Akin®

FERC's Maxim Settlement Shows Continued Focus on ISO and RTO Bidding Conduct

Sep 29, 2016

Reading Time : **6 min**

The settlement reflects the Commission's (and Enforcement's) expansive view of the Anti-Manipulation Rule, reaching conduct that complied with applicable market rules, but was inconsistent with their purpose and market design (the type of conduct that Enforcement has, at times, described as "gaming"). The settlement also reflects the Commission's continued emphasis on enforcing the duty of candor applicable to market-based rate sellers, particularly in Independent System Operator (ISO) and Regional Transmission Organization (RTO) markets—a violation that carries the same potential civil penalties as market manipulation, but does not require proof of intent. The settlement is also notable for its timing and its scope. The settlement resolves allegations that were already subject to a FERC penalty assessment proceeding and order that was being reviewed in federal court, as well as allegations that had not been subject to an agency enforcement proceeding. And the settlement involves only Maxim corporate entities, releasing from liability all Maxim employees, including one that was held individually liable in the prior agency enforcement proceeding.

2010 Bidding Conduct

FERC found that Maxim violated the Commission's Anti-Manipulation Rule and duty of candor in 2010 through its bidding conduct in ISO-NE's energy market. The settlement itself contains only limited information about these violations. However, FERC described these violations in detail in its May 1, 2015, order assessing penalties against Maxim and an employee (as part of an Order to Show Cause proceeding). Specifically, FERC found that, on a number of days in July and August 2010, Maxim submitted offers for its Pittsfield generation plant (a 181 MW dual-fuel unit in Pittsfield, Massachusetts) based on fuel oil prices when it actually burned less expensive natural gas and provided ISO-NE's market monitor with misleading and incomplete information about its fuel usage. When generators in ISO-NE are needed for reliability, they are eligible to receive supplemental payments above the energy market price to cover their operating costs (known as "Net Commitment Period Compensation," or NCPC). However, because plants needed for reliability have a form of market power, their offers are subject to mitigation based on their actual costs. Therefore, for a unit needed for reliability, its actual costs of generating energy (including fuel costs) are relevant to determining whether the unit's offers should be mitigated. FERC found that Maxim violated the Anti-Manipulation Rule and the candor requirement by submitting offers based on a higher-priced fuel (oil) than the plant actually burned (gas) and making misleading communications to ISO-NE's market monitor to prevent the market monitor from mitigating Maxim's offers based on the actual fuel used.

In the Order to Show Cause proceeding, the Commission assessed a $5 million civil penalty against Maxim (and related corporate entities), as well as a $50,000 civil penalty against a Maxim employee in his individual capacity for violating the Anti-Manipulation Rule. FERC's penalties concerning the 2010 conduct have been subject to ongoing review in federal district court in Massachusetts, where, in July, the court denied Maxim's motion to dismiss the case (finding that FERC pleaded a viable theory of manipulation) but held that the case had to proceed as an ordinary civil action under the Federal Rules of Civil Procedure rather than a more narrowly tailored review as FERC had advocated.[3]

2012-13 Bidding Conduct

Enforcement found that Maxim violated the Commission's Anti-Manipulation Rule in 2012 and 2013 by structuring its energy market offers in a way intended to evade ISO-NE's mitigation rules for reliability units in order to capture additional NCPC revenues. When generators submit their offers, they submit a "start-up" price (the price to bring the facility into full operation), a "no load" price (a fixed dollar amount per hour) and a variable "energy" offer (a dollar charge per megawatt-hour (MW/h)). Generators also specify a "minimum run time" (the shortest period for which their unit may be dispatched). For reliability units subject to mitigation, the aggregate total of the start-up, no load and energy charges is limited to 110 percent of a unit's reference costs across the minimum run time.

Enforcement found that, from July 2012 through mid-August 2013, Maxim changed its offer inputs by transferring dollars from the Pittsfield plant's start-up price (reducing it from $38,641 to $0) to its energy price (increasing it from $76.30/MW/h to $149.50/MW/h), and submitting the shortest possible minimum run time permissible under the tariff (four hours). By doing so, Maxim was able to increase its NCPC revenues when the Pittsfield plant was dispatched for longer than the four-hour minimum run time because it was paid at the higher energy offer price for each additional hour. Enforcement found that this strategy effectively allowed Maxim to receive an additional start-up payment every four hours after the minimum run time ended.

