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## ELECTRICITY LAW DEVELOPMENTS – October 10, 2007

### Prepared for ELCON

This report summarizes recent developments in FERC proceedings in which ELCON has been active and other matters of interest to industrial consumers. Inside this issue:

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New developments since the September 2007 issue of Electricity Law Developments are **in bold**.

**I. FERC PROCEEDINGS**

**A. FERC Staff Report on Demand Response**

On September 7, 2007, FERC staff issued a report assessing growth over the past year in demand response and advanced metering programs. In August 2006, pursuant to an EPCRA 2005 directive, FERC issued its first report on demand response programs in the electric utility industry. The September 2007 report is an informational update to the August 2006 report and includes an overview of demand response in the RTO/ISO markets. FERC plans to issue another comprehensive report in 2008 and will continue to track developments and activity annually.

According to the September 2007 report, demand response and advanced metering programs in wholesale markets have grown significantly during the past year, particularly with the inclusion of demand resources in forward capacity markets and ancillary services markets, and the development of new reliability-based demand response programs.

FERC staff noted that a number of states and individual utilities sought to introduce or increase opportunities for demand response and price responsiveness, including increasing customer access to information about energy consumption, adoption of time-based rates, and deployment of technologies such as advanced metering that will allow for price-responsiveness. The report also discusses a number of recent FERC actions to encourage use of demand response, including: revision of the OATT in Order 890 to require transmission service providers to incorporate demand response into their transmission planning processes and to require them to allow demand resources to provide ancillary services on a comparable basis to generation resources; ordering revision of NERC's reliability standards to include demand response; and inclusion of a number of proposals to enhance demand-response in the organized markets in the recent ANOPR on

**competition in the wholesale markets. Additionally, FERC held two technical conferences on demand response and, in November 2006, FERC began a collaborative effort with NARUC to coordinate efforts of state and federal regulators to integrate demand resources into retail and wholesale markets and planning.**

**FERC staff lists certain trends it has observed in demand response over the past year:**

- **Increased participation in demand response programs**
- **Increased ability of demand resources to participate in RTO/ISO markets as reflected by increased bidding into certain of these markets**
- **More attention to the development of a smart grid that can facilitate demand response**
- **More interest in multistate and state-federal demand response working groups**
- **More reliance on demand response in strategic plans and state plans**
- **Increased activity by third parties to aggregate retail demand response.**

**FERC staff also reports that more than 40 million advanced meters are expected to be deployed within the next few years and will enhance customer price responsiveness and will reduce the utility's costs of operations.**

**In the August 2006 report, FERC staff had identified a number of regulatory barriers to demand response which continue to be challenges:**

- **Disconnect between retail pricing and wholesale markets**
- **Utility disincentives associated with offering demand response**
- **Cost recovery and incentives for enabling technologies**
- **Need for additional research on cost-effectiveness and measurement of reductions**
- **State barriers to increased demand response**

- **Specific wholesale and retail rules that limit demand response**
- **Barriers to providing demand response services by third parties**
- **Insufficient market transparency and access to data**
- **Problems related to coordination of federal-state jurisdiction affecting demand response**

**In addition, in the September 2007 report FERC staff identifies two additional problems. First, there continues to be insufficient collection and sharing of real-time information on demand response activities among RTOs/ISOs, utilities and other providers. Second, barriers to implementing critical peak pricing tariffs remain. Staff reports that a number of utilities have announced plans for CPP programs, but will need to conduct pilot programs to test customer response in their own service territories prior to implementation.**

**B. FERC ANOPR on Reforms to the Organized Markets -- Docket Nos. RM07-19, AD07-7**

On June 22, 2007, FERC announced an Advanced Notice of Proposed Rulemaking (ANOPR) to initiate certain reforms of the organized markets. “Wholesale Competition in Regions with Organized Markets,” 119 FERC ¶ 61,306. The reforms address four of the concerns or problem areas that ELCON and other consumer interests have identified with organized markets such as PJM: (1) demand response, (2) long-term contracting, (3) market monitoring, and (4) RTO governance. Some of FERC’s proposals are outlined below:

*(1) Demand Response and Pricing During Power Shortages*

- Require RTOs and ISOs to allow demand resources to provide certain ancillary services in their markets unless not permitted by state law, modify tariffs to let demand resources provide spinning and supplemental reserves without being required to sell into the energy market.

- Modify RTO and ISO tariffs to eliminate certain charges for purchasing less energy in real time than in the day ahead market during a system emergency.
- Amend market rules to permit an entity that aggregates the demand responses of individual retail consumers to bid the aggregate demand reduction directly into an RTO or ISO energy market, unless not permitted by state law.
- Modify market power mitigation rules so that pricing during an emergency can elicit more demand response.

*(2) Long-Term Power Contracting*

- Require RTOs and ISOs to post information that would facilitate long-term contracts.
- Require or encourage efforts by RTOs and ISOs to develop standardized forward products.
- Dedicate a portion of the ISO's or RTO's website for market participants to post long-term buy/sell offers.

*(3) Market Monitoring Policies and Information Sharing*

- Remove the market monitoring unit from RTO/ISO operations.
- Require that the MMU advise the Commission and other stakeholders of any design flaws and report to the Commission any tariff violations it believes may have been committed by the RTO or ISO.
- Regular conference calls among the market monitor, interested state commission and FERC staff.
- Release of offer and bid data, with a lag period. Release would mask market participants' identities.
- Subject to certain limitations, state regulatory commissions within an RTO or ISO may request and receive information from the RTO's or ISO's market monitoring unit.
- Develop a pro forma tariff provision to address all sections relating to market monitoring.

*(4) Responsiveness of RTOs and ISOs*

- Provide RTO and ISO customers with direct access to the board of directors.

**More than one hundred commentors representing the span of stakeholders in the electricity industry had suggestions on how the wholesale markets could be improved. The**

issues of demand response, long-term contracts and RTO accountability were the subject of numerous comments. In summary, most comments indicate support for demand response, however views were strong on both sides of the question of raising price caps. Not surprisingly, the RTOs and ISOs thought responsiveness to stakeholder concerns was not a great problem, while industrial consumers generally expressed dissatisfaction with management that favors the supply side of the market. FERC's suggestion of hybrid boards received mixed comments. And while many commentors agreed that opportunities for long-term contracting are lacking, there was little agreement on how the problem can be resolved.

Following are a few highlights of the comments filed:

*Structural Reforms*

ELCON, together with AISI and ACC, commended FERC for recognizing the need for reforms to improve the operation of the organized markets and urged the Commission to reconsider its current mix of regulation and competition in the organized markets to ensure that customers are not exploited by a flawed market design and that they receive the benefits they deserve from restructured markets.

