

UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;  
Nora Mead Brownell, and Suedeen G. Kelly.

Allegheny Power	Docket Nos. ER98-1466-004 ER05-1314-002
Allegheny Energy Supply Company, LLC	Docket No. ER00-814-005
Allegheny Energy Supply Gleason Generating Facility, LLC	Docket No. ER01-2067-005
Allegheny Energy Supply Wheatland Generating Facility, LLC	Docket Nos. ER01-2068-005 ER05-1429-001
Allegheny Energy Supply Hunlock Creek, LLC	Docket No. ER01-332-004
Green Valley Hydro, LLC	Docket No. ER00-2924-005
Buchanan Generation, LLC	Docket No. ER02-1638-004

ORDER DENYING REHEARING

(Issued June 2, 2006)

1. In this order, we deny the request for rehearing filed by the West Virginia Energy Users Group and the Industrial Energy Users-Ohio (collectively, the Industrials) of the Commission's October 20, 2005 Order in this proceeding,<sup>1</sup> which accepted the Applicants' updated market power analysis.<sup>2</sup>

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<sup>1</sup> *Allegheny Power*, 113 FERC ¶ 61,052 (2005) (October 20 Order).

<sup>2</sup> Applicants include the following: Allegheny Power, Allegheny Energy Supply Company, LLC, Allegheny Energy Supply Gleason Generating Facility, LLC, Allegheny Energy Supply Wheatland Generating Facility, LLC, Allegheny Energy Supply Hunlock Creek, LLC, Green Valley Hydro, LLC, and Buchanan Generation, LLC.

## **Background**

2. On August 11, 2005, as amended August 31, 2005, Applicants submitted for filing an updated market power analysis pursuant to the requirements of the Commission's orders granting Applicants authority to sell capacity and energy at market-based rates.<sup>3</sup> The Commission accepted the updated market power analysis in its October 20 Order.

## **Rehearing Request**

3. On November 21, 2005, the Industrials filed a request for rehearing of the October 20 Order. The Statement of Issues included in the Industrials' rehearing request identifies the following issues: (1) whether the Commission erred by concluding that the triennial review proceeding is an inappropriate forum in which to address concerns regarding Applicants' market-based rate authority, specifically including its affiliate pricing provisions; (2) whether the Commission erred by presuming, with no rational basis in fact, that electricity markets in the PJM Interconnection LLC (PJM) region are sufficiently competitive to ensure that prices among Applicants' affiliates will invariably remain just and reasonable; and (3) whether the Commission erred by ignoring affirmative evidence of the real-world impact of Applicants' affiliate pricing rules.

4. On rehearing, the Industrials challenge the Commission's determination in the October 20 Order that Applicants' updated market power analysis presents no affiliate abuse concerns. They contend that the Commission improperly characterizes the issues raised by the Industrials as a collateral attack on prior Commission orders that accepted Applicants' affiliate sales provisions. The Industrials further argue that the Commission has effectively redistributed the burden of proof regarding the existence or absence of a competitive market.

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<sup>3</sup> *Allegheny Power Service Corp.*, 82 FERC ¶ 61,245 (1998); *Allegheny Energy Supply Co., LLC*, Docket No. ER00-814-000 (Jan. 20, 2000) (unpublished letter order); *Allegheny Energy Supply Gleason Generating Facility, LLC*, Docket No. ER01-2067-000 (July 13, 2001) (unpublished letter order); *Allegheny Energy Supply Hunlock Creek, LLC*, Docket No. ER01-332-000 (Dec. 11, 2000) (unpublished letter order); *Green Valley Hydro, LLC*, Docket No. ER00-2924-000 (Aug. 17, 2000) (unpublished letter order); *Buchanan Generation, LLC*, Docket No. ER02-1638-000 (May 29, 2002) (unpublished letter order).

