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Honorable Kimberly D. Bose
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E., Room 1-A
Washington, D.C. 20426

Re: *PJM Interconnection, L.L.C.*, Docket No. ER11-4402-~~000~~ 001

Dear Ms. Bose:

PJM Interconnection, L.L.C. (“PJM”) hereby submits the following responses to the correspondence issued on October 31, 2011, by the Federal Energy Regulatory Commission (“FERC” or “Commission”) requesting additional information in this proceeding.¹ In particular, the Deficiency Letter directed PJM to provide additional information and clarification regarding its August 30, 2011 filing proposing revisions to PJM’s Open Access Transmission Tariff (“PJM Tariff”)² which were meant to set forth additional means for black start service providers to recover incremental costs associated with providing black start service.³ PJM acknowledges that the information provided herein constitutes an amendment to the August 30th Filing.

A. Answers to Questions

- (1) PJM’s proposed recovery of non-NERC incremental costs does not require documentation. Please explain and provide documentation/examples of costs that cannot be documented. Explain why new black start units should be allowed to avoid documenting all capital costs of black start equipment.**

All black start unit owners are required to document their costs before they are eligible to recover those costs as contemplated in PJM Tariff Schedule 6A. Paragraph 17 of Schedule 6A specifically provides that any changes to a black start unit owner’s revenue requirements

¹ *PJM Interconnection, L.L.C.*, Deficiency Letter, Docket No. ER11-4402-000 (October 31, 2011) (“Deficiency Letter”).

² Capitalized terms not otherwise defined herein have the meaning specified in the PJM Amended and Restated Operating Agreement or the PJM Open Access Transmission Tariff, as appropriate.

³ *PJM Interconnection, L.L.C.*, ER11-4402-000 (August 30, 2011) (“August 30th Filing”).

“...must be submitted to the Market Monitoring Unit for review and analysis, *with supporting data and documentation*, pursuant to Section III of Attachment M – Appendix and the PJM Manuals.” (emphasis added) Moreover, the definition of “Incremental Black Start Capital Costs” as set forth in Paragraph 18 specifies that they “...are the new or additional capital costs *documented* by the owner or accepted by the Commission of the incremental equipment solely necessary to enable a unit to provide Black Start Service...” *emphasis supplied*. In the event that the unit owner and Market Monitoring Unit are unable to agree upon documented values, the unit owner may document those values to PJM, who may agree with the Market Monitoring Unit’s determination, or accept the documented values. See, PJM Tariff – Schedule 6A, ¶ 17. PJM has not proposed to change this requisite submittal of data and documentation by black start unit owners in the context of this filing.

Some of the confusion in this regard may be linked to discussion set forth in PJM’s transmittal letter accompanying the proposed PJM Tariff revisions. There, PJM noted that during the previous filing revising several of the black start revenue requirements provisions, some parties had requested that the Commission consider an alternative approach that would allow those black start service providers that were using the then-current formulaic rate (*i.e.* the Base Formula Rate), the option to recover NERC-CIP related capital costs without the added requirement that they document historic capital costs as required by the then-proposed Capital Cost Recovery Rate.⁴ The proposal offered in the present filing was built upon this concern and, ultimately, the submitted revisions were designed to allow black start service providers the opportunity to recover CIP-specific NERC-related capital costs as an additive to the existing Base Formula Rate without requiring them to re-submit and document those historic capital costs that are, or were, recovered utilizing the existing Base Formula Rate. However, all incremental black start capital costs above the base recovery (and all variable capital costs, regardless of the chosen recovery methodology), whether they are NERC-specific or not, must be documented and approved as set forth in Schedule 6A.