Others also remarked on the need for FERC to address fundamental structural issues. A coalition of industrial customers criticized FERC for operating "from the premise that all is generally well with the existing structure and design of organized electric markets." "[A] few 'tweaks' to the status quo" will not make the markets work better, they cautioned. APPA stated that it "highly doubts there is a Great and Powerful Oz of competition back there making RTO markets even 'workably' competitive. It is in fact more likely that one will find a mélange of administratively determined market rules,

algorithms understandable only to a privileged few, ad hoc patches, makeshift and incomplete mitigation, perverse incentives and naked profit-taking at the expense of consumers.” And the Steel Producers noted, “there seems to be little incentive on the part of utilities and suppliers to take the steps needed to improve the operation of the markets, including building new transmission, fully integrating demand response into the markets and building or acquiring lower-cost generation capacity. Indeed, for some market participants, especially companies that own both transmission and generation, taking these steps would amount to killing the golden goose.”

### *Demand Response*

ELCON et al. strongly supported the ANOPR’s attempts to expand the role of incentive-based demand response in the organized markets and made the following recommendations:

- Each ISO or RTO should have an obligation to purchase on a non-discriminatory basis demand resources in markets for ancillary services. Demand resources should be eligible to provide any ancillary service currently required in the OATT. The demand resources would be expected to meet reasonable size, telemetry, metering and bidding requirements. The protocols should not be based on the limitations of generators but rather on a source neutral basis that reflects system reliability needs.
- ISO or RTO protocols for purchasing demand response for ancillary services should be standardized to accommodate sales from industrial end users with DR capable facilities in multiple ISOs or RTOs.
- Sellers of demand response should have the opportunity to bid demand response as operating reserves without the obligation to sell into the energy market.
- Deviations charges to buyers who take less energy in the real-time energy market than purchased in the day-ahead market should be eliminated. Each ISO or RTO that imposes such charges should implement other cost-based rate mechanisms for the recovery of prudent uplift costs.

- **ISO/RTO market rules should permit aggregators of retail customers (ARCs) to bid demand reduction on behalf of retail customers. The market rules should be non-discriminatory with respect to bids from ARCs or non-aggregated bidders. Practices, rules and procedures for the acquisition of demand response should be standardized across ISOs and RTOs to promote participation.**
- **Demand response should be compensated on the same basis as generation for the same services. If generators are given the option of higher of LMP or opportunity costs, demand should be eligible for the same or comparable pricing scheme. Demand response participants should also receive incentive payments to be able to provide energy whether it is called or not.**
- **Demand response participants should not be required to purchase energy as a precondition to a demand reduction bid unless required by contract or tariff. So-called generator offsets are unnecessary as long as non-participating loads receive net benefits.**
- **ELCON urges great caution with regard to modifications to market mitigation rules to allow scarcity pricing. Any proposal to raise (not eliminate) market-wide caps in emergency situations must only be considered after end-use customer loads are adequately hedged from spot market price volatility and other pre-conditions are met. This requires the establishment of a liquid forward market. Even after such conditions are met, it is preferable that a “proof of concept” be established in a carefully designed pilot test. Raising bid caps for demand bids only may not be practical until other reforms to the market have succeeded. ELCON opposes the proposal for an administratively-determined demand curve for operating reserves because it will reduce market transparency and oversight, and may be too complex to survive intact during adjudication.**

**Among the myriad other comments filed, EEI supported providing RTOs/ISOs with the necessary flexibility to adopt different approaches to modifying ancillary service markets for the integration of demand response consistent with the reliability purposes for which ancillary services are required but took issue with the notion of incentive payments to retail customers for demand response. Such payments, according to EEI, are unnecessary and amount to double payments, since a customer’s bill decreases with every megawatt-hour not consumed.**

**The FTC disagreed with EEI that retail customers receive a double payment when they are paid for wholesale demand reductions that also result in savings on their retail**

**bills because this argument “understates the economic value of the reduction when traditional retail pricing is in place. In order to give efficient incentives for conservation during peak demand periods, the savings on the customer’s power bill must be supplemented so that the combination - savings on the bill plus the supplementary compensation – results in an efficient price to the retail customer.” Acceptance of EEI’s view, according to the FTC, would prevent or reverse FERC’s demand response regulatory reforms at the wholesale level.**

**The FTC commented that state retail price regulations impede reform of the electric power markets by subsidizing consumption of electricity during periods of high demand. They suggested that if state regulators would act to encourage retail demand response, then demand response would increase at wholesale levels. Absent this, they suggested that FERC allow customers to bid into the wholesale market and receive payments to reduce consumption, bypassing retail pricing impediments all together. The FTC also took issue with the ANOPR’s failure to identify the connection between generation market power and demand response. Increased demand response would reduce generation market power and thus reduce the need for price caps or other price regulation.**

**AF&PA focused on technical impediments to demand response, including the lack of adequate metering and other technology. FERC, however, faces a “chicken and egg” problem in trying to increase demand response because it may need to resort to scarcity pricing to motivate participation in demand response programs. They suggest the creation of a “financial performance obligation” which would require “every unit receiving a capacity payment to financially guarantee the delivery of energy to the real time market at**

or below a specified strike price in any hour.” This obligation would not require physical delivery at every hour, however.

TAPS cautioned FERC to beware of experimentation in the area of demand response. The FPA “does not permit the commission to treat consumers as guinea pigs to see whether demand response adequate to mitigate market power will develop in a reaction to exorbitant prices.”

A group of financial institutions (Barclays Capital, J. Aron & Company, and Morgan Stanley Capital Group) expressed the view that capacity markets should be temporary in nature until scarcity pricing, demand response and forward contracting are further developed. “While capacity markets are generally touted as being necessary to address the ... ‘missing money’ problem, ... these markets should be viewed as transitional mechanisms that are explicitly designed to diminish in importance over time... . Market structures that limit the ability of prices to ration power during periods of scarcity effectively encourage excess consumption... .” Energy markets that rely on robust price signals and smart grid technologies and advanced metering infrastructure “would incentive significantly more forward contracting so that only a relatively small portion of customer’s demand would be subject to scarcity prices.”

The ISO-NE indicated it did not believe removing bid caps for demand resources would be effective. While it might reduce the risk of exercise of market power, it would provide incentives for inefficient trading and contracting between supply and demand resources. They suggested that their Forward Capacity Market model is a more effective solution.

