

138 FERC ¶ 61,020
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Philip D. Moeller, John R. Norris,
and Cheryl A. LaFleur.

PJM Interconnection, L.L.C.

Docket No. ER11-4402-001

ORDER ACCEPTING TARIFF REVISIONS SUBJECT TO CONDITIONS

(Issued January 13, 2012)

1. On August 30, 2011, PJM Interconnection, L.L.C. (PJM) filed Tariff revisions (PJM filing) in order to provide additional means for black start service providers to recover incremental costs associated with providing black start service¹, particularly those associated with compliance to mandatory North American Electric Reliability Corporation (NERC) Critical Infrastructure Protection (CIP) Reliability Standards. In addition, the revisions provide for the ability of a black start service provider to elect an alternate Capital Recovery Factor (CRF) which is tied to the life span of the capital improvements being made, as opposed to the life of the unit which is being improved. PJM requests that the Commission accept the proposed revisions for filing effective November 1, 2011. For the reasons discussed below, the Commission accepts PJM's proposed Tariff revisions, to be effective November 1, 2011, subject to conditions.

I. Background

2. Schedule 6A of PJM's Tariff sets forth the details for identifying generators to provide black start service. In 2009, PJM submitted proposed, and the Commission accepted, revisions to Schedule 6A designed to allow black start service providers to recover incremental costs necessary to provide black start service.² The annual black

¹ Black start service is the ability of a generating unit to start-up without an outside electrical supply or to continue operating at reduced levels when disconnected from the grid, which is needed for restoration of the transmission system in the event of a de-energizing event (e.g., a blackout).

² *PJM Interconnection, LLC*, 127 FERC ¶ 61,197 (2009) (Commission 2009 Order).

start service revenue requirement for each provider was determined in accordance with the formula set forth in paragraph 18 of Schedule 6A.³ The formula included an incentive factor designed to provide compensation for black start service, including reimbursement for the actual out of pocket costs of providing the service plus an incentive payment to encourage provision of the service, as well as allocation factors for fixed and variable generation costs.⁴

3. PJM's 2009 Filing provided black start service providers with two commitment options linked to their recovery of new or additional Black Start Capital Costs. First, under paragraph 5 of Schedule 6A a black start service provider can elect to forego recovery of new or additional Black Start Service Capital Costs. A black start service provider electing this option is required to provide black start service on a rolling, two-year basis until PJM, the transmission owner or the black start owner provides one-year advance notice of termination. Second, under paragraph 6 of Schedule 6A, a black start service provider may elect to recover new or additional Black Start Capital Costs in which case it is required to provide the service for a term based upon the reasonable estimate of the expected life of the black start unit.

4. Under the 2009 revisions, black start providers can establish their revenue requirement either through: (1) a Commission-approved rate for the recovery of the cost of providing such service for the entire duration of the commitment term set forth in either section 5 or 6, as applicable; or (2) formulas based on the commitment terms chosen.

II. Description of Filing

5. PJM states that the revisions proposed herein represent the collective work of the Black Start Services Working Group (BSSWG), which was chartered to discuss and recommend courses of action to address additional black start service issues. The revisions are designed to: (a) allow all black start service providers regardless of their cost recovery method the opportunity to recover incremental black start capital costs; and (b) provide the option for those black start unit owners electing to recover new or additional Black Start Capital Costs to commit to providing Black Start Service for a term based upon the age of the applicable black start unit or the longest expected life of the incremental capital improvements.

³ The formula for calculating a black start service provider's annual black start service revenue requirement under paragraph 18 is: $\{(\text{Fixed Black Start Service Costs}) + (\text{Variable Black Start Service Costs}) + (\text{Training Costs}) + (\text{Fuel Storage Costs})\} * (1 + Z)$, where Z is an incentive factor equal to ten percent.

⁴ *PJM Interconnection, LLC*, 127 FERC ¶ 61,197, at P 3 and 4, (2009).

6. PJM states that the proposed revisions represent an attempt to encourage the provision of new and existing black start service by ensuring that black start service providers are afforded opportunities to recover their true costs of service, plus reasonable incentives. PJM also proposes minor revisions to Schedule 6A to correct words and punctuation. The three options available for black start cost recovery are the Base Formula Rate, the capped Base Formula Rate plus NERC-CIP Capital Cost recovery, and the FERC approved rate plus Incremental Black Start Capital Costs recovery. The three options are described below in sections A, B, and C.

A. Base Formula Rate

7. There are no substantive revisions to the previous black box rate, which PJM proposes to call the Base Formula Rate in this filing. The Base formula rate applies only to those black start units that elect to forego recovery of new or additional black start capital costs and therefore have a limited commitment period. Net CONE is defined for this purpose as the current installed capacity net Cost of New Entry (expressed in \$/MW year) for the CONE area where the black start unit is located. The proposed Base Formula Rate is $\text{Net CONE} * \text{Black Start Unit Capacity} * \text{Black Start Allocation Factor}$.

