

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Devon Power LLC

Docket Nos. ER03-563-030
ER03-563-055

ORDER ACCEPTING PROPOSED SETTLEMENT AGREEMENT

(Issued June 16, 2006)

1. In these proceedings, the Commission has been addressing a proposal by ISO New England, Inc. (ISO-NE) to establish a locational installed capacity (LICAP) mechanism. That proposal was made in response to Commission orders identifying flaws in New England's current capacity market, and was further developed through subsequent hearing procedures. As this proceeding has developed, additional evidence has been produced regarding the flaws in the current capacity market and the resulting impacts those flaws have had on New England's electric system infrastructure. As discussed in more detail below, the Commission established additional procedures to consider how the LICAP mechanism would address the deficiencies in the current capacity market and meet New England's projected need for new infrastructure in coming years. Those additional procedures also gave the parties an opportunity to discuss and develop potential alternatives to the LICAP mechanism.

2. On March 6, 2006, a broad group of the parties to this proceeding (collectively Settling Parties¹) filed a proposed settlement (Settlement Agreement) that would resolve all issues in this matter. As described in more detail in this order, the Settlement Agreement contains an alternative to LICAP, called the Forward Capacity Market (FCM). The settlement is contested. In this order, we accept the proposed Settlement Agreement, finding that as a package, it presents a just and reasonable outcome for this proceeding consistent with the public interest.

¹ Settling Parties are identified in Appendix A to this order.

I. Background and Procedural History

3. The Initial Decision contains a detailed history of this proceeding up to the point of its issuance.² Rather than repeat that detailed history here, we will briefly recount certain key points of prior proceedings and the present case.

4. As a means of ensuring reliability, for many years ISO-NE (and previously NEPOOL) has imposed an installed capacity (ICAP) requirement on load-serving entities, requiring them to procure specified amounts of ICAP based on their peak loads plus a reserve margin. Prior to the widespread unbundling of the generation, transmission and distribution functions of most New England load-serving entities (which in many cases included state-mandated divestiture of generating assets), if a utility did not have sufficient resources to meet its ICAP requirement, it could either obtain ICAP from an entity in the pool with a surplus or pay the deficiency charge.

5. Beginning in 1998, ISO-NE began operating a bid-based market for ICAP.³ In 2000, as part of the region's development of wholesale power markets and market-based rates, the Commission first began to identify flaws in the ICAP market. In an order addressing competing proposals to implement a congestion management system and multi-settlement system in New England, the Commission rejected a proposal by ISO-NE to eliminate the ICAP requirement, reasoning that ISO-NE should first propose an alternative mechanism to meet the reliability function served by the ICAP requirement.⁴ The Commission did allow ISO-NE to replace the ICAP auction mechanism with an administratively-determined ICAP deficiency charge, agreeing with ISO-NE that the auction "can produce inflated prices unrelated to the actual harm caused by ICAP deficiencies."⁵

6. In 2002, the Commission further addressed deficiencies in New England's ICAP market, this time noting the lack of a locational element. In its order addressing the implementation of energy markets and locational marginal pricing in New England, the

² See *Devon Power LLC*, 111 FERC ¶ 63,063 at P 2-36 (2005) (Initial Decision).

³ See *New England Power Pool*, 83 FERC ¶ 61,045 at 61,263 (1998).

⁴ See *ISO New England, Inc.*, 91 FERC ¶ 61,311 (2000).

⁵ *Id.* at 62,081.

Commission identified the lack of a locational element as a significant flaw in the ICAP market, stating that it “believes that location is an important aspect of ensuring optimal investment in resources.”⁶

7. These specific proceedings began in response to the February 26, 2003 filing by Devon Power LLC, Middletown Power LLC, Montville Power LLC, Norwalk Power LLC and NRG Power Marketing Inc. (collectively NRG) of four cost-of-service reliability-must-run (RMR) agreements covering 1,728 megawatts of generating capacity located within Connecticut and the constrained Southwest Connecticut area. In a series of orders addressing NRG’s filing⁷ as well as RMR agreements filed by other entities,⁸ the Commission rejected the majority of the RMR agreements, out of concern about the effect widespread use of such contracts could have on the competitive market. The Commission stated that ISO-NE, “rather than focusing on and using stand-alone RMR agreements, should incorporate the effect of those agreements into a market-type mechanism.”⁹ Accordingly, the Commission directed, pursuant to section 206 of the Federal Power Act (FPA),¹⁰ that revised bidding rules (called Peaking Unit Safe Harbor, or PUSH, bidding) be instituted on an interim basis to give low-capacity factor generating units operating in designated congestion areas the opportunity to recover their costs through the market.¹¹ To replace the interim PUSH mechanism, the Commission directed ISO-NE to file by March 1, 2004, for implementation by June 1, 2004, “a mechanism that implements location or deliverability requirements in the ICAP or resource adequacy market . . . so that capacity within [designated congestion areas] may be appropriately compensated for reliability.”¹²

⁶ *New England Power Pool and ISO New England, Inc.*, 100 FERC ¶ 61,287 at 62,278 (2002).