**Discussion**

5. As discussed more fully below, we will deny the Industrials' request for rehearing because we again find that Applicants' updated market power analysis satisfies our affiliate abuse concerns. In the October 20 Order, the Commission found that

the issues raised by the Industrials relating to the affiliate sales provisions of the Applicants' tariffs and to the adequacy of the PJM market constitute an impermissible collateral attack on both the prior Commission orders accepting the affiliate sales provisions, as well as the Commission-approved market monitoring and mitigation of PJM. To the extent that the Industrials are challenging the Commission's current approach with regard to sales between affiliates at market-based rates, we believe those arguments are more appropriately raised and addressed in the generic rulemaking proceeding in Docket No. RM04-7-000. In any event, Industrials have failed to persuade us that the affiliate sales provisions in the Applicants' tariffs are no longer sufficient. We further note, however, that the Industrials' arguments rest on the assertion that the Commission-approved pricing system in PJM is flawed, but the Industrials have failed to demonstrate the nature or extent of how the Commission-approved pricing system in PJM is flawed. Accordingly, the Commission finds that, based on Applicants' representations, Applicants satisfy the Commission's concerns with regard to affiliate abuse.<sup>4</sup>

6. As stated above, the Industrials first argue on rehearing that the Commission erred by concluding that the triennial review proceeding is an inappropriate forum in which to address all aspects of Applicants' market-based rate authority. They submit that the Commission improperly characterizes the issues raised by the Industrials as a collateral attack on prior Commission orders that accepted Applicants' affiliate sales provisions. They argue that a triennial review proceeding, which is designed to determine whether market-based rate authority should continue and under what conditions, must consider evidence of market-based rate authority deficiencies that occurred during the prior three-year period in order to promote just and reasonable outcomes.<sup>5</sup> The Industrials maintain that the statutorily mandated pro-customer objectives of the Federal Power Act (FPA)

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<sup>4</sup> October 20 Order, 113 FERC ¶ 61,052 at P 32 (footnotes omitted).

<sup>5</sup> Request for Rehearing at 5 (citing *California ex rel. Lockyer v. FERC*, 383 F.3d 1006, 1012-13 (9th Cir. 2004)).

require that triennial review proceedings comprise more than a refresher of the numbers underlying an invariable conclusion that market power does not exist.<sup>6</sup> The Industrials specifically argue that

due to the limited ability of the Commission's market power screens to analyze the competitiveness of underlying market structures, Triennial Reviews should entail more than the mere satisfaction of evolving generic screens. Utilities should be required to provide adequate analysis to support an empirical Commission finding that competitive markets do, in fact, exist and that market-based rate authority is not being used to unjustly and unreasonably ratchet up energy costs.[<sup>7</sup>]

7. To the extent that the Industrials wish to challenge the Commission's generation market power screens and the market power analysis, we find those challenges should be raised and addressed in the generic rulemaking proceeding in Docket No. RM04-7-000. The Commission reviews all four parts of the analysis (*i.e.*, generation market power, transmission market power, other barriers to entry, and affiliate abuse) to determine whether or not an applicant satisfies, or continues to satisfy, our standards for the grant of market-based rate authority. In the October 20 Order, the Commission found that Applicants satisfy the Commission's generation and transmission market power standards, was satisfied that the Applicants cannot erect barriers to entry, and found that Applicants satisfy the Commission's concerns with regard to affiliate abuse.<sup>8</sup> Therefore, the Commission accepted Allegheny's updated market power analysis.

8. We reiterate that Applicants' affiliate pricing provisions present no concerns with regard to affiliate abuse. Originally, in the orders authorizing Applicants to sell to their affiliates, the Commission found that by tying affiliate sales to the PJM market price, Applicants satisfied the Commission's concerns regarding affiliate abuse. In *Allegheny Energy*,<sup>9</sup> the Commission accepted Allegheny Energy Supply's proposal to cap sales to the APS Operating Companies<sup>10</sup> at a price not to exceed the hourly market price index

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<sup>6</sup> *Id.* at 7 (referring to 16 U.S.C. § 824d(a) (2000)).

<sup>7</sup> Request for Rehearing at 7.

<sup>8</sup> October 20 Order, 113 FERC ¶ 61,052 at P 26, 27, 28, 32.

<sup>9</sup> *Allegheny Energy Supply Co.*, 88 FERC ¶ 61,303 (1999) (*Allegheny Energy*).

