FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, DC 20426

OFFICE OF THE COMMISSIONER

August 27, 2014

The Honorable Ed Whitfield, Chairman
Subcommittee on Energy and Power
Committee on Energy and Commerce
U.S. House of Representatives
2125 Rayburn House Office Building
Washington, D.C. 20515

Dear Representative Whitfield:

Thank you for the opportunity to appear before the Subcommittee on Energy and Power on Tuesday, July 29, 2014. Attached are my responses to the Supplemental Questions for the Record posed by members of the Committee.

Sincerely,

[redacted]

Norman C. Bay

Commissioner

ADDITIONAL QUESTIONS FOR THE RECORD
FOR COMMISSIONER NORMAN C. BAY

QUESTIONS FROM THE HONORABLE ED WHITFIELD

1. How many times did you or your staff meet with EPA to discuss the Clean Power Plan proposal?

Answer: The Environmental Protection Agency ("EPA") issued its Clean Power Plan proposal in June 2014. At that time, I was the Director of the FERC's Office of Enforcement. In my duties as Director of the Office of Enforcement, neither I, nor my staff, had any consultation with EPA regarding the proposal.

2. Do you view EPA's proposed Clean Power Plan as an "energy plan" or a "pollution control" rule? Please explain your response.

Answer: The Supreme Court has upheld the designation of greenhouse gas emissions as a form of pollution under the Clean Air Act, *Massachusetts v. EPA*, 549 U.S. 497, 532 (2007). The Clean Power Plan establishes pollution control guidelines for states to follow in developing plans to address greenhouse gas emissions from existing electric generating units. That being said, state plans developed in response to the Clean Power Plan will have implications for existing electricity infrastructure.

3. Would you agree that the proposed Clean Power Plan gives EPA a certain amount of control over State decisions regarding the generation, supply and consumption of power, particularly if State renewable energy and efficiency programs are included in an EPA-approved State Implementation Plan?

Answer: In establishing state-specific emission goals and guidelines for the development of state implementation plans, the Clean Power Plan may well influence state decisions regarding the generation, supply and consumption of power. The EPA's proposal offers broad flexibilities that allow states to design state implementation plans that ensure resource adequacy and reliability. The proposal does not impose plant-specific requirements. Nor does it require compliance until 2020, and states have flexibility over a ten-year period through 2029 to reach their overall emission rate target. Much will depend upon the state plan, and the state's efforts to implement its plan.

4. As the D.C. Circuit recently held, FERC lacks authority to dictate how States plan and operate their energy systems. Are you aware of any statutory authority that permits EPA to mandate that States restructure their electric systems and subject State energy decisions to federal oversight and control.

Answer: I understand your question to refer to *Electric Power Supply Ass'n v. FERC*, Nos. 11-1486, *et al*. (D.C. Cir. May 23, 2014), in which the D.C. Circuit found that demand response was a component of the retail energy market and beyond the scope of the Commission's direct regulation. FERC's petition for rehearing *en banc* of that ruling is pending before the Court. Nonetheless, the D.C. Circuit and Supreme Court have recognized that FERC has the authority to regulate matters within its jurisdiction, even if doing so would preempt state law under the

Supremacy Clause of the Constitution. It is my understanding that the Clean Power Plan is premised upon the EPA's authority under section 111(d) of the Clean Air Act, and any questions regarding that authority will ultimately be resolved by the courts.

5. To what extent does FERC have authority over State utility and resource planning? Are you aware of any statutory authority giving EPA greater authority in this area than FERC?

Answer: Under the Federal Power Act, FERC is charged with regulating the wholesale sale and transmission of electric energy, primarily by ensuring that the energy is provided at a just and reasonable rate. *See* 16 U.S.C. § 824d(a). The Commission also possesses jurisdiction over practices affecting or relating to the rates for such sale and transmission. *See* 16 U.S.C. § 824e(a). Under the Act, states retain the right to regulate the facilities responsible for the generation of electric energy. In carrying out its statutory responsibilities, the Commission may regulate practices affecting wholesale rates, even if those determinations touch on matters subject to state authority. I have not examined the scope of the EPA's authority under the Clean Air Act or any of the other statutes it administers.

