UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

California Independent System Operator Corporation, California Electricity Oversight Board, Public Utilities Commission of the State of California, Pacific Gas and Electric Company, San Diego Gas & Electric Company, and Southern California Edison Company,	)	
Complainants,	)	
v.	)	Docket No. EL02-15-000
Cabrillo Power I LLC, Cabrillo Power II LLC, Duke Energy South Bay, LLC, Geysers Power Company, LLC, and Williams Energy Marketing and Trading Company,	)	
Respondents.	)	
California Independent System Operator Corporation, California Electricity Oversight Board, Public Utilities Commission of the State of California, and San Diego Gas & Electric Company,	)	
Complainants,	)	
v.	)	Docket No. EL03-22-000
Cabrillo Power I LLC,	)	
Respondents.	)	

COMPLAINANTS' REQUEST FOR REHEARING OF ORDER DISMISSING COMPLAINTS

Pursuant to Section 313(a) of the Federal Power Act (FPA), 16 U.S.C. § 825l(a) (2000), and Rule 713 of the Rules of Practice and Procedure of

the Federal Energy Regulatory Commission (FERC or Commission), 18 C.F.R. § 385.713 (2004), the California Independent System Operator Corporation (CAISO), Pacific Gas and Electric Co. (PG&E), Southern California Edison (SCE), San Diego Gas and Electric Company (SDG&E), the California Electricity Oversight Board (EOB), and the California Public Utilities Commission (CPUC) (collectively, Complainants) hereby submit a request for rehearing of the Commission's June 3, 2005, Order Dismissing Complaints, in the above-captioned dockets. *California Independent System Operator Corp. v. Cabrillo Power I, LLC,* 111 FERC ¶ 61,358 (2005) (June 3 Order). [1]

The June 3 Order dismissed complaints filed on November 1, 2001, and October 30, 2002 (the Complaints), which alleged that a component of the rates payable under certain "reliability must-run" (RMR) contracts – the "Fixed Option Payment" – was excessive and that the resulting rates were therefore unjust and unreasonable. At that time, the issue of how to properly calculate the Fixed Option Payment under the RMR contracts was pending before the Commission on exceptions to an Initial Decision (Mirant Initial Decision) in Docket Nos. ER98-495-000, et al. (the Mirant Dockets). [2] Thus, the Complainants requested that the Commission set refund effective dates but defer further action until a final ruling was issued in the Mirant Dockets. [3]

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[1] Williams Energy Marketing & Trading Company has reached settlement with SCE and CAISO covering the issues raised in the Complaints and is no longer a respondent in this proceeding. *See Williams Energy Marketing & Trading Company*, 105 FERC ¶ 61,165 (2003). Similarly, Duke Energy South Bay is no longer a respondent in this proceeding because it executed a settlement and release of claims agreement with SDG&E and CAISO resolving the issues in the Complaints on June 29, 2005.

[2] *Pacific Gas and Elec. Co.*, 91 FERC ¶ 63,008 (2000).

[3] The Complainants requested a refund effective date of January 1, 2002, in Docket No. EL02-15 and January 1, 2003, in Docket No. EL03-22. The Commission never set a refund effective date; the Complainants stand by their original requests as to the refund effective dates.

The Commission has now issued a final ruling in the Mirant Dockets, [4] and, based on that ruling, dismissed the Complaints at issue here. The Complainants respectfully request rehearing and reversal of that order of dismissal because it incorrectly characterized the request for relief in those Complaints and erroneously determined that there was no basis for the requested relief.

I. SPECIFICATION OF ERROR

The Commission's dismissal of the Complaints in the June 3 Order was arbitrary, capricious and an abuse of discretion because the Commission failed to provide a reasoned explanation for its action. Additionally, it was plain error for the Commission to dismiss the Complaints because a genuine, redressible dispute exists between the parties – a dispute that could result in tens of millions of dollars in refunds to customers of PG&E and SDG&E.

