

137 FERC ¶ 61,248
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Philip D. Moeller, John R. Norris,
and Cheryl A. LaFleur.

NorthWestern Corporation

Docket Nos. ER12-316-000

ER10-1138-000

(Consolidated)

ORDER REJECTING IN PART AND ACCEPTING IN PART AND SUSPENDING
REVISED TARIFF RECORDS SUBJECT TO REFUND AND
ESTABLISHING HEARING PROCEDURES

(Issued December 30, 2011)

1. On November 1, 2011, NorthWestern Corporation (NorthWestern) filed revisions to Schedule 3, Regulation and Frequency Response Service (Schedule 3 or regulation service), of NorthWestern's Montana Open Access Transmission Tariff (OATT). NorthWestern seeks an effective date of December 31, 2011. In this order, we reject NorthWestern's proposal to subject customers that elect to self-supply Schedule 3 service to additional charges. We accept the remainder of NorthWestern's revisions, suspend them for a nominal period, to become effective on December 31, 2011, subject to refund, and set them for hearing procedures. Additionally, we consolidate the matters set for hearing in this proceeding with ongoing hearing procedures in Docket No. ER10-1138-000.

I. Background

2. NorthWestern owns and operates an electric transmission system in Montana. As part of its electric operations, NorthWestern operates a balancing authority area within the state of Montana. NorthWestern maintains regulating reserves, within its balancing authority area, sufficient to provide continuously balanced resources with load on a moment-to-moment basis in order to meet operating criteria in accordance with North American Electric Reliability Corporation and Western Electric Coordinating Council reliability requirements.

3. NorthWestern states that because its predecessor, the Montana Power Company, divested most of its generating capacity more than ten years ago, NorthWestern has historically relied on third party purchases of regulation service. In order to eliminate the increasing risks associated with relying on firm third-party contracts for regulation service, NorthWestern states it constructed the Dave Gates Generating Station (DGGS) to provide regulating reserve capacity.¹ The facility consists of three natural gas-fired turbine generator units with a maximum capacity of 150 MW. According to NorthWestern, the DGGS facility began commercial operation in January 2011.

4. On April 29, 2010, in Docket No. ER10-1138-000, NorthWestern filed proposed tariff sheets to revise Schedule 3 of its OATT to recover the costs of service for the DGGS. In that case, NorthWestern proposed to recover the fixed and variable revenue requirement for the DGGS attributed to providing Schedule 3 service through a monthly demand rate and monthly energy rate. On October 15, 2010, the Commission issued an order accepting and suspending NorthWestern's proposed tariff sheets subject to refund and establishing hearing procedures.² A hearing on NorthWestern's Schedule 3 filing in Docket No. ER10-1138-000 is scheduled to begin in January 2012.

II. NorthWestern's Filing

5. NorthWestern states that the basis for its filing is to clarify several aspects of its Schedule 3. NorthWestern states that its filing is intended to: (1) identify the formula by which a customer may determine its specific regulation service obligation in order to facilitate the customer's decision whether to secure regulation service from a source other than NorthWestern; (2) identify who would be subject to the rates that NorthWestern proposes to charge for regulation service to ensure that it is able to fully recover its revenue requirements for the DGGS, and that it is able to maintain system reliability in the event that some of its customers opt to self-supply Schedule 3 service; (3) confirm that self-supplying customers will be subject to technical and operational requirements, the details of which will be spelled out in service or network agreements or NorthWestern's published business practices; (4) confirm that all revenues received for Schedule 3 charges or derived from the operation of DGGS, other than revenues from customers taking regulation service from NorthWestern, will be credited to Schedule 3 customers; and (5) clarify that operating and maintenance (O&M) expenses will be a component of the Schedule 3 monthly demand rate rather than the monthly energy charge.³

¹ NorthWestern, Transmittal Letter at 2-3.

² *NorthWestern Corp.*, 133 FERC ¶ 61,046, at P 23 (2010).

³ NorthWestern, Transmittal Letter at 4.