6. EPA projects nearly 180 gigawatts of generation capacity will retire between 2010 and 2020 in response to the Clean Power Plan and other factors, such as EPA's previously finalized Mercury and Air Toxics (MATS) rule. What do you view as the potential reliability impacts resulting from the loss of 180 gigawatts of generation over the next 6 years.

Answer: Addressing potential reliability impacts depends upon good communication and planning by and among key stakeholders, including FERC, EPA, DOE, state officials, NERC, RTOs/ISOs, and industry. Currently, the RTOs/ISOs, which serve more than half the United States, do reserve margin planning, states do resource adequacy planning, and NERC does reliability studies as well. FERC staff has also worked with EPA staff and can provide technical assistance to the EPA. I note that the ISO/RTO Council, a national organization of electric grid operators, has offered analytic support to the states in designing programs that maintain the reliability of the bulk power system. In addition, because the Clean Power Plan does not require any compliance until 2020, and gives states flexibility over a ten-year period to reach their overall emission rate targets, I believe that the proposal will empower states to design implementation plans that ensure resource adequacy and reliability.

7. Would you be supportive of EPA including in its final Clean Power Plan a "reliability safety valve" that provides FERC greater authority to prevent the retirement of reliability critical generating units? What might such a safety valve look like?

Answer: Under the EPA's rules on power plant emissions of mercury and air toxics (MATS), there is a "reliability safety valve" that allows "fourth-year" extensions of compliance obligations in many circumstances. A "fifth-year" extension can also be granted when needed for reliability, and the EPA may seek input from the Commission and others on reliability issues. I believe that a reliability safety valve should be considered by the EPA.

8. Has EPA advised you about how the Clean Power Plan would work in states with multiple Regional Transmission Organizations (RTOs) or states with RTO members and non-RTO members or state with no RTO members. If yes, how would the plan work according to EPA?

Answer: I have not had any discussions with EPA regarding the implementation of the Clean Power Plan. I believe, however, that these issues and others relating to the practical implementation of the Clean Power Plan will need to be discussed among FERC, EPA, DOE, state officials, NERC, RTOs/ISOs, and industry.

9. EPA analyzed a set of compliance scenarios referred to as "Regional" scenarios. The regional scenarios allow emission rate averaging across affected sources within six multi-state regions, informed by North American Electric Reliability Corporation (NERC) regions and Regional Transmission Organizations (RTOs). What role does FERC see for itself in overseeing such regional compliance efforts?

Answer: With respect to any role FERC may have in overseeing regional compliance efforts, please see Chairman Cheryl LaFleur's response.

10. Do you support the President's Climate Action Plan? Do you believe the President's plan is necessary to mitigate the impacts of climate change? Do you believe EPA's proposed Clean Power Plan is necessary to mitigate the impacts of climate change?

Answer: I personally believe that greenhouse gas emissions contribute to climate change. I further believe that the failure to act poses serious risks. The President's Climate Action Plan is a blueprint for action to slow the effects of climate change. That said, the Commission is a creature of statute and must respect the authority given to it by Congress. Under that authority, the Commission is an economic regulator, not an environmental one.

11. During the hearing, in response to a question from Rep. Rush regarding potential challenges from EPA's Clean Power Plan, you stated:

I think that there could be challenges, but I think that the challenges are manageable. I would note, for example, that with the 2005 baseline that the EPA used, there has already been a 15% reduction in carbon emissions from generators so that an additional 15 percent needs to be achieved over the next 16 years.

a. Do you now understand that the emissions rate baseline used by EPA is actually 2012, and not 2005?

Answer: In discussing the "2005 baseline," I was referring to EPA's projections that the proposed rule will achieve a thirty percent reduction in CO_2 emissions from the electric sector by the year 2030, relative to year 2005 levels. (*See* 79 Fed. Reg. at pp. 34832, 34839).

It is my understanding that the Clean Power Plan would use 2012 emission data as an input in calculating the proposed goals for state implementation plans. In particular, the methodology used to compute each state's proposed goal begins by compiling data from total annual quantities of CO_2 emission, net generation, and capacity from reported 2012 data.

b. Wouldn't you agree that a 2012 baseline makes compliance a considerably heavier lift than a 2005 baseline? Why or why not?