⁷ *Devon Power LLC*, 102 FERC ¶ 61,314 (2003) (March 25 Order); *Devon Power LLC*, 103 FERC ¶ 61,082 (2003) (April 25 Order); *Devon Power Company*, 104 FERC ¶ 61,123 (July 24 Order).

⁸ *PPL Wallingford Energy LLC*, 103 FERC ¶ 61,185 (2003); *PPL Wallingford Energy LLC*, 105 FERC ¶ 61,324 (2003).

⁹ See April 25 Order at P 29.

¹⁰ 16 U.S.C. 824e (2000).

¹¹ See April 25 Order at P 33; July 24 Order at P 25-31.

¹² April 25 Order at P 37.

8. On March 1, 2004, ISO-NE made its filing in compliance with the April 25 Order. In the compliance filing, ISO-NE proposed a locational installed capacity (LICAP) mechanism that would add a locational element to the current ICAP market, establishing four ICAP regions with separate ICAP requirements: Maine, Connecticut, Northeast Massachusetts/Boston (NEMA/Boston), and the remainder of New England (Rest of Pool). Under the proposal, capacity transfer limits would be established to limit the amount of ICAP that load serving entities in one region could purchase from another region. Additionally, ISO-NE proposed to use a downward sloping demand curve to establish the amount of ICAP which must be procured and the price for that capacity. Additionally, under the proposed LICAP mechanism, capacity transfer rights would be allocated to load or generators, depending on their location, to allow market participants to hedge against congestion costs. Under the proposal, holders of capacity transfer rights between two ICAP regions would receive the difference in ICAP prices between those regions.

9. In a June 2, 2004 Order,¹³ the Commission established hearing procedures regarding ISO-NE's compliance filing, and delayed the implementation of the LICAP mechanism from the proposed June 1, 2004 date until January 1, 2006. The Commission stated that it agreed with two broad concepts in ISO-NE's proposal. First, the Commission found it appropriate to establish separate ICAP regions, but questioned whether the regions proposed by ISO-NE adequately reflected where infrastructure investment is needed most, specifically noting the constrained area of Southwest Connecticut. Second, the Commission agreed with the overarching concept of a demand curve, but found that more information was necessary to develop appropriate parameters for the curve. As a result of these findings, the Commission directed ISO-NE to submit a further filing addressing whether the Commission should revise the LICAP proposal to create a separate ICAP region for Southwest Connecticut. Additionally, the Commission established a separate investigation and paper hearing in Docket No. EL04-102-000 to determine whether a separate energy load zone should be created for Southwest Connecticut, and whether it should be implemented in advance of LICAP. Finally, the Commission established hearing procedures to determine the appropriate demand curve parameters, the proper method for calculating capacity transfer limits, the appropriate method for determining the amount of capacity transfer rights to be allocated, and the proper allocation of capacity transfer rights. In subsequent orders, the Commission

¹³ *Devon Power LLC*, 107 FERC ¶ 61,240 (2004) (June 2 Order).

addressed ISO-NE's filing regarding the creation of a separate ICAP region for Southwest Connecticut, and denied rehearing and granted clarification in part of the June 2 Order.¹⁴

10. On June 15, 2005, the Presiding Judge issued an Initial Decision on the issues set for hearing in the June 2 Order.¹⁵ The Initial Decision largely (with some variation) adopted the demand curve proposed by ISO-NE in its August 31, 2004 initial testimony, and also ruled on the appropriate allocation of capacity transfer rights and the appropriate methodology for calculating capacity transfer limits. Briefs on Exceptions to the Initial Decision were filed on July 15, 2005, and Briefs Opposing Exceptions were filed on August 4, 2005.

11. In section 1236 of the Energy Policy Act of 2005, signed into law on August 8, 2005, Congress noted the New England Governors' concerns that the LICAP proposal would not provide adequate capacity or reliability while imposing high costs on consumers.¹⁶ Congress declared that the Commission should carefully consider the states' objections.