Takeaways

The Maxim settlement is notable for several reasons. First, the settlement reflects the Commission's continued use of the Anti-Manipulation Rule to target perceived "gaming" of ISO and RTO markets.[4] Unlike the 2010 bidding conduct, the 2012-2013 conduct does not involve allegedly false or misleading statements. Enforcement states in the settlement that a core component of the conduct was "permitted by the ISO-NE tariff."[5] However, Enforcement found that Maxim's 2012-2013 bidding conduct violated the Anti-Manipulation Rule because it was "designed to frustrate and evade ISO-NE's mitigation rules" and, separately, because it "interfered with a well-functioning market in ISO-NE that was designed to limit NCPC payments for reliability dispatches to 110% of a unit's reference levels." The settlement therefore reflects an expansive view of the Anti-Manipulation Rule, reinforcing that the Commission will pursue enforcement action against market participants perceived to be "gaming" rules or otherwise transacting in a way that is inconsistent with the purpose behind the rules (in this case, the market power mitigation rules). Ultimately, the extent to which the Anti-Manipulation Rule reaches this type of conduct will be decided by federal courts.[6]

Second, the Order to Show Cause proceeding and settlement show FERC's continued emphasis on enforcing the Section 35.41(b) duty of candor. Section 35.41(b) prohibits a market-based rate seller from providing false or misleading information to the Commission, ISOs or RTOs (and their market monitors), or transmission providers, unless the seller exercised due diligence to prevent such occurrences. Section 35.41(b) is a significant source of compliance risk for ISO and RTO market participants in particular, given the frequency with which they interact with ISO and RTO staff and market monitors. And importantly, it is generally easier for FERC to find a violation of Section 35.41(b) than the Anti-Manipulation Rule, since 35.41(b) does not require a finding of intent (yet, both violations carry the same potential civil penalties of up to $1 million per day, per violation).

Third, the settlement covers a broader range of conduct than the subject of the 2015 Order to Show Cause proceeding (which included the 2010 bidding conduct but not the 2012-2013 conduct), but narrower than that alleged in the Enforcement staff's November 2014 Notice of Alleged Violations (NAV) (which included the 2010 and 2012-2013 bidding conduct, as well as an allegation that Maxim artificially inflated generator performance during capacity tests for more than three years).[7] The settlement also includes only Maxim corporate entities as subjects, and releases from liability all Maxim employees, including one employee named in the OSC proceeding and another named in the NAV.

---

[1] Maxim Power Corp., 156 FERC ¶ 61,223 (2016).

[2] 18 C.F.R. §§ 1c.2, 35.41(b) (2016).

[3] Mem. and Order Regarding Procedures Applicable to FERC's Petition and Respondents' Motion to Dismiss, *FERC v. Maxim Power Corp*., No. 3:15-cv-30113-MGM (D. Mass. July 21, 2016). Under Section 31(d)(3) of the Federal Power Act, an investigation subject has the right to have a FERC penalty assessment reviewed *de novo* in federal district court.

[4] Neither the settlement nor the FERC order approving it uses the term "gaming." However, the November 2014 Staff Notice of Alleged Violations (NAV) alleged that Maxim "gamed" ISO-NE's mitigation rule.

[5] 156 FERC ¶ 61,223 at P 14 ("In mid-2012, Maxim shifted dollars from the one-time Startup charge to the recurring Energy charge. Such a change was permitted by the ISO-NE tariff in effect at the time.").

[6] As noted above, the Federal Power Act allows an investigation subject to have a civil penalty assessed by FERC reviewed *de novo* in federal district court. There are several district court review proceedings ongoing at this time involving conduct that allegedly evaded or took advantage of market rules in violation of the Anti-Manipulation Rule. While no court had decided the merits of any of these cases, FERC has defeated motions to dismiss in two such cases. *See* Mem. and Order Regarding Motions to Dismiss, FERC v. Silkman, No. 13-13054-DPW (D. Mass. Apr. 11, 2016); Order Denying Motion to Dismiss, *FERC v. City Power Mktg., LLC*, No. 1:15-cv-01428 (D.D.C. Aug. 10, 2016).

[7] 156 FERC ¶ 61,223 at P 23 (“Enforcement agrees to permanently close, without further action, any and all remaining investigations of the Maxim Respondents (and their respective current and former officers, directors, employees, agents or assigns) concerning conduct up to the date” of the settlement.).

Categories

Energy Regulation, Markets & Enforcement

Power