B. Capital Cost Recovery Rate – NERC-CIP Specific Recovery

8. The Capital Cost Recovery Rate is one option available for those black start unit owners that elect to recover new or additional black start capital costs and commit to providing black start service for a longer period of time. The formula for recovery of fixed black start costs is $(\text{Net CONE} * \text{Black Start NERC-CIP Unit Capacity} * X) + (\text{Incremental Black Start NERC-CIP Capital Cost} * \text{CRF})$. In this calculation, Black Start NERC-CIP Capital Costs are defined and limited to only those incremental costs incurred by the generator owner to maintain compliance with the applicable NERC-CIP Reliability Standards in its provision of black start service; therefore other capital costs, including those incurred to comply with the operational NERC Reliability Standards or undocumented capital costs may not be recovered pursuant to this proposed methodology. This proposed formulaic calculation is, essentially, the Base Formula Rate with the added ability to document, and recover, incremental NERC-CIP specific capital costs. The one major difference is that generators seeking recovery under this rate are limited to the first 100 MW for hydropower units and 50 MW for diesel and CT units. The ability to recover documented NERC-CIP specific capital costs requires that the unit owner commit to providing black start service for the term specified in the applicable paragraph 18 CRF Table; thus full recovery of the applicable capital costs are tied to a commitment period to provide black start service which is linked to, either, the life of the unit being improved, or the longest expected life of the capital improvement.

9. PJM states that while those capital improvements which qualify as solely necessary to meet NERC-CIP Reliability Standards have not been defined in

Schedule 6A, the existing Schedule 6A requires that the unit owner document and that the PJM IMM validate those costs that have been claimed by the unit owner in all circumstances. Specifically, the unit owner must document those costs, affirm that the costs being submitted for recovery were required to satisfy applicable CIP-specific NERC Reliability Standards, and have those costs validated by the PJM IMM. In the event that the unit owner and the PJM IMM cannot agree on the level of these rate components, the unit owner may submit them to PJM, which will determine whether it will accept such values or not. If the unit owner does not agree with these determinations, it may submit those values to the Commission for approval. PJM also proposes that when a unit owner submits NERC-CIP specific capital costs for recovery, PJM shall notify its Members thirty days prior to the effective date of the proposed increase in black start charges, and provide them the opportunity to review the supporting documentation. PJM also proposes that the PJM IMM will now include a black start service summary in its annual State of the Market report.

C. Capital Cost Recovery Rate

10. In this filing, a change has been proposed that would allow black start unit owners that are recovering legacy costs pursuant to a Commission-approved rate to also seek recovery, under Schedule 6A, of any new incremental capital improvements made that are solely related to providing black start capabilities to their units. The Capital Cost Recovery Rate has been modified to calculate Fixed Black Start Service Costs as (FERC approved rate) + (Incremental Black Start Capital Costs * CRF). The corresponding definition of Incremental Black Start Capital Costs has also been changed slightly to clarify that such costs are those new or additional capital costs documented by the owner to provide black start service, but does not include those costs that are already being recovered by the unit owner pursuant to a Commission-approved rate. Incremental Black Start Capital Costs include those costs incurred by a Black Start Owner in order to meet NERC Reliability Standards. PJM proposes to clarify that the applicable commitment period for black start unit owners that have elected to recover Incremental Black Start Capital Costs as part of the Capital Recovery Rate, in addition to any FERC-approved rate, shall be required to provide black start service for a term which is the greater of the FERC-approved recovery period or the applicable term of commitment as established by either CRF table.

D. Capital Recovery Factor

11. PJM proposes two methods of calculating the Capital Recovery Factor to be used in the recovery of incremental capital cost. The first (similar to the existing tariff) is based on the age of the black start unit and the term of commitment. The second is based on the lifespan in years of the capital improvement. In the event that a unit owner seeks recovery of capital improvements that are included in more than one category capital

improvement lifespan, the applicable commitment period, and associated recovery for each category, will be the longest expected life of those improvements.

E. Options to Change Recovery Methods

12. A black start unit owner that is recovering costs through the Capital Cost Recovery Rate – NERC-CIP Specific Recovery has the option at any time to switch to recovery under the Capital Cost Recovery Rate which requires a FERC-approved rate.

13. PJM proposes that a black start unit owner may make a non-revocable election to forgo calculation of its fixed black start service costs and revert to the Base Formula Rate (with the shortened commitment period) as long as it forfeits any future payments established under the original Capital Cost Recovery Rate. PJM believes that a unit owner that fully reaches its capital recovery term could agree to continue to provide black start service for receiving compensation through the Base Formula Rate, and that without such a provision, it is possible that the unit owner would have no incentive to continue to provide black start service.

III. Notice of Filing and Responsive Pleadings

14. Notice of PJM's August 30, 2011 Filing was published in the *Federal Register*, 76 Fed. Reg. 55,896 (2011), with interventions and protests due on or before September 20, 2011. Dominion Resources Services, Inc., FirstEnergy Solutions Corp., American Municipal Power, Inc., and NRG Companies,⁵ each filed a timely motion to intervene. PSEG Companies⁶ filed a timely motion to intervene and comments in support. Exelon Corporation, Duke Energy Corporation, and GenOn Parties⁷ each filed an out-of-time motion to intervene.

15. On September 20, 2011, the PJM IMM filed a timely protest to PJM's filing. On October 5, 2011, GenOn Parties filed reply comments in support of PJM's filing. On

⁵ The NRG Companies include NRG Power Marketing LLC, Conemaugh Power LLC, Indian River Power LLC, Keystone Power LLC, NRG Energy Center Dover LLC, NRG Energy Center Paxton LLC, NRG Rockford LLC, NRG Rockford II LLC, and Vienna Power LLC.

⁶ The PSEG Companies include PSEG Power LLC and PSEG Energy Resources & Trade LLC.

⁷ GenOn Parties include GenOn Energy Management, LLC, GenOn Chalk Point, LLC, GenOn Mid-Atlantic, LLC, GenOn Potomac River, LLC, GenOn REMA, LLC, and GenOn Wholesale Generation, LP.