Specifically, the Commission erred in concluding that the Complainants sought to have the Commission find the rates from the April 1999 Settlement unjust and unreasonable "*based on the [Mirant] Initial Decision.*" [5] This determination incorrectly characterizes the basis for the Complainants' requested relief. The Complainants' request for relief was grounded in the rights they retained in an April 1999 Settlement to seek, under Sections 205 and 206, adjustment of the Fixed Option Payments beginning January 1, 2002. This Section 206 right to request the Commission to determine the proper Fixed

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4 *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Services*, 111 FERC ¶ 61, 354 (2005).

5 June 3 Order, 111 FERC at P 1 (emphasis added).

Option Payment exists independently of and without regard to the Mirant Initial Decision.

As the Complaints stated, the Complainants anticipated that the Commission's decision on exceptions in the Mirant Dockets would have provided relevant precedent for the resolution of the issues raised in the Complaint dockets. [6] Based on the Commission's action with respect to the Mirant Dockets, no such precedent will be established. That does not mean, however, that the Complaints can be summarily dismissed. To the contrary, that fact mandates that the Commission set the issues raised in the Complaints for hearing.

The June 3 Order also seems to suggest that differences among the RMR contracts justified dismissal of the Complaints, reasoning that those differences preclude a generic approach to the Fixed Option Payment issue. Even if the Commission were to conclude that some or all of the issues raised in the Complaints are conceptually distinct for each RMR unit, the Commission's proper course of action would be to sever the proceedings for individualized consideration, not to dismiss the Complaints.

II. PROCEDURAL HISTORY

A. Origins of the RMR Contracts and the April 1999 Settlement

Since the beginning of the restructuring process in California, it has been recognized that certain generating units, because of their location and the configuration of the transmission system, are needed to provide energy or ancillary services during certain hours to assure the reliable operation of the

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[6] The Presiding Administrative Law Judge who issued the Mirant Initial Decision concluded that it was appropriate to issue both "case-specific" and "generic" rulings in the Mirant Dockets. 91 FERC at p. 65,117.

CAISO-controlled grid. It has also been recognized that the same units would be able to exercise locational market power during those hours. The underlying purpose of the RMR contract is to assure that CAISO will be able to call upon these units when it needs them for reliability purposes or to manage intra-zonal congestion and that their owners will not be able to exercise market power by withholding the output of the units or obtaining prices that include monopoly rents. Accordingly, in seeking authorization from FERC, pursuant to restructuring orders issued by the CPUC, to make sales at market-based rates from what were then their own generating units, SDG&E, PG&E, and SCE proposed that units that could otherwise exercise locational market power be made subject to must-run contracts with CAISO.

By order issued October 30, 1997, the Commission approved the companies' market-power mitigation measures, including the RMR contracts. [7] On October 31, 1997, the companies tendered for filing in Docket Nos. ER98-441 (SCE), ER98-495 (PG&E), and ER98-496 (SDG&E) unexecuted must-run contracts for the units that had been designated by CAISO as RMR units. The terms of those contracts were substantially uniform, but each contract reflected the individual costs and operating characteristics of the units it covered. [8] On December 17, 1997, the Commission accepted the contracts for filing, set them for hearing, and allowed them to go into effect – subject to refund – with the commencement of CAISO operations on March 31, 1998. [9]

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7 *Pacific Gas and Elec. Co.*, 81 FERC ¶ 61,122 (1997).

8 CAISO had filed a *pro forma* version of the contract in March 1997 and amended that version in August 1997. *Id.* at p. 61,557.

9 *Pacific Gas and Elec. Co.*, 81 FERC ¶ 61,322 (1997).

Thereafter, in 1998 and 1999, the three utilities divested themselves of the RMR units, other than certain units owned by PG&E. In each instance, the new owner (or other entity entitled to dispatch the RMR units) assumed the rights and obligations of the divesting utility under the RMR contract. [10] Under sections 5.2.7 and 5.2.8 of its tariff, CAISO bills the "Responsible Utility" for the costs paid by CAISO under the RMR contract for a given unit. The Responsible Utility is the utility in whose service area the unit is located. Ultimately, these costs become the responsibility of the ratepayers in that utility's service area. It is those customers who will benefit from any refunds that result from these dockets.