12. Several entities (mostly state entities and load representatives) requested oral argument before the Commission on the exceptions to the Initial Decision, pursuant to Rule 711(c) of the Commission's Rules of Practice and Procedure.¹⁷ In an August 10, 2005 Order, the Commission granted these requests and scheduled oral argument for September 20, 2005.¹⁸ Additionally, the Commission stated that, in light of its decision to hear oral arguments, "we have determined that the implementation of the LICAP mechanism, if it proceeds, will not be earlier than October 1, 2006."¹⁹

13. The oral argument focused on whether the LICAP mechanism, as adopted in the Initial Decision, or any alternative approach would provide for just and reasonable

¹⁴ See June 2 Order, *order on reh'g and clarification, Devon Power LLC*, 109 FERC ¶ 61,154 (2004), *reh'g denied*, 110 FERC ¶ 61,315 (2005); see also *Devon Power LLC*, 109 FERC ¶ 61,156 (order on compliance filing directing establishment of Southwest Connecticut region), *order on reh'g and clarification*, 110 FERC ¶ 61,313.

¹⁵ See *supra* note 2.

¹⁶ Pub. L. No. 109-58, § 1236, 119 Stat. 961 (2005).

¹⁷ 18 C.F.R. § 385.711(c) (2005).

¹⁸ *Devon Power LLC*, 113 FERC ¶ 61,075 (2005).

¹⁹ *Id.* at P 5.

wholesale power prices in New England, at levels that encourage needed generation additions and whether LICAP or any alternative approach would provide adequate assurance that necessary electric generation capacity or reliability will be provided. The Commission also asked the parties to address at oral argument what are the costs, benefits, and economic impacts of the proposal (or any alternative approach), compared to continued reliance on the status quo, such as the cost of RMR agreements. Both at the oral argument and in briefs filed prior to the oral argument, parties to the proceeding were given the opportunity to present alternatives to LICAP directly to the Commission.²⁰ Parties presented two alternatives to LICAP in their briefs and at oral argument: the New England Resource Adequacy Market and the New England Locational Resource Adequacy Market.

14. Following the oral argument, the Commission issued an order giving the parties an additional opportunity to pursue a settlement on an alternative to the LICAP mechanism.²¹ In that order, the Commission stated that it remained concerned about the resource adequacy situation in New England (particularly in the congested areas of Southwest Connecticut and Northeastern Massachusetts), noting that “[t]he parties at the oral argument generally agreed that the status quo is failing and that generation resources are not being added at a rate necessary to maintain reliability and assure just and reasonable wholesale power prices.”²² The Commission directed the Chief Administrative Law Judge to appoint a settlement judge to guide the process of developing a proposed alternative to LICAP. Additionally, the Commission stated that it would continue to evaluate the Initial Decision, and directed ISO-NE to make a compliance filing to aid in its consideration of the Initial Decision.²³

II. Description of Proposed Settlement Agreement

A. Forward Capacity Market

15. The Settlement Agreement provides for the implementation of an FCM as an alternative to the ISO-NE-designed LICAP mechanism. The Settlement Agreement is the end product of a series of over 30 formal settlement conferences that occurred over a four-month period with the active participation and involvement of Administrative Law

²⁰ See Notice Scheduling Oral Argument, Docket No. ER03-563-030 (August 25, 2005).

²¹ *Devon Power LLC*, 113 FERC ¶ 61,075 (2005) (October 21 Order).

²² *Id.* at P 5.

²³ *Id.* at P 10-14.

Judge Lawrence Brenner. Of 115 parties to the settlement proceedings, eight parties have formally opposed the Settlement Agreement. The NEPOOL Participants Committee voted, with 78.46 percent, to support the Settlement Agreement, with support from all six voting sectors.

16. The FCM establishes annual auctions for capacity. The capacity product will be sold on a per-megawatt of deliverable capacity basis. Capacity resources, regardless of type, will receive the same auction clearing price. The Forward Capacity Auctions (FCA) will procure capacity three-plus years ahead of the commitment period, which is intended to provide for a planning period for new entry and allow potential new capacity to compete in the auctions. The commitment period is a year-long period that corresponds to the ISO-NE power year.²⁴ Thus, sellers will commit to provide capacity for one year—for example, June 1, 2011 to May 31, 2012—three-plus years in advance of the commitment period. However, the Settlement Agreement grants new capacity the option to lock-in capacity prices for up to five years. New capacity may, during the process to qualify as an eligible resource, select a commitment period of up to five years, in one-year increments, provided that the resource meets certain auction criteria. This design element is intended to provide predictable revenues and facilitate financing for new capacity.