October 10, 2011, PJM filed an answer to the protest of the PJM IMM. On October 28, 2011, the PJM IMM filed an answer to PJM's answer. On October 31, 2011, the Commission issued a Deficiency Letter requesting additional information regarding PJM's filing. PJM filed its response on November 14, 2011. PJM's response was noticed on November 16, 2011 with interventions and protests due on or before December 6, 2011. On December 6, 2011, the PJM IMM filed comments and PJM filed an answer to the PJM IMM's comments on December 16, 2011.

A. Comments of PSEG Companies

16. The PSEG Companies support the proposed revisions to the PJM Tariff.⁸ They maintain that the proposed tariff revisions are intended to assure that adequate black start resources are available by providing an opportunity for black start generation owners to recover their prudently-incurred costs of service, including costs associated with compliance with the NERC-CIP Reliability Standards.⁹ Moreover, the PSEG Companies assert that without a mechanism to recover costs, merchant generation owners may choose to cease offering black start service which will impact the reliability of the Bulk Power System.¹⁰

B. Protest of the PJM IMM

17. The PJM IMM states that PJM's filing responds to the complaints of a few black start service unit owners that, under the recently adopted rules, would be required to spend substantial time and effort to calculate, and document, the non-NERC related capital costs; however, PJM's filing does not offer any evidence that the purported problem exists nor does it explain why the specific proposed revisions would be necessary even if the alleged problem did exist.¹¹ The PJM IMM states the proposed approach nullifies the reform of Black Start Service procurement achieved by PJM in 2009 which sought to avoid the two most serious flaws in PJM's filing: piecemeal recovery of costs in contravention of long-standing ratemaking principles, and provisions that disrupt the link between cost recovery and service obligations. The PJM IMM states that nothing substantively has changed since 2009; nevertheless, PJM allowed the complaining parties to reopen the black start procurement rules in the BSSWG, which

⁸ PSEG Companies Comments at 4.

⁹ *Id.* at 4-5.

¹⁰ *Id.* at 5.

¹¹ PJM IMM Protest at 1.

met 15 times in late 2010 and 2011.¹² During this time the PJM IMM states it repeatedly requested evidence of the alleged problem; specifically, the PJM IMM requested examples of investment costs in the incremental equipment solely necessary to provide black start service that service providers could not document. The PJM IMM states that no such evidence was provided for consideration by the BSSWG.¹³ The PJM IMM states that the BSSWG agreed to develop provisions that would: (i) allow piecemeal recovery of costs related to compliance with CIPS on top of the incentive rates; (ii) allow separate recovery of individual investments based on an individual accounting of expected lives, as opposed to a single levelized cost recovery; and (iii) permit recovery of costs through the PJM Tariff on top of costs recovered under a separate rate approved directly by the Commission; however, the relationship of items (ii) and (iii) to the alleged problem of cost documentation has never been established.¹⁴

18. The PJM IMM states that the current formula rate included in paragraph 5 of Schedule 6A is an incentive rate that was designed to create an incentive for older, fully depreciated units that have no investment to recover to continue to provide black start service. The PJM IMM states that recovery of minor investments was subsumed in the incentive rate for Fixed Black Start Service Costs while major investments were recoverable through filings with the Commission, but in 2009, PJM added a third option, a formula rate that allowed for the recovery of significant documented investment in incremental black start equipment on a cost basis that avoided a need for unit owners to file with the Commission which could include a combination of both CIPS and black start equipment. The PJM IMM states that the Commission's 2009 Order approved an approach designed to allow the recovery of CIPS costs, which had not been anticipated when the incentive rate was originally implemented; and the approach approved carefully avoided blurring compensation based on incentive payments and compensation based on cost recovery.¹⁵ The PJM IMM complains that PJM's filing inappropriately and unnecessarily blends them by creating a special adder relating to one particular type of cost and levies it on top of the incentive rate; and this approach amounts to ad hoc and

¹² *Id.* at 2-3.

¹³ *Id.* at 3.

¹⁴ *Id.* at 4.

¹⁵ *Id.* at 4-6.

piecemeal ratemaking, which is prohibited under longstanding traditional ratemaking principles.¹⁶

19. The PJM IMM proposes compromise language that would provide black start owners the opportunity for cost recovery with Tariff language targeted to solve the alleged problem and that would avoid instituting a piecemeal approach to ratemaking:

If a Black Start Service Provider seeking to recover costs for a Black Start Unit under paragraph 6 (i) is unable to sufficiently document its costs for such unit and (ii) was receiving payment under paragraph 5 for services provided by such unit as of May 15, 2010, then the Black Start Service Provider may add an amount up to its Black Start Unit Capacity times net CONE times the Black Start allocation factor (X) for its technology type up to a maximum of 50 MW for diesel or CT units, or 100 MW for hydro units as a proxy for all of its costs (whether sufficiently documented or not) other than costs incurred solely for the purpose of meeting NERC Reliability Standards. Black Start Units not meeting all of the preceding criteria are eligible for recovery of costs under paragraph 6 solely to the extent that a Black Start Service Provider can sufficiently document such costs.¹⁷

The PJM IMM believes that this compromise approach would compensate black start service units essentially as requested but would avoid the flawed elements of PJM's filing.