B. The April 1999 Settlement and Current *Pro Forma* RMR Contract

In April 1999, parties representing a broad cross section of affected interests, including all of the Complainants and respondents listed above, reached a partial settlement, the April 1999 Settlement, on many terms of a new *pro forma* RMR contract to supersede the contracts then in effect and on the unit-specific rates and terms that would apply under that contract for each of the units then designated as RMR. [11] The new *pro forma* RMR contract, with limited variations primarily to accommodate unit-specific characteristics, has been the basis for all the CAISO RMR contracts. These contracts are for a one-year term, renewable each year at the discretion of CAISO.

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[10] *Duke Energy South Bay, LLC*, 86 FERC ¶ 62,251 (1999).

[11] *California Indep. Sys. Operator Corp.*, 87 FERC ¶ 61,250 (1999). Additional *pro forma* terms were agreed in a later settlement among the same parties. *California Indep. Sys. Operator Corp.*, 93 FERC ¶ 61,089 (2000).

The issue raised by the Complaints, how to properly calculate the so-called Fixed Option Payment, arises when RMR units operate under what the RMR contract refers to as Condition 1. [12] In that circumstance, an RMR unit participates fully in markets and bilateral contracts as a merchant unit, and the owner retains all the resulting revenues from its market transactions. However, when called upon by CAISO to be dispatched, the RMR unit must be available to produce energy or ancillary services and must generate the required output. If already producing output for a transaction, the unit must continue to generate the specified output for the period required by CAISO unless a greater output is called for by CAISO, in which case the unit must ramp up to that higher level.

For providing reliability dispatch, the RMR unit owner receives both its variable costs and a Monthly Availability Payment. As the name suggests, the Monthly Availability Payment is a payment received for the fixed costs of remaining available to provide reliability dispatch, whether or not CAISO calls upon it. [13] The Fixed Option Payment is the annual sum of Monthly Availability Payments, which in the *pro forma* RMR contract is the product of a Fixed Option Payment Factor (FOPF) and the RMR Unit's Annual Fixed Revenue Requirement (AFRR). [14]

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[12] *See* RMR *Pro Forma* Contract Section 3.1, *filed in* Second Stipulation and Agreement, Southern California Edison Co., *et al.*, Docket No. ER98-441-022 (August 14, 2000).

[13] The alternative operating condition under the *pro forma* RMR contract is Condition 2. Under Condition 2, an RMR unit is no longer operated as a merchant unit. It produces energy or ancillary services only when dispatched by CAISO for local reliability. In exchange, the RMR contract specifies that owners of RMR units under Condition 2 are paid their full cost of service, i.e., all variable and fixed operating costs and return of and on capital. The owner cannot retain any market or non-RMR contract revenue it receives for the output of units under Condition 2. Fixed-cost payments for Condition 2 RMR Units are not at issue here. The decision whether to operate under Condition 1 or Condition 2 is made by the facility owner.

[14] *See* RMR *Pro Forma* Contract, Schedule B. The RMR Agreement uses the term Monthly Availability Payment, while the April 1999 Settlement refers to the Fixed Option Payment, the sum of the monthly payments. In addition to the basic formula stated above, the availability

The April 1999 Settlement locked in place most rates for a period ending December 31, 2001 (the "Rate Freeze Period"). This included an FOPF, which as part of that settlement was established on an interim basis, pending resolution through litigation or settlement, and subject to either refund or surcharge depending on the final FOPF and resulting adjustment, if any, to the Fixed Option Payment. The April 1999 Settlement reserved for litigation a number of issues relating to the new contract, along with certain issues relating to the old contracts. Among the unresolved issues was the level of the Fixed Option Payment. The Commission approved the settlement on May 28, 1999, and the new contracts took effect on June 1, 1999. [15]

The FOPFs for all RMR units other than those owned by Mirant were set under various settlements entered into in 1999 and 2000 and approved by the Commission. However, under the terms of the April 1999 Settlement, these rates were subject to change after December 31, 2001, the end of the Rate Freeze Period, through proceedings under FPA Section 205 or Section 206. Mirant chose to litigate the FOPF issue, which resulted in the Mirant Initial Decision.