<sup>10</sup> In *Allegheny Energy*, the APS Operating Companies included Monongahela Power Company (Monongahela), Potomac Edison Company (Potomac Edison), and West Penn Power Company, whose registered holding company is Allegheny Energy, Inc. Allegheny Energy Supply Company, LLC is a subsidiary of Allegheny Energy, Inc.

posted at the Allegheny Power-PJM interface. Citing Commission precedent governing affiliate sales, the Commission found that tying the price of an affiliate transaction, where a power marketer sells to an affiliated franchised utility, to an established, relevant market price adequately mitigates any affiliate abuse concerns.<sup>11</sup> The Commission found that Allegheny Energy Supply's proposal met that condition. Subsequently, in *Allegheny Power*, the Commission accepted the APS Operating Companies' proposal to sell power to one another at a rate no higher than the PJM hourly price index. The Commission stated that setting the price for transactions among the APS Operating Companies equal to the PJM price index "ensures that they will pay no more and no less than what a non-affiliated entity would pay, and that they will receive no more or less than if they had sold the power in the market place."<sup>12</sup>

9. In the October 20 Order, the Commission found that Applicants' affiliate sales continue to raise no concerns with regard to affiliate abuse because they are conducted consistently with current policy regarding the grant of market-based rate authority and sales between affiliates under a market-based rate tariff,<sup>13</sup> and concluded that Applicants satisfied the Commission's standards for market-based rate authority. Nothing in Industrials' protest or request for rehearing undercuts this finding.<sup>14</sup> Moreover, as the

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<sup>11</sup> *Allegheny Energy*, 88 FERC at 61,935.

<sup>12</sup> *Allegheny Power Services Corp.*, 90 FERC ¶ 61,002, at 61,003 (2000) (*Allegheny Power*).

<sup>13</sup> Commission precedent holds that sales from a marketing affiliate to a regulated utility affiliate may be based on an established, relevant regional market price index, such as the PJM index, to provide reasonable protection against affiliate abuse. *See Armstrong Energy Limited Partnership, LLLP*, 99 FERC ¶ 61,024, at 61,103-04 (2002); *Allegheny Energy Supply Co., LLC*, 96 FERC ¶ 61,002, at 61,005 (2001); *Potomac Power Res., Inc.*, 93 FERC ¶ 61,246, at 61,812 (2000); *FirstEnergy Trading Services, Inc.*, 88 FERC ¶ 61,067, at 61,156 (1999); *see also Brownsville Power I, L.L.C.*, 111 FERC ¶ 61,398, at P 10 (2005) ("Tying the price of an affiliate transaction to an established, relevant market price adequately mitigates any affiliate abuse concerns.")

<sup>14</sup> In their protest, the Industrials argued that they were "gravely concerned about [Applicants'] continued ability to charge up to the PJM LMP for wholesale sales to affiliates." Because the Industrials raised concerns about tying affiliate sales to an established, relevant market without alleging specific problems with that market which would render unjust or unreasonable prices and which developed since Applicants' last triennial review (*see supra* notes 12 & 13 and accompanying text), the Commission found that this was a collateral attack on earlier orders. In their request for rehearing, however, the Industrials refine their argument that tying affiliate sales to the PJM market

(continued)

Commission said in the October 20 Order, a challenge to the Commission's current approach with regard to sales between affiliates is more appropriately raised and addressed in the generic rulemaking proceeding in Docket No. RM04-7-000.

10. As discussed above, in its October 20 Order, the Commission found that the Applicants' updated market analysis satisfies our affiliate abuse concerns; by tying affiliate sales to the PJM market price, the Commission found that Applicants satisfied the Commission's concerns regarding affiliate abuse. As the Commission said in the October 20 Order, a challenge to the Commission's current approach with regard to sales between affiliates is more appropriately raised and addressed in the generic rulemaking proceeding in Docket No. RM04-7-000. Likewise, a general challenge to the Commission's market screens is more appropriately raised and addressed in a generic proceeding. With respect to the Industrials' general challenges regarding affiliate pricing provisions, we deny the Industrials' rehearing request that the Commission erred by concluding that the triennial review proceeding is an inappropriate forum to address the Commission's policy. We address below the Industrials' specific challenges to the Commission's affiliate pricing policy as applied to Applicants.