20. The PJM IMM states that to preserve separation between the formula rates and the Commission-approved rate, the Tariff should contain an existing proviso that, "The Transmission Provider will presume that any FERC-approved cost recovery plan would be the exclusive basis for the recovery of a black start unit's recovery of its costs during the applicable term."¹⁸ The PJM IMM notes that PJM's filing proposes to delete this language. The PJM IMM believes that this would permit a black start service provider to collect the Commission-approved rate, and, within the term specified for the Commission-approved rate, collect for the same service additional amounts provided under the formula rate. The PJM IMM states that the proposed revisions specifically allow for the recovery under the following formula: (FERC-approved rate) +

¹⁶ *Id.* at 6-7 (citing *Carolina Power & Light v. FERC*, 806 F.2d 1097 (D.C. Cir. 1988) (*Carolina Power & Light*) and *Florida Power & Light Co. v. City of Miami*, 92 F.2d 180, 183 (5th Cir. 1938)(*FPL*)).

¹⁷ *Id.* at 7-8.

¹⁸ *Id.* at 9.

(Incremental Black Start Capital Costs * CRF) which the PJM IMM believes is another example of prohibited piecemeal ratemaking because if a black start service provider wants to change a Commission-approved rate, the owner must file to change that rate with the Commission. The PJM IMM states that the Tariff should not provide for changes to rates separately approved by the Commission, even if the adjustment to the Commission-approved rate is subject to review by the PJM IMM.¹⁹ For the above reasons, the PJM IMM recommends that the proposed revisions be rejected. The PJM IMM states that if any change is appropriate, it would be to explicitly bar additional recovery under Schedule 6A formula rates when there is existing recovery under a comprehensive Commission-approved rate.²⁰

21. The PJM IMM states that PJM's filing claims, "the black start unit owner could be forced to recover relatively inconsiderable expenditures, and provide black start service, over a discordant amount of time based upon the life of the unit as opposed to life of the improvement itself."²¹ The PJM IMM states that the purported problem does not exist, and PJM's filing proposes a confusing approach to cost recovery that requires assessing a useful life for each investment component. Black start unit owners may receive payments at their election based upon a cost-based rate or an incentive rate. The PJM IMM states that if investment costs are small, the rational choice is to recover under the incentive rate; however, cost-based recovery makes sense when capital investments are relatively large since a cost-based rate would be greater than the incentive rate. The PJM IMM states that PJM's filing does not demonstrate the logical connection between the proposed revision and the problem that it purports to solve and does not identify an actual problem. The PJM IMM states that the primary effect of these provisions is to replace levelized recovery of an aggregate investment with an accelerated recovery based on the life of certain components which in turn permits a black start service provider to prematurely terminate cost-based recovery, to terminate the obligation to provide black start service for the life of the investment, and return to incentive recovery. The PJM IMM provides a two part mathematical example to show that the actual effect is to provide black start unit owners a windfall. In the first part of the PJM IMM's example, unit A desires to recover new investments in black start equipment in three components with varying amounts and recoverable periods and the unit owner recovers the same amount over six years, \$1,750,000, whether the total cost of service is recovered on a levelized basis or an accelerated basis as result of breaking the investments into components. The PJM IMM states that the proposed provision which allows the black

¹⁹ *Id.* at 9-10.

²⁰ *Id.* at 10.

²¹ *Id.*

start owner the option to revert from cost-based to incentive rate recovery at will provides black start unit owners with a windfall. This potential outcome is illustrated in the second part of the PJM IMM's example where terminating cost-based recovery in year 3 during the same 6 year period, the black start unit owner is paid an additional \$290,000. The PJM IMM states that this windfall is the result of improper blending of cost-based and incentive-based recovery during the commitment period. The PJM IMM believes the proposed provision that allows such payments should be rejected as unjust and unreasonable.²²

C. Answer of PJM

22. PJM maintains that the proposed revisions do nothing more than offer an alternative approach for black start unit owners to recover their incremental costs associated with providing black start service in exchange for a commitment to provide black start service in the future, without allowing the opportunity for inappropriate cost recovery.²³ PJM believes that the offered revisions are consistent with, and enhance, the reforms offered in the PJM's 2009 Filing and provides reasonable opportunities for black start unit owners to recover their costs of providing black start service. PJM states the revisions to Schedule 6A allow additional methods of incremental cost recovery which were not available in the reforms set forth in PJM's 2009 Filing, but maintain the appropriate distinction between providing a return of costs and incentive payments.²⁴

23. PJM states that the PJM IMM's position has been premised on a mischaracterization of the black box calculation of fixed costs as an incentive rate; however, PJM believes that the Base Formula Rate is a pure black box calculation of capital costs which was crafted to provide a return to black start providers based upon an approximation of fixed costs. PJM states that while the black box calculation may or may not closely match costs, it can hardly be described as an incentive rate since it was designed to provide the black start unit owner a return of its investment. While the PJM IMM would seek to characterize the black box calculation of capital costs as an incentive rate, PJM states it was clearly intended by PJM stakeholders as a proxy for black start capital costs which were either difficult or burdensome to calculate. PJM states that the proposals of its filing do not allow a black start unit owner to receive any more of an incentive rate than it was entitled to in previous iterations of the black start

²² *Id.* at 11-14.

²³ PJM Answer at 5.

