

FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, D.C. 20426

August 31, 2005

In Reply Refer To:
PJM Interconnection, L.L.C.
Docket No. ER05-1181-000

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Dear Mr. Spector:

1. On July 1, 2005, pursuant to section 205 of the Federal Power Act,¹ PJM Interconnection, L.L.C. (PJM) submitted revised tariff sheets to Schedule 9 of its Open Access Transmission Tariff (OATT) to change the rate design of PJM's administrative cost recovery from formula rates to stated rates.² PJM also submitted revised sheets to the PJM Amended and Restated Operating Agreement (Operating Agreement) to revise and clarify the terms concerning the provision of information by PJM to the PJM Finance Committee and the advisory role of the Finance Committee.³ As discussed below, the Commission finds PJM's proposed rate design change deficient under its regulations until PJM provides the necessary cost-of-service data. With regard to the proposed amendments to the Operating Agreement, the Commission will accept such amendments subject to the conditions discussed below.

2. Notice of PJM's filing was published in the *Federal Register*, 70 Fed. Reg. 41,217 (2005), with interventions or protests due on or before July 22, 2005. The parties who filed motions to intervene, protests, and comments are listed in Appendix C. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2005), the timely motions to intervene serve to make the entities that filed them parties to this proceeding. Given the early stage of this

¹ 16 U.S.C. § 824d (2000).

² See Appendix A.

³ See Appendix B.

proceeding and the absence of any undue prejudice or delay to any party, also pursuant to Rule 214, the Commission will grant out-of-time unopposed motions to intervene. PJM filed an answer on August 5, 2005. Under Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 213(a)(2) (2005), answers to protests are not accepted unless otherwise ordered by the decisional authority. The Commission will accept PJM's answer because it further clarifies the issues.

3. With respect to its proposal to convert from formula to stated rates, PJM asserts that the proposed stated rates for each PJM service is equal to or less than the rate produced under the existing formula rate under the PJM 2005 budget. Overall, according to PJM, on a per megawatt hour (MWh) composite basis for all service categories, the average rate per MWh under the stated rate proposal would be approximately \$0.39/MWh, compared to a budgeted 2005 composite charge under the existing formula rates of \$0.40/MWh.⁴ PJM contends that its proposed stated rates will facilitate PJM's ability to provide the highest quality of service to its members at the lowest possible cost and will make PJM's management of administrative costs more transparent. As a result, PJM asserts, it will be more accountable both to the Commission and to its members. PJM also contends that stated rates will bring cost control, rate predictability and stability to customers and that its proposal is consistent with Commission policy concerning regional transmission organization (RTO) cost transparency and accountability. PJM states that since it is "only changing the rate design for recovery of its administrative costs from formula rates to stated rates, and therefore is not proposing a rate increase," it filed pursuant to the Commission's abbreviated filing requirements set forth at 18 C.F.R. §§ 35.13(a)(2)(iii) and 35.13(b)-(c) (2005).⁵

4. Numerous protesters object to PJM's filing, with the most significant issue being the lack of support for the proposed rate change from formula rates to stated rates. In its answer, PJM maintains that the vast majority of its 350 members support stated rates, and that such rates will provide greater rate certainty and accountability. PJM argues that a full rate proceeding is not appropriate for a not-for-profit RTO, with stakeholder committees, and points out that even those requesting additional information express a desire to avoid the time and expense of a full rate proceeding. Instead, PJM proposes that the Commission accept the filing, subject to a nominal

⁴ Exhibit PJM-4 at 3. PJM explains that, under the existing formula rate, with the exception of Schedule 9-1 (Control Area Administration Service, which is billed monthly based on actual expenses), based on its annual budgeted costs, each year PJM fixes a monthly charge that remains constant for that year for each schedule; thus, for these service categories the rates change once per year. Exhibit PJM-4 at 7-8.

⁵ PJM Transmittal Letter at 2.

suspension, and allow PJM and the representatives of the Finance Committee to review additional information, with a subsequent report submitted to the Commission.