Answer: As noted in my previous response, my testimony referred to EPA's projections that the proposed rule will achieve a thirty percent reduction in CO_2 emissions from the electric sector by the year 2030, relative to year 2005 levels. I do not believe that the use of 2012 emission data in calculating the proposed goals for state implementation plans would necessarily affect the ability of the proposed rule to reach the projected level of emission reductions. The EPA's proposal offers states broad flexibility in designing implementation plans. In addition, the proposal does not require any compliance until 2020, and gives states flexibility over a ten-year period through 2029 to reach their overall emission rate targets.

12. You stated during your confirmation hearing on May 20 that, with respect to EPA's Clean Power Plan, you would "try to assess what the reliability impacts are and what FERC can do working with key stakeholders, like EPA, States, the State Commissioners, NARUC, RTOs, ISOs and industry to assure that there is sufficient planning and preparation and discussion that any challenges can be met."

a. Now that the rule has been out for several weeks, what conclusions do you have about its impact on reliability and rates.

Answer: It is premature, at this point, to draw any firm conclusions regarding the Clean Power Plan's impact upon reliability and rates. The EPA is still taking comments, and the rule has not been finalized. In addition, any potential impacts depend on the state plans developed in response to the rule. In that regard, the Clean Power Plan offers broad flexibilities that will empower states to design plans that ensure resource adequacy and reliability. As I testified before the Committee, implementation of the Clean Power Plan could present challenges, but the key to addressing those challenges is good communication and planning by key stakeholders.

b. Have you discussed the rule with anyone at the EPA? Please provide details with respect to any such conversation(s)?

Answer: I have not had any discussions with EPA regarding the Clean Power Plan.

13. Do you intend to identify for us the general circumstances and cases which you may consider recusing yourself from, and the results of those considerations? During your confirmation process, you identified 43 cases which might be subject to recusal. How are we going to know the disposition – and more importantly the extent – of those potential recusals?

Answer: My recusal decisions will be guided by the Standards of Conduct for Employees of the Executive Branch. *See* 5 CFR Part 2635. Under the Standards of Conduct, employees must recuse themselves to avoid conflicting financial interests (5 CFR § 2635.401 and 402), or loss of impartiality based on personal and business relationships (5 CFRR § 2635.501 and 502). Employees must also avoid actions that would give the appearance of an ethical violation. The ethics regulations provide specific criteria for determining whether a recusal is required. My recusal decisions on all matters will be guided by the applicable regulations, and by consultations

with FERC's Designated Agency Ethics Official and any other appropriate officials, and will be made on a case-by-case basis.

The 43 cases identified in my prior testimony reflected the number of pending investigations in the Office of Enforcement at the time of my confirmation. Under the most expansive potential application of the ethics rules, this appears to be the largest set of proceedings from which I could possibly need to recuse myself. In the event recusal is necessary, any published Commission orders relating to those proceedings would note that I did not participate in the consideration of the matter. I have already recused myself from several matters and will continue to do so, as appropriate.

QUESTIONS FROM THE HONORABLE JOE BARTON

1. I am concerned by FERC's practice of withholding evidence and information from the subject of investigation in cases of alleged energy market manipulation.

a. Please define market manipulation. Can an action deemed "market manipulation" follow the letter of the law but not the spirit? Please provide an example.

Answer: The Commission's definition of market manipulation is set forth in the Anti-Manipulation Rule (18 C.F.R Part 1c), the Commission's Order No. 670 implementing that Rule, and precedent developed under the Rule. In Order No. 670, the Commission set forth the requirements for finding a violation of the Anti-Manipulation Rule: "The Commission will act in cases where an entity: (1) uses a fraudulent device, scheme or artifice, or makes a material misrepresentation or a material omission as to which there is a duty to speak under a Commission-filed tariff, Commission order, rule or regulation, or engages in any act, practice, or course of business that operates or would operate as a fraud or deceit upon any entity; (2) with the requisite scienter; (3) in connection with the purchase or sale of natural gas or electric energy or transportation of natural gas or transmission of electric energy subject to the jurisdiction of the Commission."

The Commission adopted the Anti-Manipulation Rule in order to implement Congress's prohibition against fraud and market manipulation as set forth in EPAct 2005, which was passed in the wake of Enron's manipulation of Western energy markets. The Commission's definition was patterned on the Securities and Exchange Commission's core anti-fraud and anti-manipulation rule – as EPAct 2005's prohibition against fraud and manipulation was patterned on and specifically references the Securities and Exchange Act of 1934. Although there are differences in the securities and energy markets, the Commission's enforcement-related matters look to securities law precedent on fraud and manipulation where applicable. Following the Commission's implementation of the Anti-Manipulation Rule, there have been numerous public settlements and orders that have explained, often in great detail, the scope and application of the rule.