²⁴ *Id.*

service cost recovery rates, and should not be a basis for the rejection of the proposed modifications.²⁵

24. PJM states that the notion of blurring incentive and cost based recovery is really not at issue here; instead the question centers on whether allowing the unit owner to recover documented new capital costs, in addition to any of its historical costs, is appropriate. PJM states that the PJM IMM has objected to allowing a black start unit owner the ability to document new, incremental capital costs and include them with its historical cost recovery rate, whether it is a previously-approved Commission rate, or through application of the proxy cost rate. PJM states that the additional methodologies to allow a black start unit owner to seek cost recovery of capital improvements contemplate the addition of new improvements to the black start unit which, ultimately, contribute to that unit's overall value.²⁶ PJM believes that the new value of the black start unit, with the necessary additional capital improvements, would not be accounted for in either the legacy proxy calculation of fixed costs or a previously approved Commission rate since the existing rate recovery for the unit would only provide a return for the unit without additional capital improvements; therefore a unit owner should not be required to submit a base rate proceeding for each unit it seeks to improve to include known capital costs.²⁷

25. PJM states that the PJM IMM offers two hypothetical examples which purport to show that a savvy black start unit owner could garner a windfall by terminating component based cost recovery after it has received partial recovery for several high costs capital improvements. PJM believes that the PJM IMM's analysis is flawed since the actual inputs to the analysis are completely theoretical and have no basis in actual circumstances and is unlikely to be replicated in a real-life scenario. PJM states that the 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.

26. PJM states that the real purpose behind the proposed ability to allow a unit owner to revert to the base formula rate was to avoid a situation where the unit could be required to accept cost recovery payments that were insufficient to maintain the unit in black start service. In the case where an original black start unit was subject to a 15 year Capital Cost Recovery Rate, and decided in year 13 to install required CIP-specific equipment which carried a 5 year recovery term, the unit owner, upon reaching the initial 15 year

²⁵ *Id.* at 6-9.

²⁶ *Id.* at 9.

²⁷ *Id.* at 9-10.

maturity, could be faced with accepting *de minimis* payments which may prove insufficient to maintain the unit.²⁸

D. Answer of GenOn Parties

27. GenOn Parties state that the criticisms of the PJM IMM regarding this compromise proposal are unfounded on policy or legal grounds.²⁹ GenOn Parties believe that the changes the PJM IMM advocates would impose significant burdens upon existing black start generators that wish to continue to receive the compensation that they have historically received for providing black start services, and on new generators that would prefer to be compensated under the formula rate.³⁰ It is GenOn Parties' view that the proposed documentation requirements are entirely appropriate in light of the dollars at stake and the difficulty in developing the capital cost rate, especially for older units that may have changed ownership many times since their construction.³¹ While acknowledging legal precedent that prohibits an entity seeking a rate increase from doing so on a piecemeal basis and avoiding a re-examination of its base rate, it is GenOn Parties' contention that in the context of CIPS cost recovery for black start service providers, such precedent is inapposite.³²

28. It is unclear to GenOn Parties why the PJM IMM is opposed to the PJM filing when they contend it merely clarifies that the value should be Net CONE for the relevant region in which the black start generator is located; caps the number of MWs for which capital cost recovery may be received; and allows for a NERC-CIPS cost component to be recovered in addition to the formula rate. GenOn Parties contend that under the PJM IMM's proposed construct it will require new black start generators to prepare a rate case to receive compensation for their capital costs and old black start generators to demonstrate their inability to document these costs in order to justify continued receipt of the formula rate.³³ GenOn Parties assert that it is incorrect to suggest that there are no capital costs associated with the provision of black start service and that it is unaware of a generally accepted methodology for calculating the portion of a unit's cost of service

²⁸ *Id.* at 12-13.

²⁹ GenOn Parties Reply Comments at 1.

³⁰ *Id.*

³¹ *Id.* at 2.

³² *Id.*

³³ *Id.* at 3-4.

related to the provision of black start capital costs.³⁴ Moreover, given the revenue cap (based on the current Net CONE), it maintains it is burdensome to require such a necessity.³⁵

29. With regard to the PJM IMM's questioning the justification of a Fixed Black Start Service Component for older units which might be fully depreciated, GenOn Parties contend that these units provide a valuable service and in light of the limited compensation for this service, it would be unfair to force a generator to either forego the compensation to recover CIPS costs or spend thousands of dollars to prepare a cost of service study to justify these costs. They opine that PJM's filing is the more administratively efficient means of providing compensation for black start service.³⁶

30. Countering the PJM IMM's argument that the addition of the new component is a rate increase which triggers the necessity to document and review all capital costs recovered under the formula rate, GenOn Parties discount the precedent cited by the PJM IMM. First, in reference to *California Power & Light and FPL*, the GenOn Parties maintain that the *FPL* case is of limited precedential value as it concerns a municipality not subject to section 205 or the Commission's regulations and was decided in 1938. With regard to *Carolina Power & Light*, GenOn Parties opine that it is distinguishable in that it pertains to a FERC directive to the company to revise its cost of service data to reflect a reduction in the corporate tax rate.³⁷ By contrast, GenOn Parties assert that the Commission has recently held that additional investment incurred to address a reliability directive can be recovered as an adder to the public utility's transmission rate without reopening the underlying transmission base rate.³⁸ In further support of this contention, the GenOn Parties note the Commission's decision in *New York Independent System Operator, Inc.*, 109 FERC ¶ 61,372, *order on reh'g*, 111 FERC ¶ 61,182 (2005) (*NYISO*) where it accepted a rate mechanism that was limited to the recovery of transmission-related costs incurred to meet a reliability need separate from the transmission service charge and the transmission adjustment charged.³⁹ The GenOn Parties contend that the

³⁴ *Id.* at 4-5.

³⁵ *Id.* at 5.

³⁶ *Id.* at 5-6.

³⁷ *Id.* at 7.

³⁸ *Id.* at 8 (citing *Allegheny Power System Operating Companies, et. al*, 111 FERC ¶ 61,308 (2005), *reh'g denied*, 115 FERC ¶ 61,156 (2006) (*Allegheny*)).