6. NorthWestern explains that the Commission's *pro forma* Schedule 3 does not specify the terms and conditions under which transmission customers may be permitted to self-supply Schedule 3 services or the formula for customers considering self-supply to determine the amount of regulation service required. NorthWestern contends that it is appropriate to make certain limited revisions to Schedule 3 to clarify self-supply rights. However, at the same time, NorthWestern contends that the details of individual self-supply arrangements should be set forth in service or network agreements to be filed with the Commission as they arise.⁴

7. NorthWestern states that, although it expects that most of its customers will continue to secure regulation service from NorthWestern, several customers have raised the prospect of securing their own service from third party suppliers. For a transmission customer considering self-supply, NorthWestern proposes a formula that the customer can use to determine how much Schedule 3 service it would be required to procure. The formula is based on the transmission customer's projected 12 month coincident peak (12 CP) load compared to NorthWestern's total projected 12 CP load, with the resulting percentage multiplied by NorthWestern's current total regulation requirement of 60 MW. The transmission customer's obligation would be rounded up to the next highest whole number because service must be scheduled in full MW quantities.

8. NorthWestern next explains that if a transmission customer's self-supply arrangements end, fail, or become inadequate, NorthWestern may be obligated to provide Schedule 3 service.⁵ Accordingly, NorthWestern states that it may be required to serve as the backup provider of regulation service for self-supplying customers. NorthWestern also contends that self-supplying customers benefit from the DGGS because it allows the option of turning to NorthWestern for Schedule 3 service and in some cases to "lean" on NorthWestern's system for regulation service.⁶ Therefore, NorthWestern proposes to revise Schedule 3 to make clear that self-supplying customers may be subject to an additional charge under Schedule 3. NorthWestern also proposes to revise the formula for Schedule 3 to reflect that payments received from self-supplying customers, as well as revenues generated by DGGS sales of non-Schedule 3 services or products, will be credited to customers who take service under Schedule 3.

⁴ *Id.* at 4.

⁵ *Id.* at 5 (citing *NorthWestern Corp.*, 129 FERC ¶ 61,116, at P 21 (2009), *reh'g denied*, 131 FERC ¶ 61,202 (2010)).

⁶ *Id.*

9. NorthWestern contends that it is just and reasonable to impose Schedule 3 charges on self-supplying customers because it is consistent with cost causation principles.⁷ NorthWestern further argues that this will ensure that Schedule 3 charges are allocated to all customers that benefit from the DGGs facility, and that NorthWestern is fully compensated for maintaining adequate generation capacity to backstop the regulation needs of self-supplying customers. NorthWestern contends that it is not appropriate to exempt self-supplying customers from Schedule 3 charges because the DGGs provides reliability benefits for all market participants.⁸ NorthWestern does make one exception. NorthWestern does not intend to extend this charge to a self-supply contract with Bonneville Power Administration (Bonneville). NorthWestern states that it does not expect Bonneville to ever call on NorthWestern for regulation during the contract term and, as a result, Bonneville was not factored into the planning for DGGs.

10. In support of its proposal, NorthWestern contends that the Commission has approved the concept of self-supplying transmission customers being obligated to defray some of the expense incurred by the transmission provider's tariff duty to backstop the customer's regulation service needs. NorthWestern cites *Midwest ISO* for the proposition that the Commission has explicitly approved the concept of customers who self-supply regulation service still being obligated to contribute towards the transmission provider's Schedule 3 costs.⁹ NorthWestern also cites Order No. 888-A for the notion that a transmission customer that self-supplies a portion of its regulation service requirement should pay a reduced charge for the service rather than the entire charge.¹⁰

11. NorthWestern explains that it does not intend to spell out in its OATT the exact nature and amount of credits self-supplying customers will receive against their Schedule 3 charge because the appropriate credit will vary with the customer's self-

⁷ *Id.* at 6.

⁸ *Id.*

⁹ *Id.* (citing *Midwest Indep. Sys. Operator, Inc.*, 122 FERC ¶ 61,172, at P 324 (2008) (*Midwest ISO*)).