### *Long-term Power Contracts*

**ELCON et al. did not think that the proposals in the ANOPR will lead to adequate opportunities to sell and buy power through long-term power contracts and to be able to choose a portfolio of short-term, intermediate-term, and long-term power supplies. The organized markets are unwittingly structured as suppliers' markets and fundamental changes to the Day-Two market paradigm will be necessary to establish a robust forward market capable of delivery net benefits to consumers.**

**The Wisconsin Industrial Energy Group agreed with ELCON. Long term contracting can only be encouraged if there are steps taken to modify market design that would increase the incentive for sellers to enter into long term contracting. Buyers today, already have this incentive; the problem is how to motivate sellers. The Steel Manufacturers also agreed and pointed out that the “core premise of the organized markets (location-based marginal pricing of energy) is a short-run model that aims to promote operational efficiencies,” however this model is inappropriate for promoting long-term capital investments “as long as the Commission, state regulators, or both, are compelled to shield consumers from scarcity price signals.”**

**Several commentors supported the idea of a transaction bulletin board on RTO websites where offers to buy or sell power on a long-term basis could be posted. A handful of financial institutions remarked that posting of some data might help, but were skeptical of the idea of posting specific contract details.**

**EPSC did not agree that a transaction board will facilitate long-term contracting. Rather, “EPSC believes that there are no inherent impediments to longer term contracting in the organized markets today, although an overly aggressive mitigation regime in the spot market interferes with price signals that reflect true supply and demand conditions and**

**reduces buyers' need, incentive and ability to hedge the risk of exposure to accurate spot prices. Buyers and sellers who seek longer term supply arrangements must have confidence in a liquid spot market in order to make economic decisions about terms and price requirements for bilateral contracts.”**

**NARUC cautioned FERC to coordinate any long-term contracting rules with states so as not to disrupt existing state programs, particularly those regarding LSE purchasing rules.**

**EEI for its part stated that its Contract Drafting Committee and Working Group is the solution for long-term contracting concerns. The group “provides an open forum for all market participants to participate in the development of standardized products. The standardized contract language developed by EEI is used extensively in bilateral markets and new language is constantly being developed to respond to changing market needs. There is no need for the Commission to take action in this area.”**

**The financial institutions disagreed with the general assertion that long-term contracts are not available in the market, but qualified this comment with the explanation that they are available in certain regions of the country that are very liquid and subsequently have forward prices that go out many years. In regions without liquid wholesale markets, “virtually the only entity that can manage the risk of entering into a long-term contract is the utility because they have the ability to recover costs bypassing them along to captive customers.” They also acknowledged that in areas with active wholesale markets, there are still some institutional barriers to long-term contracting between non-utility market participants, including state prudence reviews of long-term power purchase agreements.**

**PJM also discussed perceived risks associated with long-term contracting. In particular, they suggested that delivery risk (LMP congestion) frustrates long-term contracting, especially when this risk cannot be hedged. They believe that their FTR program is helping, but still needs improvement: there is need for longer term FTR products than those currently available; loop flows have a disruptive impact on the pricing of FTRs; and there is not enough data transparency.**

#### ***Market Monitoring Principles***

**ELCON believes that the debate between an “internal” or “external” MMU is misplaced. In their present forms we believe that neither can be independent. We advocate a two-tiered MMU structure with the “top-tier” consisting of a small panel of part-time market experts reporting to the board. The “lower-tier” would be internal to the ISO or RTO and generally report to the board. ELCON supports other reforms proposed in the ANOPR related to MMUs.**

**EPSA commented that the challenge facing FERC is how to define the Market Monitor role while taking account of regional variances. However, all market monitors must do the following: (i) monitor the behavior of all market participants, including buyers, sellers and transmission owners; (ii) ensure that market rules produce efficient outcomes and are correctly implemented; and (iii) produce regular reports for FERC and market participants. Additionally, they assert that when MMUs report suspected tariff and rule violations to the Commission, information on such allegations must be held by FERC and disclosed publicly only when an investigation is completed and a finding of wrongdoing is made.**

**APPA commented that “the exact structure of an RTO MMU (*e.g.*, internal v. external) is less important than the day-to-day ‘rules of engagement,’ clarity regarding the**

role of the MMU, and “buy-in” to the MMU structure by the RTO’s stakeholders and management.” Regardless of the structure selected, the MMU must be able to report their concerns without fear of retribution or loss of future income (either as an employee or a contractor), including direct reporting to the RTO Board and the Commission (as well as state public utility commissions and other state entities), without seeking prior permission from RTO management; either by contract or through the RTO’s internal budget, MMUs must have sufficient facilities, personnel, computer information systems and training to carry out their duties; the RTO must provide full and complete access to RTO information staff; and it must be clear that a vital part of an MMU’s mission is the protection of wholesale and retail customers that the RTO serves from the exercise of market power and the payment of unjust and unreasonable rates.

PJM urged FERC to examine the practical reality of its proposed policy for market monitors. The Commission should “establish market monitors as entities with clear lines of responsibility and authority directly to the Commission, not the RTO. All market monitor responsibilities, authority, duties, obligations and procedures should be stated in a Commission-approved attachment to the RTO’s tariff. However, the RTO would *not* be ‘accountable’ for the actions of the market monitor or any other aspect of market monitoring.” Any other approach that attempts to preserve market monitors as instrumentalities of an RTO but limits the RTO’s ability to supervise the function “would raise serious legal questions about the Commission’s ability to limit a public utility’s management of its business.”

#### *ISO/RTO Governance*

ELCON et al. support a requirement that each ISO or RTO have a balanced “hybrid” board consisting of a majority of independent members and a minority of

members representing stakeholder interests. The stakeholder members should be evenly split between supplier and consumer interests.

The Large Public Power Council suggested that the proposed rule include requirements for: (1) publication of meaningful, detailed strategic plans; (2) periodic measures of customer satisfaction; (3) performance criteria for RTO and ISO executives tied to specific objectives, including the ability to meet budgets. Further, stakeholders must be permitted to review, and the Commission must pass on, budgets prospectively and all substantial RTO and ISO capital expenditures and all significant tariff changes must be supported with cost-benefit analyses.

The Midwest ISO and CAISO both indicated the belief that their models worked well. MISO touted its responsiveness and CAISO stated that it has already implemented many of FERC's proposals in the ANOPR. "These measures, together with other CAISO processes and structures, are working extremely well to achieve the goals established by the Commission – i.e., independent governance, responsiveness to stakeholders, and effective market monitoring."

A number of commentors urged FERC not to require hybrid boards, but rather to use a refined board advisory committee approach that includes a role for State Commission and Consumer advocate representation.

**C. SPP Utilities Seek To Terminate QF Purchase Obligations --  
FERC Docket No. QM07-5**

On September 25, 2007, four utilities in the Southwest Power Pool ("SPP") – Xcel subsidiaries Southwestern Public Service Co. and Oklahoma Gas and Electric Co. and AEP subsidiaries Public Service Co. of Oklahoma and Southwestern Electric Power Co. –

filed a voluminous application to terminate their requirement to enter into new contracts or obligations with QFs under Section 210(m) of PURPA.