³⁹ *Id.* at 8-9 (citing *New York Independent System Operator, Inc.*, 109 FERC ¶ 61,372 at P 28 (2004), *order on reh'g*, 111 FERC ¶ 61,182).

rate issues in the PJM filing are analogous to the rate issues in *Allegheny* and *NYISO* and likewise are distinguishable from traditional attempts by a public utility to obtain a limited rate increase.⁴⁰

E. Answer of PJM IMM

31. The PJM IMM objects to provisions for piecemeal cost adjustments to the incentive-based components of the formula rates for black start service provided in Schedule 6A to the OATT and to provisions disassociating the period of cost recovery from the period of service obligation.⁴¹ The PJM IMM states that these provisions remain unsupported and contradict the carefully developed approach to fairly compensate black start service approved by the Commission in 2009; therefore these provisions should be rejected, or the PJM IMM's compromise proposal should be accepted in their place.⁴² The PJM IMM is not aware of a case where a rate component entirely based on an incentive has been subject to a cost-based piecemeal adjustment when an alternative approach allowing recovery entirely on the basis of cost is available and states that no party has produced such a precedent or explained why it is appropriate. The PJM IMM states that GenOn does not attempt to defend the loophole in the proposal that introduces the potential for a mismatch of cost recovery periods and service obligations which could create a windfall.⁴³ The PJM IMM further notes that PJM does not disagree with the problem identified by the PJM IMM, defend its reasonableness, or propose a solution.⁴⁴

32. The PJM IMM states that its proposal, which GenOn never addresses, would provide exactly the same compensation as would be provided in the proposal GenOn drafted and PJM filed.⁴⁵ The PJM IMM's compromise proposal would explicitly permit GenOn to use a cost proxy calculated in exactly the same manner as Fixed BSCC under the incentive rate in paragraph 5. The difference between the PJM IMM's version and GenOn's version is that it explicitly specifies that Fixed BSCC serve as a cost proxy. The PJM IMM believes this facilitates future understanding of the nature and purpose of the rule and avoids setting a harmful precedent since the pleadings in this proceeding are

⁴⁰ *Id.* at 9.

⁴¹ PJM IMM Answer at 1.

⁴² *Id.*

⁴³ *Id.* at 4-5.

⁴⁴ *Id.* at 5.

⁴⁵ *Id.* at 4.

evidence of the potential for confusion. The PJM IMM believes that GenOn does not appear to oppose, on the substantive merits, the PJM IMM's desire for clarification that the Fixed BSCC component at issue here is a cost proxy. Another point of difference noted by the PJM IMM is GenOn's refusal to reasonably limit use of this proxy when it is no longer needed. The PJM IMM's states that this limit does not affect any of the units that GenOn currently owns and it is difficult to understand GenOn's objections to the PJM IMM's formulation.⁴⁶

F. Deficiency Letter

33. On October 31, 2011, the Commission requested additional information regarding PJM's filing. Specifically, the Commission sought answers to the following 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.

(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.

(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.

(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.

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

(6) PJM states at page 13 in its October 10, 2011 Answer to the Protest of the Independent PJM IMM 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

⁴⁶ *Id.*

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.

G. PJM’s Response to the Deficiency Letter

34. PJM responded to staff’s deficiency letter on November 14, 2011 (November 14 Response). PJM states that 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 and capacity value, and not upon documented actual cost incurrence. PJM states that 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; 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.⁴⁷

35. PJM states that 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. 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; therefore a unit owner should have a reasonable opportunity to recover those costs.⁴⁸

36. PJM states that 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. The allowance is for black start training activities involving restoration drills and procedure review activities that plant operating staff conduct throughout the year. According to PJM, these activities are not related to NERC-CIP Reliability Standard compliance and the formula was not altered to recover any NERC-CIP training expenses. PJM further notes that the incentive factor (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

⁴⁷ November 14 Response at 2.

⁴⁸ *Id.* at 3.

black start service for a term of two years as set forth in paragraph, or section, 5 of Schedule 6A.⁴⁹

37. PJM answers that not all black start unit owners have opted to establish their black start revenue requirements pursuant to a FERC-approved rate, and that the formulaic component of the Capital Cost Recovery Rate would not be applicable to those unit owners; therefore the definition of FERC-approved rate includes the caveat (if applicable)⁵⁰.

38. PJM states that 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 is paragraph 17 which requires that the unit owner submit supporting data and documentation of its costs to the PJM IMM and PJM for evaluation and, ultimately, approval. In this process, the PJM IMM 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 PJM IMM does not agree with the determinations resulting from this review, either party may petition the Commission to determine the appropriate revenue requirement. Another process included in paragraph 20 provides for 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 thirty 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 PJM IMM to review the documentation supporting the incremental costs; moreover, in proposed paragraph 21, the PJM IMM will be required to include a black start service summary in its annual State of the Market report. This additional summary will include 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.⁵¹

H. PJM IMM's Comments on PJM's Deficiency Letter Response

39. The PJM IMM states that the November 14 Response fails to respond to the request of the first question of the deficiency letter since it provides no documentation/examples of costs that cannot be documented. The PJM IMM argues that

⁴⁹ *Id.* at 4.

⁵⁰ *Id.* at 5.

⁵¹ *Id.* at 5-6.