¹⁰ *Id.* (citing *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, FERC Stats. & Regs. ¶ 31,036 (1996), *order on reh'g*, Order No. 888-A, FERC Stats. & Regs. ¶ 31,048, at 30,325, *order on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *aff'd sub nom. New York v. FERC*, 535 U.S. 1 (2002)).

supply arrangements. NorthWestern indicates that customers with longer self-supply contracts and those who agree to give NorthWestern longer notice that a self-supply arrangement will terminate would receive greater credits against the Schedule 3 charge. NorthWestern contends that consistent with Commission policy, charges and/or credits for Schedule 3 service will be set forth in individual service agreements and/or NorthWestern's business practices.¹¹

12. NorthWestern also proposes to revise Schedule 3 to clarify that self-supplying customers will be subject to technical and operational requirements to be spelled out in individual service agreements and/or NorthWestern's business practices. For example, NorthWestern states that the requirements may include identification of the supplier and resource, demonstration of automatic generation control, proof of metering and telecommunications facilities in place, evidence that the appropriate share of regulation capacity has been procured and demonstration that the necessary firm transmission has been secured from the regulating source to NorthWestern's system. NorthWestern further states that self-supplying customers will need to establish that they have procured their proportionate share of regulation capacity based on the 60 MW of regulation service that NorthWestern requires (as that amount may be adjusted from time to time).¹²

13. In addition, NorthWestern proposes to clarify that charges imposed on customers that self-supply regulation service will be credited to Schedule 3 customers when the charges are paid. NorthWestern also states that any incidental revenues derived from operation of the DGGs will be credited to the same Schedule 3 customers. NorthWestern maintains that the DGGs was constructed for the specific purpose of providing regulation service; therefore, it does not expect to realize any non-Schedule 3 revenues in the near future. However, NorthWestern asserts that if that changes in the future, then any non-Schedule 3 revenues should be credited to Schedule 3 customers, who are bearing the cost of constructing the facility.

14. Finally, NorthWestern proposes to revise its formula for the Schedule 3 rates by incorporating O&M expenses as components of the monthly demand rate, rather than the monthly energy rate.

¹¹ *Id.* at 7 (citing *Entergy Servs., Inc.*, 109 FERC ¶ 61,095, at P 68-72 (2004); *WPS Res. Operating Cos.*, 91 FERC ¶ 61,326, at 62,132 (2000); *Illinois Power Co.*, 87 FERC ¶ 61,172, at 61,683 (1999); and other cases).

¹² *Id.*

III. Notice of Filing and Responsive Pleadings

15. Notice of NorthWestern's filing was published in the *Federal Register*, 76 Fed. Reg. 69,716 (2011), with interventions and protests due on or before November 22, 2011. Timely motions to intervene and/or comments and protests were filed by the following: Powerex Corporation, NaturEner USA, LLC, Central Montana Electric Power Cooperative (Central Montana), and Bonneville. Untimely motions to intervene and/or protests were filed by Basin Electric Power Cooperative (Basin), Montana Large Customer Group (LCG), and PPL EnergyPlus, LLC and PPL Montana, LLC (collectively, the PPL Companies). On December 7, 2011, in response to the protests, NorthWestern filed a motion for leave to answer and answer (Answer).

IV. Discussion

A. Procedural Matters

16. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2011), the timely unopposed motions to intervene serve to make the entities filing them parties to the proceeding. Pursuant to Rule 214(d) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214(d) (2011), the Commission will grant Basin, the PPL Companies, and LCG's late-filed motions to intervene and/or protest given their interests in the proceeding, the early stage of the proceeding, and the absence of undue prejudice or delay.

17. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2011), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We are not persuaded to accept NorthWestern's Answer and will therefore reject it.

B. Comments and Protests

18. Both Central Montana and LCG (Protestors) contend that NorthWestern's filing is fundamentally inconsistent with customers' rights to self-supply Schedule 3 service, unsupported by Commission precedent and unduly vague. The Protestors argue that both Order No. 888 and the *pro forma* OATT make it clear that customers have the option to self-supply Schedule 3 service. They contend that the proposed revisions by NorthWestern essentially erase that right by charging self-supply customers for Schedule 3 service. Central Montana argues that this is true even if customers fully self-supply on a long-term basis.¹³

¹³ Central Montana, Protest at 6.