This is the first such application filed under Section 210(m) that involves a Day 1 RTO. The applicable criteria governing such applications are those specified in Section 210(m)(1)(B):

**(B)(i) transmission and interconnection services that are provided by a Commission-approved regional transmission entity and administered pursuant to an open access transmission tariff that affords nondiscriminatory treatment to all customers; and (ii) competitive wholesale markets that provide a meaningful opportunity to sell capacity, including long-term and short-term sales, and electric energy, including long-term, short-term and real-time sales, to buyers other than the utility to which the qualifying facility is interconnected. In determining whether a meaningful opportunity to sell exists, the Commission shall consider, among other factors, evidence of transactions within the relevant market . . .**

By regulation, FERC has determined that SPP satisfies Section (B)(i). 18 C.F.R.

§ 292.309(g). Thus, the only bases for challenge is to assert either that the applicants have not made a proper showing that there exist “competitive wholesale markets that provide a meaningful opportunity to sell capacity, including long-term and short-term sales, and electric energy, including long-term, short-term and real-time sales” or that the application does not include all of the information required by 18 C.F.R. § 292.310(d) (*e.g.*, information about transmission constraints and congestion, description of processes and practices for arranging for transmission service).

The application makes two key points.

First, the applicants assert that SPP’s Energy Imbalance Service (“EIS”) market is a robust market that sends meaningful price signals on a real time or near real time basis and that is available to all sellers. Applicants note that one QF (an ELCON member) and various IPPs actively participates in EIS and that about 8-9 percent of SPP’s total energy

requirement is met through the EIS market. The applicants also cite statistics (drawn from EQR) on SPP's short-term energy and capacity markets and long-term energy and capacity markets intended to show that each market "is deep and has numerous buyers and sellers" and therefore that there are meaningful opportunities for QFs to participate, again referencing sales of an ELCON-member QF in these markets. The application also asserts that a number of wind projects in SPP were eligible for but did not bother to obtain QF certification because they had sufficient market access simply as non-QF EWGs. The data presented in the application are based on a supporting affidavit by Drs. William Hieronymus and Matthew Arenchild.

Second, the applicants assert that the existence of formal competitive procurement processes that do not discriminate against QFs establish further evidence of sufficient access to competitive markets. Affidavits from each utility address (i) how the procurement process is designed; (ii) how the winning bids are selected; (iii) evidence of past solicitations and winning bids; (iv) solicitation characteristics; and (v) other information about the procurement process, which track the criteria that FERC spelled out in Order No. 688 at ¶ 139. Extensive documentation about each utility's RFP process is attached.

Based on initial review of the main text of the main text and Hieronymus/Arenchild affidavit, but not the voluminous appendices and attachments that would require technical review, the application appears to do a thorough job of addressing the various applicable criteria of Section 210(m) and Order No. 688. QFs within the footprint of the applicant utilities may be able to argue that the EQR data do not reflect access to true long-term markets (a key generic issue that likely will arise in any future applications.) Additionally,

the application might be challenged on the basis that, if factually supportable, the SPP EIS market (or other SPP shortcomings) and/or the utilities' RFP processes do not establish meaningful, non-discriminatory access for QFs. Such arguments would have to be based on particular aspects of the EIS or RFPs and preferably would be supported by specific anecdotes.

Interventions and protests in this proceeding are due October 23, 2007.

**D. FERC Ends Investigation of PJM Market Monitor But Orders Settlement Talks -- (Docket Nos. EL07-56 and EL07-58)**

FERC on September 20, 2007, ended its investigation into complaints of the Organization of PJM States ("OPSI") and several electric cooperatives arising out of charges by Joseph Bowring that PJM Interconnection L.L.C. ("PJM") had undermined the independence of its Market Monitoring Unit ("MMU") after finding that the record supported a conclusion that PJM did not violate its tariff. However, in the same order the Commission rejected a Unilateral Settlement Offer filed August 14, 2007, by PJM proposing to recast its MMU into an external entity which would contract with PJM to provide market monitoring services. Citing the "significant tension" between PJM management and Bowring as well as its conclusion that a consensual resolution would best address confidence in the independence of market monitoring, the Commission instead ordered the parties to engage in settlement talks through their choice of several alternative facilitators.

The proceeding arises from complaints of the Organization of PJM States ("OPSI") and several electric cooperatives relating to charges by Bowring that PJM has been undermining the independence of its market monitoring unit ("MMU"). Bowring charged that PJM deprived the

MMU of adequate resources, lured away its employees, exercised editorial control over MMU reports and interfered with MMU data systems. The complaints requested that FERC issue a declaration that PJM has violated its tariff and that PJM should be required to return MMU staffing and resources to the *status quo ante*.

FERC granted fast-track processing of the dispute. Allegheny Elec. Coop. v. PJM, 119 FERC ¶ 61,165 (May 18, 2007). Both Bowring and PJM filed responses to FERC's data demands in June 2007. Bowring's counsel subsequently filed comments noting that the documents do not so much indicate disagreement as to what factually occurred as they reflect PJM's refusal to recognize the independence of the market monitor.

#### *PJM's Settlement Offer*

On August 14, 2007, PJM filed an Offer of Settlement providing for establishment of an external MMU, modeled in large part on the MISO structure. PJM proposed that Bowring be retained as MMU and not be subject to removal without FERC approval. Under the Settlement, the MMU would have control over its own data systems; PJM would not be able to screen, alter or delay the MMU's findings; the MMU would have its own budget and if it believed it was under funded by PJM, the MMU could bring its concerns to the Commission; and procedures would also be adopted to prevent PJM from raiding MMU employees.

Bowring submitted comments on the proposed Settlement stating that he was encouraged that PJM was attempting to address some of the concerns he had raised, but that the settlement proposal "is ultimately not acceptable because it does not adequately protect the purpose, principles, functions and essential features of the MMU." With revision, he indicated that the settlement offer could be a starting point for negotiations. Bowring did not oppose making the MMU an external entity; however, he was critical of the settlement's failure to ensure MMU independence. In particular, he took issue with PJM's exclusive oversight and administration of

the retention agreement and with its review of all MMU periodic reports. Additionally, Bowring expressed concern with provisions that limit the MMU's access to data and other necessary resources and with provisions that prohibit the MMU from interacting with PJM committee members during the market rule development process.

The Allegheny Energy group (the "Joint Complainants") urged FERC to reject the settlement proposal and to proceed with the hearing process, particularly discovery. They were particularly critical of the fact that PJM "continu[es] to gloss over the distinction between an independent market monitor and one that is merely external." The Organization of PJM States, Inc. (OPSI) also filed comments strongly opposing the proposed settlement. The evidence in the record, they asserted, "clearly establishes issues of material fact that must be resolved by the Commission before PJM's proposal may be addressed on its merits." The settlement offer "does not constitute sound policy, does not resolve the issues identified in OPSI's complaint, fails to address PJM's historic tariff violations and creates unacceptable risk that PJM could continue to hamper activities of the PJM market monitor."