In Order No. 670, the Commission stated: "If a market participant undertakes an action or transaction that is explicitly contemplated in Commission-approved rules and regulations, we will presume that the market participant is not in violation of the Final Rule." The Office of Enforcement did not recommend that the Commission settle any matter or authorize any enforcement action inconsistent with this principle during my time as Director of Enforcement– and the Commission did not take any action inconsistent with this principle during this time. It is also important to note that while a finding of market manipulation is not warranted when a subject acts in a manner that is explicitly contemplated in Commission-approved rules and regulations, it is also true that a finding of market manipulation does not require any violation of a specific market rule or tariff. The Commission has made this clear many times, including in the Order approving the *JP Morgan* market manipulation settlement (issued in July 2013). There, the Commission stated:

> Market manipulation under the Commission's Rule 1c is not limited to tariff violations. That Rule 1c is not so limited is by design. In the wake of Enron's schemes in the CAISO market, the Energy Policy Act of 2005 gave the Commission "broad authority to prohibit manipulation" and "an intentionally broad proscription against all kinds of deception, manipulation, deceit and fraud." Both the breadth of Congress' authorization to the Commission and the breadth of the Anti-Manipulation Rule itself are a response to what courts have long recognized: the impossibility of foreseeing the "myriad means" of misconduct in which market participants may engage. For that reason, as the Commission observed in 2006, "[N]o list of prohibited activities could be all-inclusive." Instead, as Order No. 670 emphasizes, fraud is a question of fact to be determined by all the circumstances of a case, not by a mechanical rule limiting manipulation to tariff violations. (Footnotes omitted)

So while a market participant should not be liable for acting in a manner that is explicitly contemplated in Commission-approved rules and regulations, the absence of a tariff violation is not a defense to market manipulation.

b. Is FERC required by law to provide the subject of investigation with the information it collected during the investigation?

Answer: In most FERC investigations, the vast majority of information collected comes from the investigative subject and its employees, and is therefore readily available to the subject. There is no legal requirement that the Commission provide subjects with information collected from third-parties during the investigation while the matter is still in the investigation phase. Nonetheless, the Office of Enforcement provides a subject with additional information (documents, depositions, data, etc.) during an investigation, including relevant third-party information, so that the subject is fully informed of Enforcement staff's legal and factual conclusions. Once the matter goes to litigation (whether in federal court or before an Administrative Law Judge), the Commission provides information to the subjects as required by court rules.

Further, in 2009, the Commission formalized its existing policy of disclosing to the subject of an investigation exculpatory evidence obtained in the investigation. This is known as the *Brady* policy, as it is modeled after the *Brady* Doctrine that applies in criminal proceedings. Although

the Commission recognized that there is no constitutional requirement to adopt such a policy in civil proceedings such as FERC enforcement investigations, and application of *Brady* principles varies among administrative agencies, the Commission determined that such a policy was important in ensuring a fair enforcement process. (In fact, my recommendation to the Commission that it adopt a formal *Brady* policy was one of my first initiatives as Director of the Office of Enforcement after I joined the Commission in July 2009.)

c. Is FERC required by law to respond to the legal and factual arguments raised by the subjects?

Answer: The Commission's longstanding policy and practice is to carefully consider a subject's legal and factual arguments when determining how to proceed in any given investigation. This is true throughout the investigation itself, including when Enforcement staff engages with subjects and their counsel during the Preliminary Findings process. It is also true once the matter proceeds to the Order to Show Cause phase, in which the subjects are informed of Enforcement staff's detailed findings and are given a full opportunity to make any arguments they would like to present for the Commission's consideration. The Commission's public decisions finalizing the Order to Show Cause process make clear that the Commission does respond to the legal and factual arguments raised by subjects. (A separate webpage linking to the Orders to Show Cause decisions post-EPAct 2005 can be found at: http://www.ferc.gov/enforcement/civil-penalties/show-case-orders.asp.) And, for matters that reach federal court or Administrative Law Judge proceedings, the Commission responds to subjects' legal and factual arguments consistent with court rules.

d. Does FERC have a Compliance Office to assist those who have every intention to comply with market manipulation laws and have legitimate questions about how to do so? Would you commit to opening a Compliance Office?