11. With regard to the Industrials' second and third issues raised in their request for rehearing, the Industrials claim that while they are not challenging the privilege Applicants have been granted to engage in sales among affiliates, they are challenging the pricing structure governing these sales. They contend that the Commission erred by presuming, in the absence of empirical evidence, that markets in the PJM region are sufficiently competitive to ensure that market-based prices (including affiliate prices) are just and reasonable. The Industrials argue that, without sufficient evidence of the competitiveness of the markets in the PJM region, Applicants' affiliate pricing provisions have not been shown to be just and reasonable. The Industrials therefore challenge Applicants' pricing structure governing affiliate sales (*i.e.*, tying affiliate sales to PJM real-time clearing prices), submitting that such sales have been and can be used to drive unnecessary rate increases at the state level and to harm customers. The Industrials contend that the Commission failed to consider evidence of the effects of affiliate pricing provisions as they relate to the PJM pricing system.

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will result in unjust or unreasonable prices because the market lacks competition; they include examples of the real-world impact of Applicants' affiliate pricing. We address their argument below. We note that Industrials refined their argument in their answer to the Applicants' answer to the protest, but the October 20 Order did not consider this refinement because the answers were rejected. 18 C.F.R. § 385.213(a)(2) (2005); *see also* October 20 Order, 113 FERC ¶ 61,052 at P 20.

12. Moreover, with regard to pricing structure, the Industrials note that, as the Commission stated in *Edgar*, “where affiliates are entering agreements for which approval of market-based rates is sought, it is essential that ratepayers be protected and that transactions be above suspicion in order to ensure that the market is not distorted.”<sup>15</sup> The Industrials argue that “[t]he current process has not met the *Edgar* standard because ratepayers are not protected and because tying [Applicants’] affiliate sales to PJM real-time clearing prices enables [Applicants] to sell power to [their] affiliates at prices that far exceed their [all-in] costs of production.”<sup>16</sup> The Industrials submit that they have examples in both Ohio and Maryland demonstrating the adverse effects of Applicants’ affiliate pricing provisions. They contend that Applicants used affiliate pricing privileges to siphon additional revenue from and take advantage of retail customers.<sup>17</sup> The Industrials contest the Commission’s conclusion in the October 20 Order with regard to the grant of market-based rate authority, arguing that electricity markets in the PJM region are not sufficiently competitive and that the Commission ignored affirmative examples of the real-world impact of Applicants affiliate pricing.

13. As we found in the October 20 Order, the Industrials’ general challenge to the competitiveness of the PJM market does not demonstrate that the Commission-approved pricing system in PJM is flawed or that there is a lack of competition in the PJM market.<sup>18</sup> The Industrials’ proffered examples merely describe certain prices derived

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<sup>15</sup> Request for Rehearing at 11 (citing *Boston Edison Co. Re: Edgar Elec. Energy Co.*, 55 FERC ¶ 61,382 (1991) (*Edgar*)).

<sup>16</sup> *Id.*

<sup>17</sup> Specifically, the Industrials state that Monongahela and its affiliate, Allegheny Energy Supply, used affiliate pricing to siphon additional revenue from Monongahela’s retail customers at levels far in excess of the actual cost of running the units that produced the power. Similarly, the Industrials state that in Maryland there is also a “disconnect” between the actual cost of production and the prices that Allegheny and its affiliate, Potomac Edison, are “flowing through” to their Maryland retail customers. Request for Rehearing at 13.

<sup>18</sup> See *Pennsylvania-New Jersey-Maryland Interconnection, LLC*, 81 FERC ¶ 61,257 (1997) (approving PJM’s market monitoring and mitigation); see also PJM, *2005 State of the Market Report*, at 23 (2006) (affirming competitiveness of markets), available at <http://www.pjm.com/markets/market-monitor/som.html>. See generally PJM Open Access Transmission Tariff (PJM Tariff), Attachment M (PJM Market Monitoring Plan); Amended and Restated Operating Agreement of PJM Interconnection, L.L.C., Schedule 1 (PJM Interchange Energy Market).

from the PJM market, which the Industrials believe are too high.<sup>19</sup> As the Commission explained in *AEP Power Marketing, Inc.*, “added protections provided in structured markets with market monitoring and mitigation generally result in a market where prices are transparent and attempts to exercise market power would be sufficiently mitigated.”<sup>20</sup> Furthermore, “markets with Commission-approved market monitoring and mitigation undertake daily and hourly oversight of seller’s pricing behavior to ensure, consistent with clearly established Commission-approved rules, that *prices do not exceed competitive levels.*”<sup>21</sup>