On August 22, 2007, ELCON weighed in, expressing several concerns with the Settlement Offer, among them the need for the Commission to send a message to RTOs about the independence and integrity of MMUs by issuing a final decision evaluating the RTO's past conduct vis-à-vis the MMU, regardless of any settlement moving forward. Additionally, ELCON suggested that PJM be required to file the report of the "independent investigation" that it commissioned to examine Bowring's charges. ELCON also urged FERC to reject PJM's proposal Market Monitoring Advisory Panel is made up of three people -- one of whom is an employee of PJM, and urged that the MMU should report directly to the Board and be assured of retaining current personnel and budgeting.

### *FERC's Tariff Decision*

Even after indicating that the RTO's tariff must be changed in order to restore confidence lost through PJM's "unusual degree of supervision over the market monitor," FERC concluded that the record of more than 2,700 pages supported the finding that PJM did not violate its tariff. This conclusion was at least partially based on Bowring's failure to claim that PJM had violated its tariff. Rather, Bowring claimed that PJM actions may eventually rise to a violation of its tariff if left unchecked.

FERC dismissed each of Bowring's accusations. First, Bowring argued that PJM transferred two employees from the MMU in order to weaken the unit. The Commission found no tariff violation because the MMU was still meeting its monitoring obligations. The Commission also noted that the two employees were transferred to another division in order to exploit their specific expertise, and they continued to devote 30% of their time to MMU duties. FERC deemed the use of contract employees to make up for reduced MMU staffing levels appropriate in light of the uncertainty arising from the prospective switch to an external market monitor. Second, FERC concluded that the transfer of control of the database which the MMU uses to the RTO's vice president of markets would only violate its tariff if the database was altered, or the MMU's access to the database was restricted. FERC concluded that has not happened.

Finally, FERC rejected several accusations relating to the MMU's reporting and recommendation roles. Bowring had argued that PJM attempted improper influence over his final Draft of the *2005 State of the Market Report* by "ordering" that he replace his revised conclusion as to the effect of consolidation on market competitiveness with a statement that the MMU would make such a recommendation in the near future. PJM

countered that it had only “requested” the change because Bowring’s last-minute revision had not undergone PJM’s internal review process. The Commission concluded that PJM’s motive in requesting the change was “unclear,” yet it found no tariff violation because Bowring’s revised analysis remained in the final draft, and the requested deferral of his revised conclusion did not contradict that analysis. The Commission finally noted that the RTO’s failure to follow the MMU’s recommendations did not constitute a tariff violation, because the independence of the MMU does not require PJM to adopt every recommendation.

*FERC Orders Consensual Resolution*

FERC noted that PJM’s actions, while not a tariff violation, demonstrated sufficiently disruptive supervision to call into question the market monitor’s ability to ensure the integrity of PJM’s market operations. The Commission accordingly concluded that the RTO’s tariff must be changed in order to reform the relationship between PJM management and the MMU in a way that assures sufficient MMU independence. The Commission refused to accept PJM’s unilateral offer of settlement, reasoning that “[a] consensual resolution is most likely to restore confidence in the efficient, impartial and competitive operations of PJM’s markets and in the monitoring of those markets.”

FERC allowed the parties 14 days to decide whether they would prefer a settlement judge appointed, to use the Commission’s dispute resolution service, or to allow the Commission’s general counsel to facilitate.

**E. FERC States That No Changes Have Been Made to Its Intervention Policies for Membership Organizations -- Docket No. QM07-4-000**

On September 21, 2007, FERC issued a response to membership organizations' concern that the Commission had changed its policy on interventions. The issue arose in connection with FERC's July 18, 2007, order granting AEP a waiver from the mandatory PURPA purchase obligation. 120 FERC ¶ 61,052. ELCON and AF&PA had each intervened, protesting AEP's request. AEP asserted that neither ELCON nor AEP had standing in the proceeding.

FERC denied ELCON's motion to intervene because ELCON did not present "case-specific" arguments or state that any ELCON member was, in fact, affected by AEP's petition. FERC went further to chastise "all membership organizations that going forward, when seeking to intervene in case-specific adjudications such as this one, they are expected to confine their comments to specific factual and legal argument raised in the individual proceeding." FERC stated that it will not allow such proceedings to be used to re-litigate generic matters.

In response, ELCON and several organizations sent a joint letter to FERC Commissioners and staff on July 31 concerning the intervention rights of member organizations in FERC proceedings. In particular, ELCON noted:

the Commission's frequent use of adjudicatory proceedings to announce and implement new policy, policy changes or policy refinements requires that the Commission grant broad intervention rights. FERC frequently announces important new rules in adjudications and then applies the results reached in those adjudications prospectively thereafter as FERC policy. ... [W]ithout the intervention of national membership organizations FERC could inadvertently issue a sweeping decision apparently logical in the facts of a specific case without being advised that the issue is under consideration in other regions where markets, reliability or local regulations require a different solution.

**The Commission responded to those concerns in a September 21, 2007 Order (QM07-4), where it clarified that no change in policy had occurred, and that "membership organizations are free to continue to pursue their concerns as they have in the past."**

**FERC defended its July 18, 2007 decision to reject ELCON’s request to intervene on the grounds that ELCON had failed to show that it had members in AEP’s service territory. By contrast, FERC granted intervenor status to AF&PA because it successfully demonstrated that its members owned and operated QFs in AEP’s service territory, which therefore “may be directly affected by the outcome of the proceeding.” FERC further stated that a membership group’s concern with the precedential effect of a FERC determination in an adversarial proceeding “normally is not, by itself, a basis for intervention.”**

**FERC noted that the AEP case did not give rise to a new generic policy, but instead applied existing policy to a fact-specific case. FERC accused ELCON of trying to rehash general policy arguments it first made on rehearing of FERC’s final mandatory purchase obligation rule by resubmitting the same filing in the fact-specific AEP proceeding, “but with a cover letter.” The Commission therefore urged that its July 18 comment that membership organizations seeking to intervene in case specific adjudication “are expected to confine their comments to specific factual and legal arguments raised in the individual proceeding” be read in this context, and assured the trade groups that its intervention policies for membership organizations remain unaltered.**

**F. FERC Proposal To Grant Blanket Authorization to Certain Transactions under FPA Section 203 -- (Docket No. RM07-21)**

On July 19, 2007, FERC issued a NOPR seeking comment on a proposal to grant limited blanket authorization for certain dispositions of jurisdictional facilities. 120 FERC ¶61,062. Under section 203 (a) (1) of the FPA, a public utility, without prior Commission authorization, may dispose of less than 10 percent of its voting securities to a public utility holding company

only if, after the disposition, the holding company and any associate company will own, in the aggregate, less than 10 percent of the public utility. The Commission believes that the disposition of such limited voting interests (less than 10 percent) with the proposed “in aggregate” restriction and the existing reporting requirements applicable to holding companies will not harm competition or captive customers and will accommodate additional investment and market liquidity in the electric industry.