A. Deficiencies with PJM's Filing

5. The Commission finds PJM's use of the abbreviated filing procedures to be patently deficient under its regulations. As noted above, PJM filed pursuant to § 35.13(a)(2)(iii) which provides an abbreviated filing procedure for filings that do not provide for a rate increase. This section permits the omission of cost of service data for filings in which the new rate is the same or lower than the existing rate, thereby clearly benefiting (or at least not harming) customers.⁶ The outcome PJM seeks in the instant filing is not simply a rate decrease covered by § 35.13(a)(2)(iii) because PJM seeks to replace a formula rate with stated rates. There is no way, in the instant case, to know whether a stated rate is, per se, lower or higher than a formula rate because a formula rate produces varying rates over time as costs change, while a stated rate, by definition, applies the same rate. It is the formula for calculating a rate that is itself the rate, not the number that results from the formula.⁷ Therefore, although the existing formula resulted in a composite charge of \$0.40 (based on 2004 data to be applied during 2005), and the proposed stated rate would be \$0.39, this is not necessarily a rate decrease but a rate design change in which the stated rate simply happens to be lower than the product of the formula rate at a particular time.⁸ Thus, despite PJM's assertions,⁹ it has not satisfied the threshold filing requirements.

6. In such a circumstance, where a utility proposes to change from a formula rate, with charges that can vary from year to year, to stated rates which may remain in effect for many years, the Commission requires cost-of-service data with which to evaluate whether the proposed stated rates represent a just and reasonable projection for future years.¹⁰ The Commission's regulations further provide that, when

⁶ See generally Revised Requirements for Filing Changes in Electric Rate Schedules and for the Preparation and Submission of Supporting Data, Order No. 91, FERC Stats. & Regs. ¶ 30,170 (1980).

⁷ See, e.g., *ChevronTexaco Exploration & Production Co. v. FERC*, 387 F.3d 892, 892 (D.C. Cir. 2004).

⁸ Additionally, the composite \$0.40 charge does not reflect a true-up mechanism that is part of the formula rate. This mechanism could result in a rate higher or lower than \$0.40 each month. Due to this factor, comparing the formula rate to stated rates is further hindered.

⁹ See, e.g., PJM Answer at 11.

¹⁰ For example, protesters argue that PJM's current formula rate could include non-recurring or other costs that may not reasonably be included in projected future rates, and they question the volume assumptions used by PJM to project future rates.

necessary to facilitate analysis of a rate change proposal, the applicant can be required to provide additional cost of service data.¹¹

7. While the Commission recognizes PJM's desire to avoid the full expense of a rate proceeding, the Commission cannot accept PJM's alternative proposal of accepting the filing, and allowing PJM and the Finance Committee to further review and negotiate. Without the provision of any cost of service data, the Commission does not have the necessary minimum data for determining whether to accept PJM's contested rate filing. Indeed, the Finance Committee stated in its comments that, based on its initial review, a rate between \$0.33 to \$0.36 would be a better projection,¹² and further stated that additional information was essential to its evaluation. In its answer, PJM itself puts forward a number of factual assertions as to the reasonableness of its projections, assertions that neither the Commission nor the parties can verify without a full rate case filing.¹³ Although PJM asserts that RTOs should be treated differently from other utilities, its filing for stated rates is the equivalent of a standard utility rate case filing.¹⁴ Thus, PJM must conform with the same filing requirements as applied to any other utility making a section 205 filing to change its rate design.

8. PJM argues that the Commission's cost of service regulations were not designed for RTO submissions, and that it should not be required to file under the current regulations because the Commission is in the process of revising the Uniform System of Accounts to better accommodate RTO reporting. While the Commission is examining the reporting requirements for RTOs, the Commission has not made any determinations that the current regulations do not apply to RTOs.¹⁵ Therefore, PJM

¹¹ Cf. 18 C.F.R. § 35.13(a)(3) (2005) (delegating authority to require utility to submit such specified cost of service data as needed for Commission analysis of rate schedule change).

¹² The use of the \$0.33 rate would provide for an over 15 percent rate decrease compared to PJM's \$0.39 proposal.

¹³ PJM Answer, at 15-17 (raising factual arguments about the timing and reasonableness of expenses and volume projections).