Answer: The Commission has numerous avenues open to market participants interested in obtaining compliance-related advice from Commission staff, including compliance with the Commission's Anti-Manipulation Rule. This includes the Compliance Help Desk, which is staffed by employees from numerous Commission offices and is available to market participants who wish to seek compliance-related advice. It also includes the No-Action Letter process, in which market participants may obtain written advice as to whether staff would recommend that the Commission take no enforcement action with respect to specific proposed transactions, practices, or situations. Market participants may also request declaratory orders, obtain guidance from general counsel opinion letters and accounting interpretations, as well as seek informal contact with staff. In addition, market participants who think they may have violated the Commission's Anti-Manipulation Rule may submit a self-report about the relevant conduct, which could result in a reduction of the otherwise applicable civil penalty (or, depending on the circumstances, no civil penalty). Because of the mechanisms and approaches described above, I do not believe there is a compelling reason for the Commission to create a separate Compliance Office. However, I am always open to considering new ideas that promote compliance with Commission-jurisdictional statutes, rules, and regulations.

QUESTIONS FROM THE HONORABLE DAVID B. MCKINLEY

1. This January, during the "Polar Vortex," electricity customers in the PJM region experienced significant abrupt increases in their electricity costs, with bills rising to several times their normal levels. These price spikes were caused, in part, by significant generation outages during January, despite these generation resources receiving billions of dollars a year in advanced payments in exchange for their being available to provide energy during peak periods, whether in the extreme heat of the summer or the extreme cold of the winter. I am concerned that the causes of this situation have not been understood well enough to prevent it from happening again. Do you think you fully understand what happened and can assure us it isn't going to happen again? Has the Commission conducted a comprehensive root cause investigation and analysis of the situation, or directed P JM or the PJM Independent Market Monitor ("IMM") to do so?

a. If yes, have those results been released publicly?

b. If no, why not?

Answer: On April 1, 2014, the Commission held a technical conference on Winter 2013/14 Operations and Market Performance in RTOs/ISOs to explore the impacts of the season's cold weather events on the RTOs/ISOs, and to discuss the responses of the RTO/ISOs and the Commission to those events (Docket No. AD14-8-000). During this conference, OE shared the preliminary findings from its review of the Polar Vortex events. At the Commission's invitation, thirty-five entities filed post-technical conference comments addressing the impacts of the cold weather events on the RTO/ISO markets. The Commission's technical conference and comprehensive review of the Polar Vortex events for manipulative or improper activity has assisted the Commission in better understanding the causes of the high natural gas and electricity prices during the events. The Commission may provide additional details related to its review of the Polar Vortex events in the future.

In addition, the Commission's Office of Enforcement (OE) regularly conducts surveillance of the natural gas and electric markets to detect potential market manipulation and other potentially improper conduct. Because of extreme price spikes during the "Polar Vortex" events, OE conducted an extensive review, in addition to its regular surveillance efforts, to look specifically for any manipulative or improper behavior that could have contributed to the high natural gas prices and elevated electricity costs. As a result of that review, OE has not found any manipulative activity that would have caused the high natural gas and electricity prices. Nevertheless, OE staff continues to examine whether market participants may have improperly benefitted from the unusually constrained conditions in the electric markets in violation of Commission's rules.

While the Commission has not directed PJM or its IMM to conduct an analysis of the Polar Vortex events, both have undertaken examinations of the events. The IMM is conducting its own independent review of the Polar Vortex events and has worked closely with OE to determine whether any market participants violated the PJM tariff. In addition, PJM analyzed the January 2014 Polar Vortex events and released a public report of its findings on May 9, 2014

(available at http://www.pjm.com/~/media/committees-groups/task-forces/cstf/20140509/20140509-item-02-cold-weather-report.ashx). This report describes PJM's efforts to maintain reliability, the challenges it faced in doing so, and some of the reasons for those challenges. In addition, the report outlines actions items to improve operations and market performance in the future.

2. What efforts has the Commission undertaken, or directed PJM and the IMM to undertake, to identify potential solutions to the generation performance problems that occurred during January 2014 in the PJM region?