**EPSA, APPA and NRECA, EEI, and a group of financial institutions submitted comments on the Commission’s proposal.**

**EPSA limited its comments to support for a “narrowly defined” blanket authorization for the acquisition or disposition of a jurisdictional contract where the acquirer does not have captive customers and the contract does not convey control over the operation or a generation or transmission facility.**

**APPA and NRECA disagreed with EPSA. They argued that FERC should not allow public utilities to dispose of or acquire jurisdictional contracts, irrespective of the existence of captive customers of either the seller or the acquirer. Public power utilities and co-ops rely on jurisdictional power-purchase contracts that are “situation specific and unique.” Even where these contracts are at market-based rates, they expressed concern about their treatment as freely transferable commodities. APPA and NRECA supported addition of the 10-percent aggregate ownership limitation to the Commission’s regulations regarding blanket authorizations, but suggested that FERC require the public utility to report on all dispositions of its securities undertaken pursuant to the blanket authorization. They urged FERC not to extend the proposal to include blanket authorization for public utilities to dispose of unlimited amounts of securities to entities that are holding companies**

solely because of ownership of and EWG, FUCO or QF. Such authorization, they caution, could result in the acquisition of market power without Commission approval. They also discouraged FERC from including in the blanket authorization the transfer of unlimited amounts of securities to non-bank holding companies for the purpose of engaging in hedging transactions, even where the holding company may only vote less than 10 percent of the public utility's outstanding voting securities, because FERC's regulations do not define "hedging transactions."

The Financial Institutions Energy Group, comprised of bank and other financial institution power marketers, supported the NOPR and suggested expanding the proposed blanket authorization to include disposition of less than 10% of the voting securities of a public utility to any entity, not just a holding company. They also suggested that the blanket authorizations for the transfer of voting securities of EWGs, QFs and FUCOs, for dispositions of securities to a fiduciary, dispositions for hedging and underwriting purposes, as collateral for a loan, or for purposes of liquidation in connection with a loan be extended to acquiring entities that are not holding companies.

EEI supported the NOPR with the clarification that absent a change in control (as analyzed under the Commission's existing regulations and practice), sales of securities are not transactions subject to FERC's jurisdiction. EEI, like the financial institutions, encourages FERC to extend the blanket authorizations to cover jurisdictional transactions involving securities transferred from any public utility to any person (and not just to any holding company).

On July 19, 2007, FERC also issued a Policy Statement and another NOPR related to its merger and corporate review policies.

In the Supplemental Policy Statement (120 FERC ¶61,060, Docket No. PL07-1), the Commission provides guidance regarding future implementation of FPA section 203. The guidance reportedly is based on the Commission’s experience since amending its FPA section 203 regulations and enacting new regulations under the PUHCA 2005, and discussion at two technical conferences held in December 2006 and March 2007. Among the issues discussed in the Supplemental Policy Statement are:

- Safe harbor transactions that are unlikely to raise cross-subsidization issues.
- Deference to state-adopted protections, such as ring-fencing measures. Ring-fencing is a means of separating and protecting the financial assets and ratings of a regulated utility from the business risks of other companies in a holding company.
- Broader blanket authorizations considered on a case-by-case basis and a proposal for certain generic blanket authority addressed in a concurrent NOPR discussed below.
- Guidance regarding disposition of “control” of jurisdictional facilities.
- The Appendix A merger analysis, used to help identify instances of market power. The Commission will continue to analyze mergers by focusing on a company’s ability and incentive to exercise market power.

In the other NOPR, the Commission proposes to codify cross-subsidy pricing restrictions on power and non-power goods and services transactions between franchised public utilities with captive customers and their market-regulated power sales affiliates or non-utility affiliates. (120 FERC ¶ 61,061, Docket No. RM07-15).

**A few companies and organizations submitted comments on this NOPR. EEI expressed the view that the Commission’s exceed its jurisdiction, and criticize FERC for its failure clearly to explain the need for the proposed rules:**

**The Commission’s authority to impose the cross-subsidy constraints under FPA sections 205 and 206 is limited. These sections of the FPA provide the Commission authority to determine that jurisdictional rates are just and reasonable, and the sections do not explicitly authorize cross-subsidy or utility-affiliate transaction constraints. Therefore, if the Commission has authority to restrict the price at which non-power goods and services are**

**purchased or sold between a public utility with captive customers and its affiliates under sections 205 and 206, that authority extends only so far as necessary to ensure that the utility's wholesale and transmission rates are just and reasonable.**

**But the Commission has not demonstrated why its proposed regulations are necessary to achieve this just-and-reasonable-rate result. In the NOPR, the Commission focuses on regulating utility-affiliate transactions, rather than on wholesale rates, thereby exceeding its section 205 and 206 authority and potentially conflicting with state decisions as to such issues.**

**APPA and NRECA, on the other hand, commented that the proposed rule does not go far enough. They suggested that FERC clarify that the rule protects transmission customers as well as "captive customers" against cross-subsidization; that the final rule does not apply to electric cooperatives; and that the rule does not foreclose the Commission from imposing additional cross-subsidization restrictions on affiliate transactions on a case-by-case basis, e.g., in utility mergers. Additionally, they favor after-the-fact reporting requirements on non-power goods and services transactions covered by the proposed restrictions.**

**Occidental Power Marketing generally supported the initiative, but felt that as drafted, the proposed restrictions will not fully achieve the Commission's goal of protecting against inappropriate cross-subsidization of market regulated and unregulated activities by the captive customers of public utilities. They suggested that the affiliate transaction restrictions are written too narrowly and risk permitting a utility to engage in otherwise prohibited conduct simply by conducting all of its market-based rate activities within its franchised public utility. They also urged FERC to revise the definition of "captive customer" to treat wholesale customers that have alternatives the same as retail customers with retail choice.**

State regulators were generally in favor of FERC's proposal, particularly in the wake of the repeal of PUHCA. The New York Public Service Commission was concerned that large interstate holding companies now "have the opportunity and incentive to combine utility and non-utility businesses and to use transactions among affiliated companies to benefit the holding company and the utilities' affiliates, at the risk of increasing costs recovered from captive utility customers." They recommended that FERC require utilities to record purchases of non-power goods and services from an affiliated entity at the lower of cost or market price, and to require any utility that engages in transactions with an affiliated entity to report those transactions, along with supporting information, to FERC.