¹⁴ For instance, although PJM asserts that as a nonprofit entity different filing rules should apply to it, *see, e.g.*, PJM Answer at 2, a number of commenters argue that PJM has failed to take its not-for-profit status into account and, like any other utility, seeks to retain revenues produced from its stated rates that significantly exceed its costs. *See, e.g.*, PSEG Protest at 8-10; Old Dominion Protest at 9-10 (opposing PJM's proposal to retain earnings).

¹⁵ *See Financial Reporting and Cost Accounting, Oversight and Recovery Practices for Regional Transmission Organizations and Independent System Operators*, 108 FERC ¶ 61,237 (2004).

must follow the existing filing requirements to ensure that sufficient information is available to the parties and the Commission to evaluate the filing.

9. If PJM believes that further discussions can eliminate the need for a full rate case filing here, PJM is free to withdraw this filing and pursue further discussions with the Finance Committee and its members. The Commission reminds the parties that its Settlement Judge and Alternative Dispute Resolution procedures are available to aid in such an effort. If PJM seeks to pursue this filing, it must cure its deficiencies within 60 days of the date of this order, in accordance with 18 C.F.R. § 35.13(a)(1) (2005), without utilizing the abbreviated filing procedures. The amended filing should use the same test year period (calendar year 2004) as in the July 1 filing, and the information should be presented by class of customer.

10. PJM also should address in detail several issues raised but not supported by its July 1 filing. First, PJM asserts that formula rates “do not align well with control mechanisms that help measure performance” while stated rates will “enhance management discipline” and provide “significant benefits to PJM customers” through improved productivity and other management objectives.¹⁶ PJM should explain why formula rates, in contrast to stated rates, do not sufficiently permit performance measurement, and why stated rates are superior to formula rates in improving productivity and other management objectives. Second, PJM states that if its revenues exceed its costs, it would be appropriate for PJM to have modest retained cash.¹⁷ PJM must provide the proposed accounting treatment of its excess revenues and the rationale thereof. Third, in Exhibit PJM-11, PJM provides a one-page table showing projected revenues and expenses for 2006-2010. As this table is insufficiently supported, PJM must provide detailed budget support for this data. Finally, PJM proposes September 1, 2005, as the effective date for its proposed change to stated rates. PJM must explain how a mid-year transition in rate design will be reconciled with the calendar-year budget on which PJM’s formula rates are based.

B. Operating Agreement Revisions

11. PJM proposes to modify its Operating Agreement to increase the members’ representation on the Finance Committee from one to two members from each member sector. PJM further proposes to delineate the advisory nature of the Finance Committee. In addition, PJM proposes to make financial documents available to the Finance Committee for review such as annual and multi-year operating and capital budgets, FERC forms, and other financial information regarding other matters pertaining to the appropriate level of PJM’s rates, proposed major new investments and allocation and disposition of funds. Finally, PJM proposes that its representative to the Finance Committee be the Chair of that committee.

¹⁶ PJM Transmittal Letter at 7.

¹⁷ *Id.* at 8.

12. Pepco Holdings, Inc. (Pepco) objects to two provisions in PJM's proposed changes to the Operating Agreement and requests that these provisions be deleted. The first provision to which Pepco objects would require that the stakeholder representatives on the Finance Committee "represent the interest of their respective sectors." Pepco contends that for the Finance Committee's rate review to be meaningful and a basis for Commission jurisdiction, such review must be carried out in the interests of PJM as a whole, and that persons serving on the Finance Committee must be free to exercise their responsibility to the PJM Board in the public interest. Second, Pepco objects to the provision which mandates that the Chair of the Finance Committee be the Office of Interconnection (PJM) representative. Pepco does not object to the PJM representative being elected the Chair, but only to the practice mandating that the PJM representative be the Chair.

13. In its answer, PJM explained that Pepco's proposed modifications in some respects are identical to specific amendments that were considered by the PJM members and rejected, while others were never presented to the members.¹⁸ PJM requests that the Commission not change the manner of PJM's governance under the Operating Agreement beyond that proposed in the filing.

14. The Commission agrees with Pepco that PJM has not adequately explained why members of the Finance Committee should be obligated to represent the interests of their sectors, rather than to act in the best interests of PJM as a whole. Also, PJM has not supported its proposed amendment to mandate that the PJM representative to the Finance Committee be the Chair of that committee. PJM did not directly address either of these points in its answer.