14. The Commission has approved PJM’s markets, finding that the prices that result from the markets will be just and reasonable.<sup>22</sup> We approved PJM’s market mitigation and market monitoring proposals, including the establishment of an independent market monitor (the PJM Market Monitor), to ensure just and reasonable results.<sup>23</sup> In particular, the Commission authorized a series of measures that mitigate price bids submitted by generators, and these bids are used to determine the locational marginal prices.<sup>24</sup> Under the PJM market power mitigation scheme, PJM applies a \$1,000 energy offer cap, system-wide.<sup>25</sup> In addition to the overall \$1000 energy offer cap, PJM can also determine

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<sup>19</sup> See *supra* note 17 and accompanying text.

<sup>20</sup> *AEP Power Marketing, Inc.*, 107 FERC ¶ 61,018, at P 189 (April 14 Order), *order on reh’g*, 108 FERC ¶ 61,026 (2004) (July 8 Order).

<sup>21</sup> April 14 Order, 107 FERC ¶ 61,018 at P 190 (emphasis added).

<sup>22</sup> *PJM Interconnection, LLC*, 86 FERC ¶ 61,247 (1999).

<sup>23</sup> *Id.*

<sup>24</sup> See, e.g., *PJM Interconnection, L.L.C.*, 107 FERC ¶ 61,112 (2004), *order on reh’g and compliance*, 110 FERC ¶ 61,053 (2005) (modifying offer price caps for units offer capped for 80 percent or more of run hours), *order on reh’g*, 112 FERC ¶ 61,031 (2005) (granting rehearing in part and establishing hearing procedures on the test used to examine whether generators possess market power sufficient to trigger mitigation, and the need for scarcity pricing in PJM); *PJM Interconnection, L.L.C.*, 106 FERC ¶ 61,277 (2004), *order on compliance*, 111 FERC ¶ 61,066 (2005) (setting for hearing PJM’s proposals that exempt generating units in the PJM West and PJM South Regions from offer capping), *consolidated in* 112 FERC ¶ 61,031 (2005). The Commission recently accepted a settlement in these proceedings. *PJM Interconnection, L.L.C.*, 114 FERC ¶ 61,076 (2006).

<sup>25</sup> Amended and Restated Operating Agreement of PJM Interconnection, L.L.C., Schedule 1, § 1.10.1A(d)(viii).

hourly whether suppliers should be subject to offer capping when they are dispatched out of economic merit order to maintain system reliability.<sup>26</sup> Mitigation measures, thus, result in PJM's automatic calculation of market-clearing prices using a pre-specified default bid for the actual bid. Among other things, the independent PJM Market Monitor is responsible for monitoring the PJM markets for the potential exercise of market power by a market participant.<sup>27</sup> Furthermore, the Commission has directed the PJM Market Monitor to provide annual reports on the overall competitiveness of its markets,<sup>28</sup> and the independence and objectivity of the market monitor helps ensure that important information about the functioning of the PJM markets is available to the Commission.<sup>29</sup> Therefore, we are satisfied that PJM has mitigation measures, along with market monitoring, in place to address instances where non-competitive prices arise, and to render just and reasonable prices.

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<sup>26</sup> PJM Tariff, Attachment K, App. § 6.4.1(e).

<sup>27</sup> PJM Tariff, Attachment M § III.

<sup>28</sup> The Commission expects to receive the reports and analyses of an RTO's market monitor because:

[t]he Commission has the statutory responsibility to ensure that public utilities selling in competitive bulk power markets do not engage in market power abuse and also to ensure that markets within the Commission's jurisdiction are free of design flaws and market power abuse.

*PJM Interconnection L.L.C.*, 96 FERC ¶ 61,061 (2001) (order provisionally granting RTO status).