C. Mirant Settlement

A settlement was filed with the Commission on January 31, 2005, that settled several Mirant-related RMR proceedings, one of which had led to the Mirant Initial Decision. [16] The Mirant Settlement provided that, following

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payment is adjusted for actual availability of the RMR Unit, e.g., an Owner is paid less when its unit is not available when called upon by CAISO.

[15] *California Indep. Sys. Operator Corp.*, 87 FERC at pp. 61,968-70.

[16] *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Service*, 111 FERC ¶ 61,017 (2005) (Mirant Settlement).

Commission approval of that settlement, Mirant and PG&E would cooperate to request that the Commission rule on the merits of the Mirant Initial Decision. The Commission denied the request for a ruling on the merits, finding that the matter was moot. [17] The Commission terminated the proceedings that led to the Mirant Initial Decision and denied rehearing of the termination of the Mirant Dockets. [18] Concurrent with the denial of rehearing in the Mirant Dockets, the Commission issued the June 3 Order dismissing the Complaints at issue here.

III. LEGAL STANDARD FOR PROPER COMMISSION DECISIONMAKING

Section 706(2)(A) of the Administrative Procedure Act (APA) prohibits agency action that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." [19] The Commission's determinations must be "the result of reasoned and principled decisionmaking that can be ascertained from the record." [20] Likewise, "it is imperative that the Commission articulate the critical facts upon which it relies" in support of its decision. [21]

IV. ARGUMENT

A. The Commission Incorrectly Interpreted the Requests for Relief in the Complaints

The Commission erred in concluding that the Complainants sought to have the Commission find the rates from the April 1999 Settlement unjust

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[17] *Id.* at P 19-20.

[18] *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Service*, 111 FERC ¶ 61,354 at P 25, 31 (2005).

[19] 5 U.S.C. § 706(2)(A) (1994); *see Wisconsin Valley Improvement Co. v. FERC*, 236 F.3d 738, 742 (D.C. Cir. 2001); *Sithe/Independence Power Partners v. FERC*, 165 F.3d 944, 948 (D.C. Cir. 1999).

[20] *Tarpon Transmission Co. v. FERC*, 860 F.2d 439, 442 (D.C. Cir. 1988).

[21] *Columbia Gas Transmission Corp. v. FERC*, 628 F.2d 578, 593 (D.C. Cir. 1979); *see Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 851 (D.C. Cir. 1970).

and unreasonable "*based on the [Mirant] Initial Decision.*" [22] This determination incorrectly characterizes the Complainants' requested relief and the basis for that relief. Though the Complaints followed temporally the Mirant Initial Decision and relied on the reasoning of that decision in support of its allegations, the Mirant Initial Decision did not constitute the grounds for the Complainants' request for relief. Instead, the request was grounded in the rights the parties retained in the April 1999 Settlement to seek, under Sections 205 and 206 of the FPA, adjustment of the Fixed Option Payments effective January 1, 2002, and in their conclusion that Fixed Option Payments that are in excess of the net incremental costs of the RMR unit owners are excessive and therefore unjust and unreasonable.

Specifically, the Complaints clearly asserted a basis for relief that is independent of the Mirant Initial Decision:

> The Fixed Option Payments currently in effect . . . exceed the levels allowable under the net incremental cost method. To that extent, *i.e.*, to the extent that they actually place the owner of the RMR unit in a *better* position than it would be in if it lacked localized market power and were not subject to an RMR contract, those rates are manifestly unjust and unreasonable. [23]

To be sure, the Complainants recognized at the time of filing that the Commission was already in the process of addressing the proper methodology for the calculation of the Fixed Option Payment under the RMR contracts and that an Initial Decision had accepted net incremental cost as the appropriate

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[22] June 3 Order, 111 FERC at P 1 (emphasis added).

[23] Complaint, Docket No. EL02-15, at 4 (emphasis in original).

basis for the FOPF, asserting that the ruling in that respect was "generic." [24] Thus, in the interest of administrative efficiency, Complainants suggested that the Commission hold the Complaints in abeyance pending a final Commission decision on the Mirant Initial Decision. [25] The Complainants contemplated that this case would "proceed to adjudication on those issues that remain[ed]" following the resolution of the exceptions to the Mirant Initial Decision. [26] In so doing, however, Complainants in no way asserted that their claims for relief depended on the Mirant Initial Decision becoming a final Commission decision.