15. The Commission accepts the proposed changes to the Operating Agreement, effective September 1, 2005, as requested, subject to PJM filing, within 60 days, to explain why members of the Finance Committee must represent the interests of their own sector rather than the interests of PJM, and why the Chair of the Finance Committee must be the PJM representative.

16. In addition to these specific issues with PJM's proposal, several intervenors make recommendations regarding the role of the PJM Finance Committee. With the exception of the issues described above, the Commission does not find that PJM's proposal is unjust and unreasonable. However, the Commission encourages the parties to continue discussions regarding the role of the Finance Committee.

By direction of the Commission.

Magalie R. Salas,
Secretary.

¹⁸ PJM Answer at 22-24.

APPENDIX A

PJM Interconnection, L.L.C.

Tariff Sheets Found to be Deficient

FERC Electric Tariff, Sixth Revised Volume No. 1

First Revised Sheet No. 250
First Revised Sheet No. 251
Second Revised Sheet No. 252
Third Revised Sheet No. 254
Second Revised Sheet No. 255
Second Revised Sheet No. 256
First Revised Sheet No. 256A
Second Revised Sheet No. 257
Fifth Revised Sheet No. 258
Second Revised Sheet No. 258A
Second Revised Sheet No. 259
Second Revised Sheet No. 261
Fourth Revised Sheet No. 262
Sixth Revised Sheet No. 263
Fourth Revised Sheet No. 264
Fourth Revised Sheet No. 265
First Revised Sheet No. 266
Third Revised Sheet No. 267

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APPENDIX B

PJM Interconnection, L.L.C.

Tariff sheets accepted subject to modification, effective September 1, 2005.

Third Revised Rate Schedule FERC No. 24

Second Revised Sheet No. 31

Original Sheet No. 31A

APPENDIX C

Motions to intervene and protest or comment:

American Electric Power Service Corporation on behalf of certain operating companies of the American Electric Power System
Allegheny Power and Allegheny Energy Supply Company
American Municipal Power-Ohio, Inc.
Constellation Generation Group, Inc., Constellation Energy Commodities Group, Inc., Constellation NewEnergy Inc., and Baltimore Gas and Electric Company
Consumers Energy Company
Dayton Power and Light Company
DC Energy, LLC
Dominion Resources, Inc.
Exelon Corporation
Jersey Central Power & Light Company, Metropolitan Edison Company, and Pennsylvania Electric Company (collectively, First Energy);¹⁹
Old Dominion Electric Cooperative
Pepco Holdings, Inc. on behalf of itself and its subsidiaries, Potomac Electric Power Company, Delmarva Power & Light Company, and Atlantic City Electric Company (Pepco)
PPL Electric Utilities Corporation and PPL EnergyPlus, LLC
Public Service Electric and Gas Company and PSEG Energy Resources & Trade LLC
Sector Elected Representatives to the PJM Finance Committee*
Williams Power Company, Inc.*

* Filed out of time.

Motions to intervene:

Allegheny Electric Cooperative, Inc.
The Borough of Chambersburg, Pennsylvania
Cinergy Services, Inc. on behalf of its franchised utility affiliates, the Cincinnati Gas & Electric Company, PSI Energy, Inc., and the Union Light, Heat and Power Company
The City of Hagerstown, Maryland and the Town of Front Royal, Virginia
Edison Mission Energy, Edison Mission Marketing & Trading, Inc., and Midwest Generation EME, LLC
The Maryland Public Service Commission

¹⁹ On July 25, FirstEnergy filed an errata to its motion to intervene and protest.

APPENDIX C (cont'd)

Mirant Americas Energy Marketing, LP, Mirant Chalk Point, LLC, Mirant Mid-Atlantic, LLC, Mirant Peaker, LLC, and Mirant Potomac River, LLC
North Carolina Electric Membership Corporation
The Pennsylvania Office of Consumer Advocate, Maryland Office of People's Counsel, and the Office of People's Counsel for the District of Columbia
The Pennsylvania Public Utility Commission
The PJM Industrial Customer Coalition
Public Utilities Commission of Ohio
Reliant Energy, Inc.
Rockland Electric Company
Southern Maryland Electric Cooperative, Inc.
Strategic Energy, LLC
Wisconsin Electric Power Company