19. Central Montana asserts that the tariff language in NorthWestern's proposal fails to detail the rate that will be charged by NorthWestern in the event a customer elects to self-supply Schedule 3 service. Central Montana argues that NorthWestern's failure to spell out the nature and amount of credit a self-supplying customer will receive results in tariff revisions that are so vague as to constitute a substantive nullity. Central Montana maintains that the provisions in the tariff should be sufficient to allow a customer to calculate the charges it would face if it elects to self-supply.¹⁴ Both Protestors argue that without clear and specific tariff language, the Commission and/or the public would not know the actual rates, terms, and conditions and whether they are just and reasonable.

20. Central Montana argues that NorthWestern has not demonstrated in its proposed formula that it is just and reasonable to use projections of a customer's 12 CP load and NorthWestern's total 12 CP load to determine a customer's proportion of total Schedule 3 costs. Moreover, Central Montana adds that NorthWestern's total regulation requirement has been contested in the ongoing proceeding in Docket No. ER10-1138-000. Protestors both argue that because the instant proceeding clearly overlaps with NorthWestern's ongoing Schedule 3 proceeding, the Commission should consolidate this proceeding with Docket No. ER10-1138-000.¹⁵

21. LCG argues that NorthWestern's proposal to charge customers that elect to self-supply Schedule 3 services for the cost of DGGS is unreasonable, unsupported by Commission precedent, and discriminatory.¹⁶ LCG claims that because most of the costs associated with providing regulation service are fixed, it would be difficult if not impossible for a customer to make an economic decision to self-supply the service.

22. LCG argues that NorthWestern's proposal does not specify the amount of costs a customer is obligated to pay or a methodology to calculate such costs. In addition, LCG contends that the proposed revised tariff contains language that is neither clear nor specific. LCG asserts that the Commission requires terms that are incorporated in rate schedules and tariffs be clearly spelled out and provide adequate notice of the meaning and effect of such terms.¹⁷ Both Protestors assert that NorthWestern's proposal is patently deficient because it is inconsistent with customers' rights to self-supply regulation service and contains unacceptably vague tariff provisions; and therefore should be rejected.

¹⁴ *Id.* at 7.

¹⁵ *Id.* at 9.

¹⁶ LCG, Protest at 4.

¹⁷ *Id.* at 6.

23. Although NorthWestern cites *Midwest ISO*¹⁸ in an effort to support its position of imposing Schedule 3 charges on certain customers that elect to self-supply regulation service, LCG argues that the case cited is not applicable to the instant filing. LCG contends that NorthWestern is a vertically integrated transmission provider that is providing service from facilities it owns, unlike Midwest ISO, which is independently operating a market for regulation service. Thus, LCG asserts that there are no regulation market costs for NorthWestern to recover.¹⁹

24. LCG also contends that there is no Commission precedent that requires self-supply regulation service customers to defray the cost of generation facilities transmission providers use to provide Schedule 3 service. LCG claims that such provisions amount to a vehicle to recover stranded costs associated with customers that elect to self-supply Schedule 3 service. LCG maintains that OATT customers under Order Nos. 888 and 890 are only required to purchase Schedule 3 service from NorthWestern to the extent that they do not make comparable arrangements. LCG further adds that if a self-supply customer fails to meet its regulation capacity obligation and NorthWestern acts as a backstop, there are Commission authorized penalties in place for unauthorized use of ancillary services, provided the penalty rate is included in Schedule 3 of the transmission provider's OATT.²⁰

25. LCG asserts that NorthWestern's proposal is unduly discriminatory and contrary to law because it exempts Bonneville from the charges imposed on self-supply customers in the instant proceeding. LCG contends that there is no justification for imposing dramatically different terms and charges on other customers that, like Bonneville, elect to self-supply regulation service.²¹

26. Bonneville comments that in 2008, prior to the construction of the DGGS, it entered into a Regulation and Frequency Response Self-Supply Agreement (Agreement) with NorthWestern to serve certain Bonneville customers in NorthWestern's balancing authority area. Thus, Bonneville explains (and states that NorthWestern agrees) that its regulation service needs for servicing its customers in NorthWestern's balancing authority were purposely excluded from the planning and development of DGGS.