In short, the Complainants' Section 206 right to ask the Commission to determine the proper methodology for calculating the Fixed Option Payment exists independently and without regard to the Mirant Initial Decision. While a final Commission's decision in the Mirant Dockets could have provided relevant precedent, [27] the fact that the Commission concluded that case was moot does not mean that the issues raised in the Complaints can be summarily dismissed. To the contrary, that fact mandates that the Commission set the Complaints for hearing and final decision.

B. The Commission Failed to Provide a Reasoned Explanation for Dismissing the Complaints

In addition to erring in its characterization of Complainants' requested relief, the Commission's June 3 Order was arbitrary, capricious, and an abuse of discretion because the Commission did not provide a clear

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[24] 91 FERC at p. 65,117.

[25] Complaint, Docket No. EL02-15, at 4.

[26] *Id.* at 21.

[27] *Id.*

explanation of its rationale or underlying assumptions. [28] The Commission noted that Initial Decisions do not create binding precedent and that the Mirant Initial Decision was "fact-specific" to the Mirant RMR units. [29] The Commission thus concluded that the Mirant Initial Decision did not provide a basis for an investigation in the instant dockets. [30] Dismissing these Complaints based on a settlement agreement in another case, with different parties and different facts – without any consideration of the law and facts as they apply to Complainants – is arbitrary and capricious. [31]

A Section 206 complaint need only establish that a party seeking an investigation into existing rates has some basis to question the reasonableness of the rates charged. [32] The Complaints at issue here plainly meet this standard. They assert that, in light of the purpose of RMR contracts – namely, to mitigate the market power of generating units needed to maintain local reliability – "the Fixed Option Payment cannot lawfully exceed the sum of the costs (other than the opportunity cost of not being able to exact monopoly rents) that are imposed on the owner by virtue of operating under the RMR contract." [33]

As outlined in the Complaints, in general terms, the net incremental cost method calculates the Fixed Option Payment to make the

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[28] *See Sithe/Independence Power Partners, L.P. v. FERC*, 165 F.3d 944, 949 (1999).

[29] June 3 Order at P 24.

[30] *Id.*

[31] *See City of Holyoke Gas & Elec. Dept. v. FERC*, 954 F.2d 740, 743 (D.C. Cir. 1992) (finding that it was inappropriate for the Commission to rely upon a prior similar case to determine rate methodology when that case did not even "purport to find" the requisite facts as they applied to the City of Holyoke and remanding despite the fact that the Commission's methodology may have been reasonable).

[32] *See Sithe*, 165 F.3d at 951-52 (determining that the case should be remanded because the Commission failed to provide a reason why the Section 206 burden was not satisfied).

[33] Complaint, Docket No. EL02-15, at 15; also incorporated by reference in Complaint, Docket No. EL03-22, at 8.

owner (or operator) whole for the costs, including opportunity costs, imposed upon the owner as a result of its obligations under the RMR contract. [34] There are four incremental costs to RMR owners that arise out of the RMR contracts: (1) administrative costs, (2) certain costs of keeping a unit operational for short periods, (3) the net costs of operating and maintaining certain units that would otherwise shut down, and (4) certain opportunity costs of having to run when dispatched by CAISO. [35] There are certain offsetting benefits of running at CAISO's expense in low-load hours. [36]

Through declarations accompanying the Complaints, each of the Responsible Utilities analyzed the incremental costs for the RMR units in its service territory. These calculations were explained and set forth in the declarations of Laura Douglass for PG&E and Ali Yari for SDG&E, which were attached to the 2001 Complaint as Appendices E and F, respectively. As explained in those declarations, Ms. Douglass and Mr. Yari concluded that the respective Fixed Option Payments then in effect for the units that were the subject of the Complaints were likely well above the net incremental fixed costs for those units.