## II. COURT PROCEEDINGS

### A. Supreme Court To Review Ninth Circuit Decision Criticizing FERC's Reliance on Mobile-Sierra in Addressing Long-Term Power Contracts in California

On September 25, 2007, the Supreme Court agreed to hear petitions filed by a dozen generators and power marketers asking for review of the Ninth Circuit's December 19, 2006 decision in Snohomish P.U.D. v. FERC on the grounds that the Ninth Circuit's decision leaves FERC with excessive discretion to reform or set aside power sales contracts. (Pub. Util. Dist. No. 1 of Snohomish County v. FERC, 2006 U.S. App. LEXIS 31297 (9<sup>th</sup> Cir. 2006)).

The dispute arises from two companion decisions issued by the Ninth Circuit on December 19 of considerable significance reversing FERC's treatment of long-term power contracts entered into by the California Public Utilities Commission and the California Electric Oversight Board at the time of the California energy crisis in 2001. See Pub. Util. Dist. No. 1 of

Snohomish County v. FERC, 2006 U.S. App. LEXIS 31297 (9<sup>th</sup> Cir. 2006); Pub. Util. Comm'n of Cal. v. FERC, 2006 U.S. App. LEXIS 31140 (9<sup>th</sup> Cir. 2006).

These decisions emphasize, first, that the fundamental purpose of the rate authority that FERC exercises under the Federal Power Act is to protect consumers. The decisions are of considerable importance as FERC initiates a proceeding, prompted by ELCON and other allies, to revisit whether the wholesale markets are functioning in competitive fashion.

The Ninth Circuit found that there is a single, general standard for FERC's adjudication of contract challenges like the present one: whether the challenged contract is "just and reasonable." The question therefore cannot be not whether the Mobile-Sierra or the "just and reasonable" standard of review applies.

The original Mobile-Sierra cases, which arose in the context of sellers seeking relief from low-rate contracts, hold that lack of profitability alone is not a basis for deeming a contract unreasonable when the seller has agreed to the rate that proves unprofitable. The Ninth Circuit noted that at the time that Mobile-Sierra was adopted, FERC approved individual contracts, which the Commission does not do under the current market-based rate regime where it has pre-approved the seller on the basis that the seller has no market power.

The Ninth Circuit applied a tripartite analysis in considering whether forward contracts entered into during the western markets crisis were just and reasonable.

*First*, the court agreed with FERC that as a contractual matter the Mobile Sierra standard could be applied.

*Second*, the Ninth Circuit found that market-based rate authority *can* qualify as sufficient prior review to justify limited Mobile-Sierra judicial review only "when accompanied by effective oversight permitting timely reconsideration of market-based authorization if market

conditions change.” Here, the fatal flaw in FERC’s approach to ‘oversight’ is that “it precludes timely consideration of sudden market changes and offers no protection to purchasers victimized by the abuses of sellers or dysfunctional market conditions that FERC itself only notices in hindsight.” FERC applies the Mobile-Sierra presumption that long-term bilateral contracts will reflect just and reasonable rates, without *any* opportunity for initial review of the rates. This, according to the court, amounts to an abdication of FERC’s statutory duty to provide rate revision when necessary to assure just and reasonable rates.

The court does not deny that FERC may adopt a market-based rate regime “if sufficient safeguards are taken to provide for sufficient oversight.” However, FERC cannot use the choice of the market-based rate regime and couple with it Mobile-Sierra to adopt a process that precludes ordinary rate review, including the propriety of a grant of market-based rate authority at the time the contracts become effective.

*Third*, the Ninth Circuit held that FERC erred by adhering to Mobile-Sierra without considering market conditions at the time the contracts were formed: “Mobile-Sierra cannot apply without determination that the challenged contract was initially formed free from the influence of improper factors . . . .” While FERC acknowledged its own Staff Report concluded that the western markets were dysfunctional, FERC failed to consider whether the influence of the spot markets on the forward markets reached a level sufficient to raise the question whether two parties could negotiate a just and reasonable contract triggering the Mobile-Sierra presumption. FERC failed to consider whether the contracts in question were entered into in fully functioning markets as a prerequisite to whether Mobile-Sierra should apply.

The court found that FERC further compounded the error by applying Mobile-Sierra analysis taken from the context of low-rate challenges to high-rate challenges. In a *low rate* case

like the Sierra/Papago context, the important “public interest” concerns relate to the selling utility’s solvency and assuring that under recovered costs are not recouped from other customers. In contrast in a *high rate* challenge, the public interest requires that the consuming public not be required to pay a rate too high to fall within the zone of reasonableness.

**In the wake of the Ninth Circuit’s decisions, Californians for Renewable Energy (“CARE”) has attempted to use the rulings in Snohomish and companion cases to set aside contracts among California energy market participants. FERC on September 24, 2007, dismissed CARE’s complaints challenging the reallocation of a contract between California’s Department of Water Resources and the City and County of San Francisco (EL07-49) to Pacific Gas and Electric, and also challenging a purchase agreement between Southern California Edison and Blythe Energy (EL07-50).**

CARE had argued that Snohomish further eroded the legal basis for FERC’s market based rates program, such that only prices filed with FERC in advance may now enjoy Mobile-Sierra protection. FERC rejected this interpretation by noting that Snohomish specifically acknowledged “market-based rate authority *can* qualify as sufficient prior review to justify Mobile-Sierra review.” Rather, FERC wrote that the Ninth Circuit in Snohomish reversed FERC for failing to consider market failures in determining whether Mobile-Sierra protection should apply to the contracts in issue. In dismissing CARE’s complaint, FERC enumerated several improvements to its market-based rate program in the years after the Western Energy Crisis.

The crux of the recent petitions for *certiorari* is that the Ninth Circuit’s ruling in Snohomish and its companion cases departed both from other court rulings and that the decision effectively renders market-based rate approval useless by eliminating Mobile

Sierra protection except when FERC reviews a contract in advance of its taking effect. Petitioners assert that the decisions overturn long-term power contracts and will result in a flood of complaints from disgruntled purchasers seeking to reform what in hindsight turned out to be a bad deal, even if not in the public interest. They also worry that going forward, application of the decision will result in differing review standards for buyers and sellers of power. Sellers, they fear, may be subject to an unfavorable public interest standard when they challenge a low rate, whereas buyers may seek to apply a more favorable “zone of reasonableness” standard when they challenge a high rate, leaving the Mobile-Sierra doctrine “in the historical dustbin”.

FERC’s brief to the Court denies that the Mobile-Sierra doctrine or its market-based rate program have been undone by the Ninth Circuit ruling in Snohomish. FERC argued that the Ninth Circuit in Snohomish merely applied the principles of the Mobile-Sierra doctrine to the highly unusual situation created by the 2000-2001 western energy crisis. “Taken as a whole, the decisions of the Court of Appeals allow the Commission sufficient discretion on remand to consider all relevant factors in determining whether the contracts at issue should be upheld or reformed . . . .” FERC states that petitioners overstate the breadth of the court of appeals decisions and assert that further review is unwarranted.

