CLIENT ALERT

Dominion Pays $14 Million to Settle Manipulation Allegation

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AUTHORS

Paul J. Pantano, Jr. | **Sohair A. Aguirre** | **Thomas R. Millar**

On May 3, 2019, the Federal Energy Regulatory Commission issued an Order approving a Stipulation and Consent Agreement (**"Settlement"**) between the Office of Enforcement (**"OE"**) and Virginia Electric and Power Company (doing business as Dominion Energy Virginia) (**"Dominion"**). 167 FERC 61,103 (May 3, 2019) (hereinafter **"Order"**). Although the Order approving the Settlement was published on May 3, 2019, the parties executed the Settlement with OE in December 2018, an unusually long period of time between the execution of a settlement and its approval by the Commission. Dominion is a vertically integrated, franchised public utility that serves retail and wholesale customers in Virginia and North Carolina. The utility agreed to pay disgorgement of $7,000,000 to PJM Interconnection, L.L.C. (**"PJM"**) and a civil penalty of $7,000,000 to the United States Treasury, and to be subject to compliance monitoring, including an annual compliance monitoring report. Dominion stipulated to the facts set forth in Section II of the Settlement but neither admitted nor denied the alleged violations. The Commission concluded that the settlement was in the public interest because it resolved on fair and equitable terms OE's investigation into whether Dominion violated any Commission rules, including the Anti-Manipulation Rule, 18 C.F.R. § 1c.2 (2018), related to its receipt of lost opportunity cost credits ("**LOCs**") in the PJM market.

The Settlement asserts that PJM established LOCs to encourage generators to offer their resources into the PJM day-ahead (**"DA"**) energy markets, and if awarded a DA commitment, to be dispatched as part of PJM's pool-scheduled resources. *Id.* P 6. LOCs are not, the Settlement states, "intended to be an incentive for generators to design offers that seek to target and maximize LOCs or discourage PJM's dispatch of units in" the real-time (**"RT"**) market. *Id.* P 15. The Order explains that LOCs are designed to compensate generators for lost opportunity costs resulting from PJM's generation dispatch decisions and to enhance PJM's ability to ensure efficient and reliable power to meet RT demand system-wide in PJM. *Id.* P 6.

OE determined that from April 1, 2010 to March 31, 2011, Dominion engaged in a strategy to target and maximize its receipt of LOCs to the detriment of the proper functioning of PJM's market. OE alleged that in late 2009, Dominion "recognized that the revenue from LOCs had the potential to both produce positive margin and partially offset operational costs incurred in making DA offers, such as staffing and fuel costs that are incurred when the [simple cycle combustion turbines (**"CT units"**)] are not dispatched by PJM." Order P 8. Dominion allegedly developed and implemented a strategy to maximize receipt of LOCs by "offering its CT units in the DA market with price-based offers with substantially increased start-up and no-load values than previously used and with discounted incremental energy offers." *Id.* P 14. OE explained its view that through the allegedly manipulative strategy, Dominion "sought to obtain more DA commitments by correspondingly lowering the incremental energy offers in the CT units' offers, and at the same time sought to reduce the chance the units were dispatched by PJM in RT by increasing the start-up values in the offers." Recall that OE stated that the purpose of LOCs is to compensate generators for lost opportunities resulting from PJM dispatch decisions *in the RT market*.

OE also acknowledged, however, a number of facts that suggest that Dominion sought to and did engage in commercially reasonable, profit-seeking strategy. For example, OE acknowledged that Dominion's "DA commitments, RT run times, net positive energy revenue, and LOCs for the CT units significantly increased relative to earlier time periods, as [Dominion] expected." *Id.* P 12. OE stipulated that Dominion employed its strategy "with the expectation that its energy offers would produce more DA commitments, increased LOCs, and longer RT run times when dispatched." Settlement P 10. Neither the Order nor the Settlement contains an explanation of how OE could conclude that Dominion engaged in a manipulative scheme to maximize LOC payments and minimize RT dispatch while simultaneously stipulating that the expected and actual outcome of the strategy was that RT run times and energy revenue for the units "significantly increased." OE also acknowledged that Dominion "expected that offering its CT units according to this strategy would better optimize the CTs paid for by its customers." Again, neither the Order nor the Settlement seeks to explain how this fact fits into OE's conclusion that Dominion engaged in market manipulation.

At the end of the day, Dominion serves as another reminder that trading strategies that involve LOCs and any other type of out-of-market payment require careful scrutiny and, potentially, documentation before they are undertaken. This is especially so if the strategy targets or seeks to maximize out-of-market payments. Failure to scrutinize those sorts of strategies carefully risks trading in a manner that contradicts OE's view of the purpose of the products or payment mechanisms, which could lead to a long investigation and significant civil penalties.

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

Paul J. Pantano, Jr.	**Sohair A. Aguirre**	**Thomas R. Millar**
202 303 1211	202 303 1140	202 303 1144
ppantano@willkie.com	saguirre@willkie.com	tmillar@willkie.com