¹⁸ *Midwest ISO*, 122 FERC ¶ 61,172 at P 324.

¹⁹ LCG, Protest at 8.

²⁰ *Id.*

²¹ *Id.* at 9-10.

27. Bonneville asserts that there are certain issues in the Agreement that need to be amended to reflect the parties' understanding in light of NorthWestern's proposed filing. First the Agreement needs to be amended to reflect that NorthWestern's proposed Schedule 3 costs will not be applied to Bonneville. In addition, the unilateral termination provision in the Agreement will be modified such that a party must provide a minimum five-year notice to terminate the Agreement. Bonneville asserts that with this understanding it does not object to NorthWestern's proposed revisions to Schedule 3.

C. Commission Determination

28. We find that NorthWestern's proposal to subject customers that elect to self-supply their own regulation reserves to additional charges under Schedule 3 is not consistent with Commission policy, and we therefore reject that proposal here. With respect to the remainder of NorthWestern's proposed tariff revisions, our preliminary analysis indicates that NorthWestern has not shown them to be just and reasonable, and they may be unjust, unreasonable, unduly discriminatory or preferential, or otherwise unlawful. NorthWestern's filing raises issues that cannot be determined based on the record before us, and are more appropriately addressed in the hearing procedures ordered below. Therefore, we accept the remainder of NorthWestern's proposed tariff revisions, suspend them for a nominal period, to be effective December 31, 2011, subject to refund and hearing procedures. Finally, in light of the common factual issues presented in this proceeding and the proceeding in Docket No. ER10-1138-000, which is currently set for hearing, we consolidate those two proceedings.

29. Since Order No. 888, the Commission has required transmission providers to allow customers to satisfy their Schedule 3 obligations through self-supply arrangements.²² The Commission explained that the pricing of ancillary services should include the amount of each ancillary service that the transmission customer must purchase, self-supply, or otherwise procure and must be readily determinable from the transmission provider's tariff and comparable to obligations to which the transmission provider itself is subject.²³ Accordingly, the *pro forma* Schedule 3 states that the transmission customers must either purchase this service from the transmission provider or "make alternative comparable arrangements" to satisfy its regulation service obligation.

30. NorthWestern argues that it is reasonable to subject self-supply customers to additional charges because the regulation service provided by the DGGs acts as a backstop should a self-supply customer's outside arrangements fail, become inadequate,

²² Order No. 888, FERC Stats. & Regs. ¶ 31,036 at 31,717.

²³ *Id.* at 31,721.

or end. NorthWestern also argues that the presence of the DGGS provides reliability benefits to all customers (even those who self-supply). Accordingly, NorthWestern seeks the authority to impose what is effectively a standby Schedule 3 charge on customers that self-supply regulation reserves. However, we find that NorthWestern's vague assertions of reliability benefits from the DGGS do not justify its novel proposal to impose a standby regulation service charge to self-supplying customers.

31. NorthWestern argues that its proposal is consistent with Commission precedent. NorthWestern cites Order No. 888-A for the proposition that a transmission customer that self-supplies a portion of its regulation service requirement should pay a *reduced* charge for the service rather than the *entire* charge.²⁴ This does not support NorthWestern's contention because, in Order No. 888-A, the Commission was addressing the situation where a customer chooses to self-supply a portion of its regulation reserves, while still relying on the transmission provider to provide additional regulation service. NorthWestern, however, seeks to levy Schedule 3 charges on customers who self-supply their entire regulation reserve requirement.