In a joint brief, Snohomish, Nevada Power, Sierra Pacific Power, Golden State Water, and the Nevada attorney general opposed granting certiorari on the grounds that FERC reforms enacted in response to the California energy crisis have been effective. They also argue that FERC has sufficient discretion under the Snohomish ruling to adhere to market-based rates and intervene only when there are obvious flaws in the market. The

**California Public Utilities Commission and the California Electricity Oversight board in a separate brief opposed granting certiorari because FERC's reforms have not yet had the chance to be tested.**

**Chief Justice John Roberts and Justice Stephen Breyer did not participate in the decision granting certiorari in the Snohomish Case. This raises the possibility that they may have had to recuse themselves in both the decision to hear the case and in the case itself.**

**B. AF&PA Files Petition for Review with D.C. Circuit Challenging FERC's New Rules Implementing PURPA Sec. 210(m) (Case No. 07-1328)**

**On August 16, 2007, the American Forest & Paper Association filed a petition for review in the D.C. Circuit challenging FERC's new rules implementing PURPA Section 210(m) establishing the procedures and conditions under which a utility may seek relief from PURPA mandatory QF purchase obligations. (Order Nos. 688, 117 FERC ¶61,078 (October 20, 2006) and 688A, 119 FERC ¶61,305, (June 22, 2007).)**

The rules in question represent FERC's fulfillment of Congress' mandate in EAct 2005 to grant utilities waivers from the PURPA QF purchase obligation if certain conditions described in the statute are met. The Final Rule (Order No. 688) was only slightly modified by the rehearing order. The Final Rule represented a compromise between utility and QF interests. FERC found that the section 210(m)(1)(A) of the statute did not require a showing of competitive markets as a prerequisite to relieving utilities from purchases obligations in the four Day 2 markets. However, in a change from the NOPR favorable to QF interests, FERC recognized several showings related to operational characteristics or transmission constraints that QFs above 20 MW could rely on to rebut a presumption of access to markets. QFs below 20

MW are rebuttably presumed not to have access to markets. Additionally, the Final Rule was favorable to ELCON and QF interests by requiring a “facility-specific” determination of access and by requiring that utilities provide information on transmission constraints and congestion that would not otherwise be available to QFs.

ELCON filed a short rehearing request, but others including AF&PA, the Cogeneration Association of California and CIBO submitted more extensive rehearing requests. The utilities also sought rehearing, complaining in particular about informational requirements.

In a key passage in the rehearing Order, FERC explains: “Congress could have stated a broad general finding to be made by the Commission such as ‘workably competitive markets.’ Instead Congress tailored subparagraphs (A) and (B) to establish criteria specific to each market design...”. Order No. 688-A at para. 47. “While it is true that EPACT 2005 did not repeal PURPA or the Commission’s obligations to encourage QF development, enactment of section 210(m) of PURPA clearly changes the rights of QFs under PURPA. The Commission has no discretion other than to terminate the purchase requirement if it finds that a QF has nondiscriminatory access... It would be inappropriate for the Commission to ignore this mandate... in a way that undermines the specific standards of relief that Congress chose to establish in the statute.” *Id.*, at para. 48.

Perhaps the most important change is that where there is credible evidence in a complaint that OATT is being violated, access to transmission will not be presumed.

In the Rehearing Order, FERC rejected AF&PA and CCC’s argument that Congress intended that there be a meaningfully competitive market prior to terminating a QF’s purchase obligation and that such markets that do exist are predominantly for resale and very short-term.

FERC finds that on the basis of EQR reports long-term contracts do exist in the Day 2 markets. RTOs have no incentive to favor one set of suppliers over others in providing transmission access. FERC finds that the existence of a spot market as an alternate source for power reduces the costs to buyers and sellers of long-term bilateral supply commitments. FERC stresses most heavily the different standard that Congress applied in Section 210(m)(1)(B)(ii) which requires a finding of access to “competitive wholesale markets that provide a meaningful opportunity to sell capacity, including long-term and short-term sales, and electric energy including long-term, short-term and real tie sales.” Such language is not contained in (A)(ii) which only requires access to markets. Order No. 688-A, at para. 24. Even if Day 2 long-term markets are nascent, Congress in (A)(ii) only required that the Commission finds that they exist, not that they be robust. *Id.*, at para. 26, 28.

Without much rationale, FERC finds that the one-year term used for EQR reports is sufficient to meet the statutory requirement that there be “wholesale markets for long-term sales of capacity and energy” within the meaning of section 210(m)(1)(A)(ii), *id.*, at para. 27. FERC does mention that it is trying to improve the quality of the markets and opportunities for long-term contracting.

With respect to CAISO and SPP, Congress required termination of purchase obligations if a QF has nondiscriminatory access to (i) transmission provided by an RTO and (ii) “competitive wholesale markets providing a meaningful opportunity to sell long-term and short-term capacity to buyers other than the interconnecting utility.” As in the final rule, FERC finds that CAISO and SPP have only been found to satisfy the first prong, and “the issue of whether ‘competitive wholesale market’ exist will be an issue in the proceeding and the burden will be on the applicant to make the required demonstration.”

The Commission reaffirmed that ERCOT offers a market of comparable quality to the Day 2 and Day 1 markets.

FERC reaffirms that the presumptions of access may be rebutted where a particular QF has operational characteristics that effectively prevent its participation in a market or lacks access to a mechanism to schedule transmission service or make advance sales on a consistent basis. Order 688-A, at para. 66. Further, utilities will be required to submit information on transmission constraints, levels of congestion and interconnections to enable the QF to have access to relevant information. Id., at para. 67.

In a change from Order 688, on rehearing the Commission provides that while the complaint process is the preferred mechanism to adjudicate transmission disputes, especially since the Commission has only 90 days to act under 210(m), “where there are pending complaints raising credible issues concerning a transmission provider’s implementation or administration of its OATT, the Commission will also consider that fact...when evaluating whether a QF does in fact have nondiscriminatory access to that market. FERC rejected CAC’s comment that OATT does not guarantee physical transmission rights; the Commission regards financial transmission rights as supplementary.

With respect to the obligation to provide backup power, FERC reaffirms the statement made in the final rule (responsive to ELCON’s comments) that “lifting the obligation from a particular utility to purchase electric energy from a QF did not relieve such utility of its obligation to sell backup, standby and supplemental power.” Id., at para. 123. However, FERC imposes no requirement that rates for replacement power are reasonable since FERC has no jurisdiction over retail rates. Id., at para.127.

**The Central Vermont Public Service Corporation, the Cogeneration Association of California and the Energy Producers and Users Coalition have filed motions to intervene in the case. ELCON plans to file an *amicus* brief in support of the petitioner to address FERC's poor rationale for finding long-term markets and possibly raise other issues ELCON raised in the proceeding before FERC.**

**The Court has not yet set a schedule for briefing and oral argument.**

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