<sup>29</sup> *PJM Interconnection*, 86 FERC at 61,891. We note that the PJM Market Monitor's annual reports continually find that the market results in PJM are competitive. *See The New PJM Cos.*, 106 FERC ¶ 63,029, at P 112 (2004) (referring to findings of competition in the PJM market in the 2002 State of the Market Report, as well as the prior three years), *order on reh'g, The New PJM Cos.*, Opinion No. 472, 107 FERC ¶ 61,271, at P 49 (2004) (affirming generally the initial decision and further stating that protesters "had produced little evidence to support their contention that PJM's market monitor is ineffective."); *see also* PJM, *2005 State of the Market Report*, at 23 (the PJM Market Monitor generally concluded that the market results are competitive, even though it mitigates some generators). Additionally, the 2005 report notes that a combination of factors in the PJM energy markets, including high levels of supply, generally moderate demand, generators' obligation to serve load, local market power mitigation, and competitive participant behavior, offset market structural concerns. *Id.*

15. Whether the Applicants' pricing provisions may result in Applicants selling power to their affiliates at prices that exceed their costs of production does not contradict the Commission's policy with regard to protection against affiliate abuse as outlined in *Edgar*, as the Industrials suggest. Nor would the resulting higher prices necessarily make Applicants' pricing provisions unjust and unreasonable.<sup>30</sup> In *Edgar*, the Commission noted several ways for a utility to show it has not unduly favored its affiliates. One type of evidence would be the prices that non-affiliated buyers were willing to pay for similar services.<sup>31</sup> The Commission stated that it would consider benchmark evidence showing the prices, terms, and conditions of sales that non-affiliated sellers have made. This evidence could include purchases made by the buyer, or by other buyers in the relevant market. Thus, the Commission did not require affiliates to transact at cost, but rather "that ratepayers be protected and that transactions be above suspicion in order to ensure that the market is not distorted."<sup>32</sup> By tying its affiliate sales to the PJM market, Applicants satisfy Commission policy and concerns about sales to affiliates, regardless that market prices may exceed costs of production.

16. Finally, the Commission has not effectively redistributed the burden of proof regarding the existence or absence of a competitive market. Rather, we found in the October 20 Order, and reiterate here, that Applicants met their burden to provide current relevant information in their triennial review regarding affiliate abuse concerns and that Applicants otherwise satisfy the Commission's standards for market-based rate authority. At the triennial review stage, the intervenor or the Commission has the burden to show

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<sup>30</sup> See, e.g., *Commonwealth Edison Co.*, 113 FERC ¶ 61,278, at P 32, 44 (2005) ("With respect to whether or not the proposal 'will result in the lowest price for customers,' we note that our standard for reviewing rates is whether those rates are just and reasonable."); *Potomac Elec. Power Co. v. Allegheny Power Sys.*, 85 FERC ¶ 61,160 n.7 (1998) ("[T]he Commission's mandate is not to set the lowest possible rate."); see also *Cities of Bethany v. FERC*, 727 F.2d 1131, 1136 (D.C. Cir.), *cert. denied*, 469 U.S. 917 (1984) (affirming the Commission's finding that the utility only bore the burden to demonstrate that its proposed method of allocating costs was reasonable, not that it was more reasonable than an alternative method).

<sup>31</sup> *Edgar*, 55 FERC at 62,169.

<sup>32</sup> *Id.* at 62,167; accord *Southern Power Co.*, 104 FERC ¶ 61,041, at P 23, 25 (2003).

that the existing rates are not just and reasonable and justify a change in rates.<sup>33</sup> Nothing the Industrials present undercuts the Commission's finding that, consistent with Commission precedent, Applicants' affiliate sales will result in just and reasonable rates because they are tied to the PJM market rates.

17. Accordingly, we deny the Industrials' request for rehearing.

The Commission orders:

The Industrials' request for rehearing is hereby denied, as discussed in the body of this order.

By the Commission.

( S E A L )

Magalie R. Salas,  
Secretary.

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<sup>33</sup> The Commission explained that the triennial market updates by applicants are made pursuant to a condition placed on the Commission's initial authorization of market-based rates under FPA section 205. April 14 Order, 107 FERC ¶ 61,018 at P 200. We have found that these updates are not section 205 filings because while they provide the Commission with updated information upon which the Commission can determine whether the seller should continue to be able to charge market-based rates, they are not filings to change the rates, terms, and conditions of service. July 8 Order, 108 FERC ¶ 61,026, at 61,115 n.23. The Commission clarified that the Commission will institute a section 206 proceeding where the applicant in a three-year market-based rate review proceeding is found to have failed either of the new generation market power screens. April 14 Order, 107 FERC ¶ 61,018 at P 201; and July 8 Order, 108 FERC ¶ 61,026, at 61,115 n.23.