These allegations are more than sufficient to raise a question as to whether the resulting rates should be found by the Commission to be unjust and unreasonable. Moreover, no facts have come to light since the Complaints were filed that change the assessments they contain. The requirements of Section 206 are, therefore, fully satisfied. Assuming the Commission establishes the

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[34] Complaint, Docket No. EL02-15, at 3.

[35] *Id.* at 16.

[36] *Id.*

Complainants' requested refund effective dates [37] and adopts the requested net incremental cost methodology, PG&E estimates that its ratepayers would receive refunds of more than $50 million, before interest, from RMR unit owners in its service territory with whom no settlement of this issue has been reached. Similarly, SDG&E estimates that its ratepayers would be entitled to refunds of approximately $13.5 million, before interest. [38]

In dismissing the Complaints, the Commission left unaddressed these specific and comprehensive allegations. Moreover, the Commission, by its own account, did not consider the merits of the Mirant Initial Decision following the Mirant Settlement, and thus did not create generic policy for application in the instant dockets. Yet, contrary to its own reasoning, the Commission has proceeded as though the settlement in the Mirant Dockets somehow created binding precedent warranting dismissal of these Complaints. In so doing, the Commission has failed to make "a reasoned decision based upon substantial evidence in the record of these dockets." [39] Indeed, no evidence in the record, nor any case law developed under the FPA, supports the dismissal without investigation or hearing into the facts alleged in the Complaints.

C. Unique Circumstances May Warrant Independent Dockets, But Not Dismissal

The June 3 Order notes that there are some unit-specific terms and conditions in particular RMR contracts and seems to suggest that, as a result, the issue of an appropriate method for setting the Fixed Option Payment does

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[37] *See* note 3 *supra.*

[38] PG&E and SDG&E are fully prepared to document these estimates in further proceedings in these dockets.

[39] *Town of Norwood v. FERC,* 962 F.2d 20, 22 (D.C. Cir. 1992).

not lend itself to consideration in a single proceeding. Complainants believe that, despite some limited differences among RMR contracts, the analysis underlying the question whether an FOPF payment that exceeds net incremental costs is unjust and unreasonable is the same for all RMR units. However, even if the Commission were to find that contractual differences warrant separate proceedings on this issue, the Commission's proper course of action is to sever the matters for individual adjudication, not to dismiss the Complaints. Indeed, the Commission has often severed dockets where it has determined that differing issues of fact warranted separate consideration of some or all issues. [40]

Here, Complainants believe the rate methodology should be uniform for all RMR units, thus justifying a consolidated proceeding on that issue. The Commission or a Presiding Administrative Law Judge may reach a contrary conclusion. In that event, a severance order can be tailored to address individualized issues. The remedy of dismissal, however, is arbitrary, capricious and without support in the Commission's own precedents.

CONCLUSION

For the reasons presented above, the Commission should reverse its decision to dismiss the complaints in Docket Nos. ER02-15-000 and ER03-22-000, promptly institute proceedings pursuant to FPA Section 206 to investigate the rates related to the Fixed Option Payment payable by CAISO under the

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[40] *See, e.g., Investigation of Certain Enron-Affiliate QF's*, 106 FERC ¶ 63,037, at P 4 (2004) (finding good cause to sever two dockets because it would "permit the efficient and expeditious resolution of the remaining issues" with regard to the severed parties); *Pacific Gas & Elec. Co.*, 89 FERC ¶ 63,003, at p. 65,003 (1999) (ordering severance because there were unique issues for several parties that would "require different factual showings and that may require a different methodology" in each case in order to produce a reasonable rate); *Southern California Edison Co.*, 82 FERC ¶ 63,011, at p. 65,023 (1998) (finding that administrative efficiency and the public interest would best be served if non-rate terms and conditions that were not rate related and unit specific were severed for separate hearing).

respective RMR contracts, and set the requested refund effective dates for both dockets.

Respectfully submitted,

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Dated: July 5, 2005

CERTIFICATE OF SERVICE

I hereby certify that I have, this 5th day of July 2005, caused to be served a copy of the foregoing Request for Rehearing upon all parties listed on the official service list compiled by the Secretary of the Federal Energy Regulatory Commission in this proceeding.

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