“because the purpose of the filed proposal, as the transmittal letter states (at 4) is to avoid ‘substantial time and effort to calculate, and document, the non-NERC related capital costs,’ the failure to provide even one example deprives the filed proposal of an evidentiary foundation.”⁵² The PJM IMM’s focus has been on the need to require new black start units recovering costs under paragraph 6, which concerns cost-based recovery, to document all incremental capital costs for providing black start service regardless of whether they are related to compliance with NERC CIP Reliability Standards. The PJM IMM intended that its compromise proposal would ensure that new unit owners document all black start costs and refrain from using a cost proxy because they would have ample notice in the Tariff of the need to document and preserve records relating to all black start capital expenses. The PJM IMM believes that a requirement to recover costs initially under paragraph 6 would make sound policy for a completely new black start investment.⁵³

40. The PJM IMM states that under PJM’s approach, the cost proxy never expires; therefore a black start unit owner would eventually over recover. The PJM IMM states that PJM’s November 14 Response also fails to refute the specific scenario identified by the PJM IMM that could result in over recovery by a black start service provider inappropriately switching between cost recovery under paragraph 6 and incentive recovery under paragraph 5. The PJM IMM believes its alternative compromise proposal eliminates the flawed proposed tariff revisions that would allow this scenario for over recovery; but asserts that the best approach to avoid over recovery would be to reject the proposal and preserve the current arrangement unless and until the Commission has evidence that the current arrangement is deficient.⁵⁴

41. The PJM IMM agrees with the November 14 Response that the intent is to include only capital costs for CIPS compliance and that training costs are not appropriately included among such capital cost; however, inclusion of an explicit provision would help to avoid confusion on this point. The PJM IMM agrees with the November 14 Response that the incentive factor Z does not apply to black start unit recovery under paragraph 6.⁵⁵

42. The PJM IMM states that with the inclusion of the phrase, “if applicable,” the proposed tariff revisions would allow the formula rates to modify, without any further opportunity for review or approval by the Commission, rates for black start service

⁵² PJM IMM Response to Deficiency Letter at 1.

⁵³ *Id.* at 2.

⁵⁴ *Id.* at 3.

⁵⁵ *Id.*

separately and specifically approved by the Commission. Despite having opted out of the Schedule 6A formula rate structure, this provision allows the owner to opt back in, with no additional opportunity for the Commission to ensure that rates approved in its separate proceeding are consistent with the results from applying the formula rate. Therefore the PJM IMM argues that this is an improper approach to ratemaking.⁵⁶

43. Responding to Question No. 6 of the Deficiency Letter, the PJM IMM states that it has no authority, and should have no authority, to alter the terms for applying a formula rate; consequently, those terms must build in appropriate safeguards or they should not be approved. The PJM IMM further states that the November 14 Response offers no explanation of any appropriate safeguards that would prevent the potential windfall identified by the PJM IMM. The PJM IMM notes that it is the overly complicated and conflicted language proposed that creates the need for such safeguards. The PJM IMM states that the proposed revisions to the formula rate should be rejected since the potential windfall identified by the PJM IMM is not a problem in the current rules.⁵⁷

I. PJM's Answer

44. PJM states that new black start units would be required to document all capital costs of black start equipment; otherwise, the black start unit owner would be limited to recovery under the proxy Base Rate Formula which, presumably, would be insufficient to adequately and reasonably compensate the black start unit owner for its costly investment.⁵⁸ PJM states that the proxy cost Base Formula Rate assumes token ongoing capital investment and was never intended to provide recovery for significant capital expenditures that might be needed to allow the unit to operate in compliance with mandatory reliability standards and was previously considered reasonable means to compensate for historic and capital costs.⁵⁹ PJM also states that the proposed tariff revisions do not contemplate allowing PJM or the black start unit owner the ability to restructure or modify any prior existing FERC-approved rate for black start service.⁶⁰

⁵⁶ *Id.* at 4.

⁵⁷ *Id.* at 4-5.

⁵⁸ PJM December 16 Response at 2-3.

⁵⁹ *Id.* at 4.

⁶⁰ *Id.* at 5.

IV. Discussion

A. Procedural Matters

45. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2011), the timely, unopposed motions to intervene serve to make those entities that filed them parties to this proceeding. Pursuant to Rule 214(d),⁶¹ the Commission will grant the untimely, unopposed motions to intervene of Exelon Corporation, Duke Energy Corporation, and GenOn Parties given their interest in the proceeding, the early stage of this proceeding, and the absence of undue prejudice or delay.

46. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2011), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept the answers of GenOn Parties, PJM, and the PJM IMM because each has provided information that assisted us in our decision-making process.

B. Commission Determination

47. As discussed below, the Commission accepts PJM's proposed Tariff sections, to be effective November 1, 2011, as requested, subject to conditions as discussed below.

48. PJM states that while the PJM IMM would seek to characterize the black box calculation of capital costs as an incentive rate, it was clearly intended by PJM stakeholders as a proxy for black start capital costs which were either difficult or burdensome to calculate. PJM also states that 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; 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. PJM believes that the 2009 revisions 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; therefore a unit owner should have a reasonable opportunity to recover those costs. The proposed formulas are consistent with, and enhance, the revisions approved by the Commission in PJM's 2009 Filing and provides a just and reasonable method for black start unit owners to recover their costs of providing black start service. We agree that black start unit owners should be able to recover their

⁶¹ 18 C.F.R. § 385.214(d) (2011).

incremental costs associated with providing black start service in exchange for a commitment to provide black start service in the future (which can be longer than the 2 year commitment under the Base Formula Rate) while affirming that the costs being submitted for recovery are required to satisfy applicable CIP-specific NERC Reliability Standards and having the PJM IMM validate those costs.

