. Bogorad
William S. Huang
Latif M. Nurani

Attorneys for
Transmission Access Policy Study Group

Law Offices of:
Spiegel & McDiarmid LLP
1875 Eye Street, NW
Suite 700
Washington, DC
(202) 879-4000

December 19, 2016

CERTIFICATE OF SERVICE

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

Dated on this 19th day of December, 2016.

/s/ Latif M. Nurani
Latif M. Nurani

Law Offices of:
Spiegel & McDiarmid LLP
1875 Eye Street, NW
Suite 700
Washington, DC 20006
(202) 879-4000