Answer: As noted in my response to Question 1, the Commission held a technical conference on Winter 2013/14 Operations and Market Performance in RTOs/ISOs on April 1, 2014 to explore the impacts of the season's cold weather events on the RTOs/ISOs and to discuss action taken to respond to those impacts. Generator performance issues was one of the topics highlighted at this technical conference and in the post-technical conference comments, which were submitted by May 15, 2014. In addition, as part of its comprehensive review of the Polar Vortex events described above in my response to Question 1, OE has been working with the IMM to determine whether any generators violated any existing rules governing generator performance in PJM. If the Commission determines that any generators failed to perform in accordance with those rules, the Commission has the authority to impose penalties and to require disgorgement of any unjust profits.

Prior to the cold weather events this winter that highlighted generator performance issues, the Commission had commenced an inquiry into the centralized capacity markets in the eastern RTOs and ISOs, including PJM, to consider how their rules and structures are supporting the procurement and retention of resources necessary to meet future reliability and operational needs. This inquiry has also brought attention to generator performance issues, resulting in some RTOs/ISOs proposing rule changes. For example, the Commission recently approved a new "Pay for Performance" capacity market design in the New England region, which is expected to improve generator availability and performance by rewarding generators that are available during critical events on the grid with higher payments, while ensuring that generators that are not available during such events lose their capacity payments. In addition, PJM is considering similar revisions to its capacity market through its stakeholder process to improve generator availability and performance during periods of high demand on the grid.

3. Has the Commission determined whether any generation outages were reflective of attempts to manipulate market-clearing prices?

Answer: OE's review of the Polar Vortex events, as described in my response to Question 1, included a comprehensive review of generation outages. OE analyzed outage information from PJM and the IMM, interviewed generator operators regarding the circumstances surrounding their outages, reviewed information related to generation owners' asset portfolios to determine if they had financial incentives to manipulate by withholding generation, and collected and analyzed additional data from generator operators, when necessary. OE has not found any instances in which generator operators took outages to raise market-clearing prices.

4. We understand that the delivered price of natural gas rose to historic highs in the PJM region during January 2014, and that these unprecedented delivered prices for

natural gas were primarily the result of extraordinarily high prices for capacity on interstate natural gas pipelines in the PJM region. Has the Commission conducted a comprehensive root cause investigation and analysis, or directed PJM or the PJM Independent Market Monitor ("IMM") to conduct a comprehensive root cause investigation and analysis, of the unprecedented natural gas prices that surfaced in the PJM region during January 2014?

Answer: As noted in my responses to Questions 1 and 2, the Commission held a technical conference on Winter 2013/14 Operations and Market Performance in RTOs/ISOs on April 1, 2014 to explore the impacts of the season's cold weather events on the RTOs/ISOs and to discuss action taken to respond to those impacts. Natural gas prices were discussed at this technical conference and in the post-technical conference comments, which were submitted by May 15, 2014.

OE conducted an extensive review, in addition to its regular surveillance efforts, to look specifically for any manipulative behavior that could have contributed to the high natural gas prices during the cold weather events. OE interviewed natural gas suppliers, pipelines, and local distribution companies, analyzed physical natural gas transactions data, collected and analyzed additional information from market participants, and reviewed information related to natural gas market participants' financial positions to determine if they held financial incentives to increase natural gas prices. OE did not find any patterns of manipulative behavior that would have caused the high natural gas prices.

While the Commission has not directed PJM or its IMM to conduct an analysis of the Polar Vortex events, the IMM is conducting its own independent review of the Polar Vortex events. In addition, OE has worked closely with PJM and the IMM during its comprehensive review of the events.

a. If yes, have those results been released publicly?

b. If no, why not?

Answer: OE shared its preliminary findings related to its review of the Polar Vortex events at the Commission's Technical Conference on Winter 2013/2014 Operations and Market Performance in RTOs/ISOs on April 1, 2014. I am open to releasing additional information relating to this review in the future.

5. What efforts has the Commission undertaken, or directed PJM and the IMM to undertake, or directed interstate natural gas pipeline operators to undertake, to identify potential solutions to the natural gas deliverability problems that occurred during January 2014 in the PJM region, either by better optimizing the use of existing assets or by constructing new assets or both?