49. With regard to the Capital Cost Recovery Rate – NERC-CIP Specific Recovery formula, the PJM IMM argues that PJM’s filing inappropriately and unnecessarily blends cost and incentive based rates by creating a special adder relating to one particular type of cost and levies it on top of the Base Formula Rate; and this approach amounts to ad hoc and piecemeal ratemaking, which is prohibited under longstanding traditional ratemaking principles. Regarding the Capital Cost Recovery Rate formula, the PJM IMM states that the Tariff should not provide for changes to rates separately approved by the Commission, even if the adjustment to the Commission-approved rate is subject to review by the PJM IMM, and thus, the proposed revisions should be rejected.

50. In a Statement of Policy issued September 14, 2001, the Commission provided assurances to regulated entities that the Commission “will approve applications to recover prudently incurred costs necessary to further safeguard the reliability and security of our energy supply infrastructure in response to the heightened state of alert. Companies may propose a separate rate recovery mechanism, such as a surcharge to currently existing rates or some other cost recovery method.”⁶² The Commission has stood by this policy and clarified that the policy extends to the recovery of prudent reliability expenditures, including those for vegetation management, improved grid management and monitoring equipment, operator training and compliance with NERC standards.⁶³ The Commission recognized that its Policy Statement benefits citizens by providing clarity about the agency’s policies to support and take steps under existing law to enhance transmission grid reliability.⁶⁴ Because black start service is critical to maintaining grid reliability, the Commission finds that PJM’s proposal to add costs related to NERC-CIP Reliability Standards in the Capital Cost Recovery Rate – NERC-CIP Specific Recovery formula and the Capital Cost Recovery Rate formula is just and reasonable.

⁶² Extraordinary Expenditures Necessary to Safeguard National Energy Supplies, 96 FERC ¶ 61,299, at 61,129 (2001).

⁶³ Policy Statement on Matters Related to Bulk Power System Reliability, 107 FERC ¶ 61,052 (2004) at P 28.

⁶⁴ *Id.* at P1.

51. The PJM IMM states that the division of cost of service into separate components and revisions, which allow a black start unit to revert from cost-based recovery to recovery under the Base Formula Rate, is to replace levelized recovery of an aggregate investment with an accelerated recovery based on the life of certain components which in turn permits a black start service provider to prematurely terminate cost-based recovery, to terminate the obligation to provide black start service for the life of the investment, and to return to the Base Formula Rate which only requires a two year commitment. The PJM IMM also maintains that this proposal can lead to over recovery because it permits a black start unit a non-revocable opportunity to change from cost-based to incentive based rate recovery. The PJM IMM argues that this proposal allows the unit to recover greater costs by prematurely terminating cost based recovery and returning to recovery under the Base Formula Rate. The PJM IMM provides an example showing that an owner making several investments with different depreciation periods would be able to recover a greater amount of revenue by terminating cost based recovery and returning to recovery under the Base Formula Rate.

52. PJM argues that the PJM IMM's analysis is flawed since the actual inputs to the analysis are completely theoretical and have no basis in actual circumstances, and PJM maintains this scenario is unlikely to be replicated in real-life. PJM argues that this proposal is designed to ensure that Black Start units are not faced with a situation in which they would be required to accept cost recovery payments that were insufficient to maintain the unit in black start service. PJM provides, as an example, a case where an original black start unit was subject to a 15-year Capital Cost Recovery Rate, and decided in year 13 to install required CIP-specific equipment which carried a 5-year recovery term. Without the ability to revert to the Base Formula Rate, the unit owner, upon reaching the initial 15-year maturity, PJM maintains the owner could be faced with accepting *de minimis* payments which may prove insufficient to maintain the unit.

53. While PJM states the concern of the PJM IMM with regard to the premature return to the Base Formula Rate from cost based rates to create a windfall or over recovery is unlikely, it has not stated that it cannot occur or justified why the scenario has no basis in actual circumstances. Nor has PJM questioned the mathematical accuracy of PJM IMM's calculation. PJM has not shown how its proposed review process would prevent the over recovery from occurring or why a potential reduction in the black start commitment period by switching to the Base Formula Rate would not cause a reliability problem. The Commission finds that the PJM IMM's concern is legitimate with regard to the revisions which allow a black start unit to switch from an accelerated cost based rate to recovery under the Base Formula Rate.

54. The Commission will accept PJM's alternative method of calculating the Capital Cost Recovery factor, since basing recovery on the life of the investment is a reasonable method of cost recovery. However, given the potential demonstrated by the PJM IMM for a unit owner to increase recovery through changing cost recovery methods, we cannot

find that this aspect of PJM's proposal is just and reasonable. We therefore will accept the filing conditioned on PJM removing the ability to make the non-revocable election in paragraph 18 of Schedule 6A, providing a detailed justification of the need for the non-revocable election in light of the PJM IMM's example showing potential over recovery, or filing a mechanism that will permit changes in rate recovery that are legitimate without allowing such changes that will lead to over recovery.

55. In response to the deficiency letter, PJM has clarified that 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. Since PJM's Tariff does not state this, the Commission requires that PJM, as part of its compliance filing revise its Tariff to specify that the incentive factor (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. PJM has also clarified that the proposed tariff revisions do not contemplate allowing PJM or the black start unit owner the ability to restructure or modify any prior existing FERC-approved rate for black start service; therefore the Commission will accept the filing on condition that PJM revise its Tariff to make clear that neither PJM nor a black start unit owner has the ability to restructure or modify any prior existing FERC-approved rate for black start service.

The Commission orders:

(A) PJM's proposed Tariff sections are hereby accepted to become effective November 1, 2011, subject to conditions, as set forth in the body of this order.

(B) PJM is directed to submit a compliance filing within 30 days of the date of this order with its response to the conditions.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.