To be clear, the Base Formula Rate is a proxy cost rate that has existed in PJM Tariff Schedule 6A since its inception and provides a black start unit owner the opportunity to recover its assumed fixed capital costs utilizing a straight formula based upon the unit’s respective CONE (Cost of New Entry) and capacity value, and not upon documented actual cost incurrence. As set forth in Schedule 6A, Fixed Black Start Capital Costs for these specific units are calculated, simply, as **CONE * Black Start Unit Capacity * X** (“X” approximating 1 or 2%, depending on the unit’s attributes). Because the Base Formula Rate is a proxy cost rate, a unit owner electing to recover its fixed capital costs would not provide documentation to PJM of any actual fixed costs it had incurred because it has been assumed that the proxy cost rate is an appropriate approximation of those costs – a true black-box cost recovery mechanism.⁵ However, the fixed capital cost recovery formulas that were instituted in 2009 and the presently proposed mechanisms, all require the documentation and approval of any costs not recovered pursuant to the proxy cost Base Formula Rate.

⁴ See, PJM Transmittal, pp. 3-4.

⁵ However, even under the historical Base Formula Rate, to obtain recovery of any variable capital costs, such as operation and maintenance expenses, the black start unit owner must document those costs annually.

(2) In the case of older, fully depreciated units that have no investment to recover, please explain why the Capital Cost Recovery Rate – NERC-CIP Specific Recovery equation, which includes the black box equation for existing investment would not result in over-recovery of costs.

As noted above, the Base Formula Rate is a proxy cost rate which has existed in Schedule 6A since its inception and provides a black start unit owner with a nominal return of and return on its putative, or expected, annual fixed capital investment to provide black start service. It was not contemplated or designed to be representative of the unit owners actual capital investment, but was considered, and accepted as, a just and reasonable approximation of that investment. Because it is a proxy cost rate, for those unit owners that have elected to recover their revenue requirements utilizing the Base Formula Rate, it is assumed that they have incurred a level of capital investment commensurate with the return provided in that rate. There is no inherent limitation on how long a black start unit owner may continually seek recovery using the Base Formula Rate.

In this case, the proposed NERC-CIP Specific Recovery allows the black start unit owner to recover, in addition to the Base Formula Rate, those incremental costs documented by the owner for equipment necessary to maintain its black start unit in compliance with mandatory NERC CIP Reliability Standards. The Base Formula Rate was developed prior to any contemplation of any NERC-related costs. In this case, PJM stakeholders decided not to take on the arduous task of renegotiating the entire Base Formula Rate just to cover NERC-CIP specific related costs generically, especially since some black start units may not incur any costs for compliance. Instead, stakeholders broadly supported a narrow process where the owner could document and request actual capital costs for NERC CIP compliance for approval. This process of demonstrating the NERC-CIP specific costs will ensure that the costs included in the NERC-CIP specific recovery are, in fact, related to the unit owners' compliance with NERC-CIP standards, and are not other costs that are being recovered under the Base Formula Rate. In addition, PJM's proposal in this proceeding contains a concession in response to concern raised by the Independent Market Monitor ("IMM") during the stakeholder process that limits recovery under the NERC-CIP Specific Recovery for larger units when those costs are also being recovered.

Quite frankly, the IMM's argument as stated in its comments that allowing a unit owner the opportunity to recover incremental costs necessary to maintain the black start unit in compliance with NERC CIP Reliability Standards could result in over-recovery of costs for older units is misplaced. Both the Commission and PJM stakeholders have previously determined that it is a reasonable allowance for a black start unit owner to receive the nominal Base Formula Rate for its imputed capital investment on a rolling basis and that rate was designed, both, to be a proxy for historic and nominal ongoing capital investment. But, as noted above, it did not contemplate that a unit owner could be required to invest significant capital into the black start unit to maintain compliance with reliability standards. Such unit owner should have a reasonable opportunity to recover those costs.

No PJM stakeholder or the IMM has ever argued that a black start unit owner should not be allowed to recover its imputed capital investment pursuant to the Base Formula Rate because

it has an older, fully depreciated unit presumably because it is recognized that the Base Formula Rate is a proxy for both historic and nominal ongoing capital investment. The simple allowance of providing the unit owner the opportunity to recover documented, incremental (and potentially costly) NERC-CIP specific capital costs does not change the rationale supporting the adoption of the Base Formula Rate in the first instance and should not be considered an impediment to adopting the proposal offered in this filing.