Answer: At the April 1 Technical Conference on Winter 2013/2014 Operations and Market Performance in RTOs/ISOs, the Commission highlighted concerns that electric generators without firm fuel arrangements faced natural gas deliverability challenges during the Polar Vortex events of last winter. In response, New England has filed a Winter Reliability Program with the Commission that, if approved, would procure additional on-site supplies of oil and

liquefied natural gas to guard against potential pipeline deliverability issues this coming winter. Also, as discussed in my response to Question 2, since that time the Commission has approved revisions to the New England capacity market to establish a "pay for performance" market design that is expected to provide much stronger incentives for electric generators to firm up their fuel supply arrangements to be sure they are available during critical events. Following the Commission's approval of this market design, PJM launched a stakeholder effort to reform its capacity market to put similar incentives in place for generators in its region.

The Commission has also focused attention on the increasing interdependence of the natural gas and electric industries, and launched a variety of initiatives to improve coordination between the two industries. These long-term efforts (begun in 2012) are aimed at ensuring that adequate market structures and appropriate regulations are in place to support the increasing reliance on natural gas-fired electric generation. For example, last year the Commission adopted new regulations to facilitate enhanced communication between pipeline operators and electric system operators for the purpose of ensuring reliability. In addition, the Commission issued a Notice of Proposed Rulemaking last year proposing a number of changes to its regulations that would better align the scheduling practices of the electric and natural gas industries.

6. Has the Commission determined whether any natural gas deliverability problems were reflective of attempts to manipulate natural gas prices or electricity market clearing prices?

Answer: OE's review of the Polar Vortex events included conducting an analysis of natural gas and electric market data and gathering information related to natural gas deliverability problems, including conducting multiple interviews with gas suppliers, LDCs, and pipelines, as well as generation operators to determine if manipulation may have contributed to the high natural gas prices or increased electricity market clearing prices during the cold weather events. OE did not find indications that natural gas deliverability problems were reflective of attempts to manipulate natural gas prices or electricity market clearing prices.

7. Price increases for natural gas and electricity in the PJM region, and elsewhere, are very concerning to me. My constituents in the PJM region have asked me to ensure that markets have been, and are, functioning properly and that prices have not been increased by speculation or manipulation. It is now July, can you assure me that FERC intends to have answers to these questions about natural gas and electricity pricing BEFORE next winter?

Answer: The Office of Enforcement comprehensively reviewed the natural gas and electric markets immediately following the Polar Vortex events to determine whether any manipulative behavior may have contributed to the high natural gas prices and/or the elevated cost of electricity during the events. This review involved conducting in-depth analysis of a variety of natural gas and electric market data and information and interviews of numerous market participants, including energy trading companies, generators, pipelines, and local distribution companies. OE also coordinated with the RTOs/ISOs and the market monitors. As a result of this review, OE has not found any indication that manipulative activity caused the high natural gas or electricity prices.

The Commission does extensive outreach to stakeholders, works with the market monitors, and conducts its own monitoring and surveillance efforts in order to do its best to help ensure that the markets are functioning properly and that rates are just and reasonable as per our statutory mandate. There are also several initiatives underway at the Commission to continue to assess the energy and capacity markets. The Commission will host a series of workshops on price formation in the RTO/ISO energy and ancillary services markets to explore potential improvements to market design and operational practices that impact how these prices are determined. The Commission also launched an inquiry to evaluate how the rules and structures of the centralized capacity markets in the eastern RTO/ISOs are supporting the procurement and retention of resources necessary to meet future reliability and operational needs.

8. In the Clean Power Plan proposed rule's Regulatory Impact Analysis, EPA notes that the Integrated Planning Model (IPM) was used to project the impact of the rule on electricity prices. The documentation for the IPM on the EPA's web site explains that the model assumes both perfect competition and perfect foresight. The former means that "IPM does not explicitly capture any market imperfections such as market power, transaction costs, informational asymmetry or uncertainty." The latter "implies that agents know precisely the nature and timing of conditions in future years that affect the legitimate costs of decisions along the way." Does FERC agree that such a model can accurately capture how the proposed rule will impact prices? What are some likely differences in the actual implementation of the rule and this model?

Answer: I understand that the Integrated Planning Model is a well-established planning tool used by EPA, other agencies, and utilities. I do not know whether there is a better model for analyzing the potential market impacts of the Clean Power Plan.