32. NorthWestern also cites *Midwest ISO* for the proposition that the Commission has approved the concept of charging customers who self-supply regulation reserves for the transmission provider's Schedule 3 costs.²⁵ However, NorthWestern's proposed Schedule 3 charge is fundamentally different from the facts of *Midwest ISO*, rendering NorthWestern's use of selected language from that case unpersuasive in this context. The issue in *Midwest ISO* was whether the self-scheduling option in Midwest ISO's proposed Ancillary Services Market (ASM) was consistent with or superior to the *pro forma* OATT's self-supply requirement. Because an entity that previously self-supplied its ancillary service requirements would have to self-schedule in Midwest ISO's ASM, there was a concern that a customer might be subject to some additional charge reflecting the difference between Midwest ISO's ancillary service charge and the payment that customers would receive for its self-scheduled resources.²⁶ The Commission accepted Midwest ISO's proposal, noting that the self-scheduling option would allow market participants to enter bilateral contracts for reserves and that it met the features of the *pro forma* OATT's requirement that customers be allowed to self-supply ancillary services.²⁷ Because *Midwest ISO* involved the self-scheduling of resources in ancillary services

²⁴ NorthWestern, Transmittal Letter at 6, n.12 (citing Order No. 888-A, FERC Stats. & Regs. ¶ 31,048 at 30,235).

²⁵ *Midwest ISO*, 122 FERC ¶ 61,172 at P 324.

²⁶ *Id.* P 318.

²⁷ *Id.* P 324.

market run by an independent system operator, it does not support NorthWestern's proposal to levy a standby Schedule 3 charge to any and all customers who would supply the resources themselves.

33. Accordingly, we reject NorthWestern's proposal to subject customers who elect to self-supply Schedule 3 service to additional charges as inconsistent with the requirements of Order No. 888. We will accept the remainder of NorthWestern's revisions, suspend them for a nominal period, to become effective on December 31, 2011, subject to refund, and set them for hearing procedures. The hearing will address, among other things, the manner in which NorthWestern proposes to set the regulation requirements for self-supplying customers, the movement of O&M costs from the monthly energy rate to the monthly demand rate, and the manner in which NorthWestern proposes to credit certain revenues to Schedule 3 customers.

34. In addition, because the issues in this proceeding are closely intertwined with those raised in Docket No. ER10-1138-000, we will consolidate the instant filing with the ongoing proceeding in that docket for purposes of hearing and decision. Consolidation is appropriate where there are common questions of law or fact and consolidation will result in greater administrative efficiency.²⁸ Both proceedings involve NorthWestern's proposal to base its Schedule 3 charge on the cost of service of the DGGs. NorthWestern's proposal in Docket No. ER10-1138-000 sets forth the overarching structure of Schedule 3 (i.e., establishing a revenue requirement and the demand rate and energy rate components of the charge).²⁹ While the instant filing deals primarily with how customers who self-supply regulation service will be treated under NorthWestern's Schedule 3, it also includes a change as to how O&M costs are treated and how certain revenues are credited to Schedule 3 customers. Moreover, NorthWestern's proposal to establish the amount of service a self-supplying customer must provide, as well as its proposed revenue crediting mechanism, are based on the structure of the Schedule 3 it proposed in the earlier filing. Therefore, there are common issues of fact present in both filings that supports consolidation. Accordingly, the Commission will consolidate the two proceedings here.

The Commission orders:

(A) NorthWestern's proposal to subject self-supply customers to additional charges under Schedule 3 is hereby rejected, as discussed in the body of this order.

²⁸ *ISO New England, Inc.*, 124 FERC ¶ 61,013, at P 36 (2008).

²⁹ *NorthWestern Corp.*, 133 FERC ¶ 61,046 at P 23.

(B) The remainder of NorthWestern's revisions to Schedule 3 are hereby accepted for filing and suspended for a nominal period, to become effective December 31, 2011, subject to refund and hearing, as discussed in the body of this order.

(C) NorthWestern's filing is hereby consolidated with the ongoing proceeding in Docket No. ER10-1138-000 for the purpose of hearing and decision, as discussed in the body of this order.

(D) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Commission by section 402(a) of the Department of Energy Organization Act and by the FPA, particularly sections 205 and 206 thereof, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the FPA (18 C.F.R. Chapter I), a public hearing shall be held concerning the justness and reasonableness of the proposed revisions.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.