- (3) Explain how PJM will prevent the over-recovery of training costs since training costs are included in the NERC-related Critical Infrastructure Protection Standards and also in the formula for calculating a generator's annual Black Start Service revenue requirement.**

Schedule 6A defines "Incremental Black-Start NERC-CIP Capital Cost" as "those *capital costs* documented by the owner or accepted by the Commission for the *incremental equipment* solely necessary to enable a Black Start Unit to maintain compliance with mandatory Critical Infrastructure Protection Reliability Standards. . . ." (emphasis added). By its definition, Incremental Black-Start NERC-CIP Capital Cost does not include training costs, rather it is limited to "capital costs" for "incremental equipment." Schedule 6A provides an allowance for black start training activities, set at a fixed annual rate of 50 hours per site at a rate of \$75 per hour for all plants that are black start resources. This is for black start training activities involving restoration drills and procedure review activities that plant operating staff conduct throughout the year. These activities are not related to NERC-CIP Reliability Standard compliance and the formula was not altered to recover any NERC-CIP training expenses.

- (4) Please clarify, or submit a tariff amendment, that describes whether the incentive factor Z is applicable to those black start units that establish a commitment pursuant to paragraph 6 of Schedule 6A since the Tariff does not explain how it would apply in this circumstance.**

The incentive factor, or "Z," does not apply to any black start cost recovery other than those units that have elected to forego recovery of new or additional Black Start Capital Costs and commit to provide black start service for a term of two years as set forth in paragraph, or section, 5 of Schedule 6A. The definition of "Z" in Paragraph 18 of Schedule 6A explicitly limits the application of the incentive factor to those "...Black Start Units with a commitment established under section 5 above and shall be ten percent."⁶ As such, those black start unit owners who elect to recover any new or additional Black Start Capital Costs (as stated in paragraph 6) and commit to a term of service set forth in the applicable Cost Recovery Factor ("CRF") table in Schedule 6A, will not be eligible to recover the incentive factor.

⁶ While this definition makes reference to "section 5," it is clarified that references to "sections" within Schedule 6A refer to sections of Schedule 6A, unless otherwise specified.

(5) Please clarify by what is meant by the phrase, “if applicable,” in the definition of “FERC-approved rate” included in the Capital Cost Recovery Rate equation.

A black start unit owner providing black start service in the PJM Region has, basically, three avenues of cost recovery:

1. Under paragraph 5 of Schedule 6A, it can forego recovery of any new or additional Black Start Capital Costs, establish a two-year rolling commitment and obtain its revenue requirement pursuant to the proxy cost Base Formula Rate;
2. Under paragraph 6 of Schedule 6A, it can seek to recover new or additional Black Start Capital Costs, establish a commitment period as set forth in the applicable CRF table and obtain its revenue requirements utilizing one of the established, or proposed, Capital Cost Recovery rates set forth in paragraph 18;
3. Finally, the unit owner could pursue a rate filing with the Commission and seek to establish its black start revenue requirements based upon a Commission-approved rate, thereby essentially sidestepping the Schedule 6A formulaic methods altogether.

Under the proposed revisions to Schedule 6A, PJM stakeholders opted to allow those unit owners that had previously established their revenue requirements pursuant to a Commission, or FERC, approved rate, the opportunity to recover new or additional incremental capital costs that necessarily would not have been included in that approved rate. Under Schedule 6A as it exists today, these unit owners could have been required to forego any of their previously Commission-approved cost recovery in favor of documenting new or additional incremental costs for recovery under Schedule 6A. Therefore, the Capital Cost Recovery Rate is proposed to be amended to include the allowance of the FERC-approved rate as a formulaic component.

However, not all black start unit owners have opted to establish their black start revenue requirements pursuant to a FERC-approved rate, and that formulaic component of the Capital Cost Recovery Rate would not be applicable to those unit owners. As a result, the definition of FERC-approved rate includes the caveat that it should be calculated as a component of the Capital Cost Recovery Rate only if the unit owner has documented a prior FERC-approved rate.