9. Achieving compliance with the proposed rule will require a replacement of higher carbon dioxide emitting resources with new lower or zero-emitting units. Yet a recent study by Christensen Associates commissioned by the Electric Markets Research Foundation concluded that the RTO markets "do not and cannot address long-term capacity needs." The study also found that "[b]ilateral forward contracting remains key under any market design for locking in revenues and facilitating financing of new resources. Contrary to this key necessity, however, the RTO markets include some design elements that impede long-term investments and long-term bilateral contracts." What steps does FERC intend to take to ensure that RTO markets do not impede bilateral contracting needed for new resource development that will be required for state compliance with the rule?

Answer: I have not reviewed the Christensen Associates' study and am unable to comment on the validity of its conclusions. But the Commission has devoted significant time and resources to reviewing the centralized capacity markets. Last summer, the Commission released a staff white paper detailing the capacity market designs in PJM, New York ISO and ISO-New England. On September 25, 2013, the Commission convened a well-attended technical conference to explore issues associated with the design and operations of those markets. Following the conference, the Commission issued a number of questions and invited industry participants to submit written comments. Among the issues addressed was the manner in which capacity markets could

accommodate bilateral contracting decisions to meet resource adequacy requirements or to accommodate state environmental policies. The Commission received over 50 sets of comments. The Commission is carefully reviewing those comments in determining how to move forward.

10. Within the retail access states, most of the generation is no longer owned by vertically-integrated utilities and instead is under merchant ownership. There is no state or local jurisdiction over these merchant generation owners regarding whether to continue to operate or close a plant or what types of generation technology should be built. Does FERC see any difficulties in implementing the proposed rule in states with large amounts of merchant generation?

Answer: In the past, the RTO and ISO markets that incorporate retail access states and significant merchant generation fleets have been able to successfully integrate state and regional environmental requirements into their market operations. So long as there is open and ongoing communication among FERC, EPA, DOE, state officials, NERC, RTOs/ISOs, and industry, I believe the same will be true with respect to Clean Power Plan.

QUESTIONS FROM THE HONORABLE GENE GREEN

Director Bay, as Director of Enforcement, your office is responsible for violations and inquiries into market manipulation.

However, unlike other federal agencies, FERC does not have an Office of Compliance or any other resource for the regulated community to address questions and concerns.

1. Mr. Bay, do you believe an Office of Compliance would be a benefit to the regulated community?

Answer: While I am always open to considering new approaches to improve the Commission's efforts to promote compliance, I do not believe that a new, separate Office of Compliance would necessarily benefit the regulated community. The Commission already has a number of important ways in which it promotes compliance. These include resources for the regulated community to address questions and concerns, such as the Commission Compliance Help Desk, the Hotline, the No Action Letter process, informal staff contact, General Counsel opinions, declaratory orders, accounting interpretations, and the guidance on compliance that comes from detailed, transparent annual reports and orders (those relating to Enforcement as well as other Commission program offices). In addition, market participants who think they may have violated Commission rules or regulations may submit a self-report about the relevant conduct, which could result in a reduction of the otherwise applicable civil penalty (or, depending on the circumstances, no civil penalty). In my view, it would be best to work on continuing to improve these existing mechanisms and approaches rather than create a new Office of Compliance.

2. Is the Office of Enforcement opposed to additional transparency in its dealings with the regulated community?

Answer: When I was Director of the Office of Enforcement, that Office, like the Commission as a whole, was always looking for possible ways to provide additional transparency in its dealings with the regulated community. I take that approach with me now that I am a Commissioner. I note that much of what the Office of Enforcement does, by nature, is confidential under Commission regulations and policies. Also, my view is that both the Office of Enforcement and the Commission generally have already achieved a significant amount of transparency in enforcement matters through annual reports and a statement of enforcement priorities, Notices of Alleged Violation, Penalty Guidelines, the *Brady* policy, settlement and show cause orders, and speaking appearances at industry and bar association conferences. But if there are ways to provide additional transparency, I would carefully consider them.

3. Would you oppose efforts to create such an Office and/or other resources to assist in compliance activities?

Answer: I am very much in favor of considering whether additional resources would assist the Commission's efforts to promote compliance. For the reasons mentioned above in response to Question 1, however, I do not believe that creating a new, separate Office of Compliance would be the best use of resources.