(6) PJM states at page 13 in its October 10, 2011 Answer to Protest of the Independent Market Monitor that: “appropriate safeguards have been included which limit the opportunity for a black start unit owner to garner a windfall from its investment in the black start unit.” Explain in detail what PJM means by “appropriate safeguards” and how those safeguards will prevent a black start unit owner from garnering a windfall.

Under Schedule 6A, black start unit owners have historically submitted cost data to PJM and the Market Monitoring Unit for review and analysis and, in the last couple of years, this process has been enhanced by revisions to paragraph 17 which set forth the review process in more detail. Serving as perhaps the most important safeguard to ensure that a black start unit

owner is only requesting compensation for actual costs and through that process cannot garner an inappropriate windfall, paragraph 17 requires that the unit owner submit supporting data and documentation of its costs to the Market Monitoring Unit (and PJM) for evaluation and, ultimate, approval. In this process, the Market Monitoring Unit must approve the level of costs submitted by the black start unit owner, but if it does not, then the unit owner may seek approval of those costs from PJM. Ultimately, in the event that the unit owner or the Market Monitoring Unit does not agree with the determinations resulting from this review, either party may petition the Commission to determine the appropriate revenue requirement. This independent scrutiny and resulting process ensures that the black start unit owner is seeking recovery of only those costs that are appropriate as being solely necessary to enable the black start unit to provide black start service.

Additionally, with the revisions proposed in this filing, another process has been included in paragraph 20 to provide PJM Member review of any additive NERC-CIP costs submitted by a unit owner for recovery under the paragraph 18 Cost Recovery Rates. Under this proposed provision, when a unit owner submits NERC-CIP specific capital costs for recovery, PJM shall notify its Members 30 days prior to the effective date of the proposed increase in black start charges. In turn, a Member may submit a written request to PJM and the Market Monitoring Unit to review the documentation supporting the incremental costs. In the event that the PJM Member is not satisfied that the black start unit owner has justified its costs, it ultimately may seek to challenge those costs.

Moreover, in proposed paragraph 21, the Market Monitoring Unit will be required to include a black start service summary in its annual State of the Market report. This additional summary will contain a descriptive summary of the NERC-CIP specific capital costs documented by black start unit owners, including an overview of the types of expenses documented and the overall cost of those expenses on an aggregate basis. This additional transparency will allow the PJM stakeholders who ultimately pay for black start service, the opportunity to scrutinize the level of such costs to ensure that they are not inadvertently misapplied.

Taken together, these safeguards provide an appropriate level of transparency and analysis to confirm that black start unit owners are not capable of garnering a windfall on its investment, but simply recovering its documented costs.

B. Service

PJM has served a copy of this filing on all PJM Members and on all state utility regulatory commissions in the PJM Region by posting this filing electronically. Electronic service is permitted as of November 3, 2008, under the Commission's regulations⁷ pursuant to Order No. 714⁸ and the Commission's Notice of Effectiveness of Regulations issued on October

⁷ See, 18 C.F.R. §§ 35.2, 154.2, 154.208 and 341.2.

⁸ *Electronic Tariff Filings*, Order No. 714, 124 FERC ¶ 61,270.

28, 2008, in Docket No. RM01-5-000. In compliance with those regulations, PJM will post a copy of this filing to the FERC filings section of its internet site, located at the following link: <http://www.pjm.com/documents/ferc-manuals/ferc-filings.aspx> with a specific link to the newly filed document, and will send an e-mail on the same date as this filing to all PJM Members and all state utility regulatory commissions in the PJM Region⁹ alerting them that this filing has been made by PJM today and available by following such link. If the document is not immediately available by using the referenced link, the document will be available through the referenced link within 24 hours of the filing. Also, a copy of this filing will be available on the Commission's eLibrary website located at the following link: <http://www.ferc.gov/docs-filing/elibrary.asp> in accordance with the Commission's regulations and Order No. 741.

3. Conclusion

With this additional information and clarifications, PJM respectfully requests that the Commission accept the proposed revisions for filing as offered in the August 30th submittal.

Respectfully submitted,

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⁹ PJM already maintains updates and regularly uses mail lists for all PJM Members and affected commissions.