17. The FCAs are designed as descending clock auctions. In such an auction, the administrator announces a starting price. Bidding in the FCA will begin at a specified price—two times the agreed Cost of New Entry (CONE).²⁵

18. Following the first auction, subsequent CONEs will be mathematically established, based on preceding CONEs and the clearing price of the preceding auction. The proposed FCM provides annual reconfiguration auctions to be held two and a half years prior to each commitment period, as well as twice-yearly seasonal auctions and monthly auctions just prior to, and during each commitment period. These reconfiguration auctions provide for the buying, selling and exchange of capacity obligations and maintenance of liquidity. There are three types of reconfiguration auctions: (i) three annual auctions (for trading year-long commitments) before the relevant commitment period, (ii) monthly auctions held prior to each commitment month,

²⁴ The ISO-NE power year is a period of twelve months beginning June 1 of each year and ending on May 31 of the next calendar year.

²⁵ CONE, which represents the initial price of each auction, is set for the initial auction at \$7.50/kW-month, which was negotiated as part of the settlement.

and (iii) seasonal auctions held prior to June and October of each year to accommodate transactions to sell a seasonal strip product. The reconfiguration auctions will preserve the locational element of the initial auction.²⁶

19. Until there have been three successful auctions, the price for existing capacity will be set within a ceiling of 1.4 times CONE and a floor of 0.6 times CONE, which is referred to as the “collar mechanism.” In the auctions to which the collar mechanism applies, if the auction clearing price is greater than 1.4 times CONE, existing capacity will be paid 1.4 times CONE and new capacity will be paid the auction clearing price. The auction clearing price will not fall below 0.6 times CONE. In the first year, this means that auction prices for existing capacity can range from \$4.50 to \$10.50/kW-month.

20. The amount of capacity procured will be that amount required to maintain the installed capacity requirement. Thus, if the system has surplus capacity, not all capacity resources offered will be purchased.²⁷ Each load-serving entity, as the ultimate purchaser of capacity, is required to pay for a share of the installed capacity requirement proportionate to its share of peak load. FCM allows load-serving entities to self-supply: load-serving entities may use owned and contracted resources (in whole or in part) to supply their capacity obligations. Thus a load-serving entity can meet its capacity obligations without paying the auction clearing price. Resources designated as self-supply are subject to the same performance obligations and qualification requirements as other resources participating in the FCM and the FCAs.

21. Resources participating in the auctions will be designated as existing or new resources. Existing capacity will be defined as a resource previously listed as a resource in New England’s capacity market; new capacity will never have been listed as a capacity resource. Existing capacity may also qualify as new capacity if it undertakes specified types of major investments to upgrade its facilities. The incremental amount of an increase in output from an existing capacity resource will be considered new capacity, provided the output increase is greater than or equal to two percent of the Resource’s Summer Seasonal Claimed Capability. The Settlement Agreement indicates that additional thresholds for new capacity may be addressed in the stakeholder process, which will enable consultation from state utility regulatory agencies. The Settlement Agreement sets rules under which imported capacity is included in the FCAs.

²⁶ The locational element of the FCM is described below.

²⁷ This component of the FCM differs from the LICAP proposal, which set a target level of capacity in excess of the installed capacity requirement.

22. Capacity resources, existing and new, are required to submit qualification documentation to be eligible to participate in the auctions. New capacity that is selected to provide capacity in the future must demonstrate control over the proposed project site, a critical path schedule with milestones supporting the feasibility of the project, and an interconnection analysis showing the impact of connecting to the transmission grid. The FCM proposal also enables bidding by demand-side and intermittent resources.

23. The FCM proposal contains a locational component. Before each auction, ISO-NE will determine capacity zones based on an identification of transmission limits that may bind. In instances where transmission limits are expected to bind (accounting for predicted upgrades that will be on-line by the commitment period), ISO-NE will designate separate capacity zones and hold separate but simultaneous auctions.

24. Capacity suppliers will have their monthly capacity payments reduced to account for two phenomena. First a “peak energy rent” sum will be deducted from monthly capacity payments. The peak energy rent sum, originally developed in the LICAP proposal, is based on revenues that would be earned in the energy market by a hypothetical, proxy peaking unit. There are a number of agreed characteristics that apply to the hypothetical unit, including indexing to the marginal fuel. The peak energy rent deduction is designed as a hedge for load against price spikes in the energy market.

25. Suppliers will also have payments reduced to account for availability during designated periods of system stress (*i.e.*, Shortage Events). This provision is intended to create an economic incentive for capacity resources to be available when capacity is most valuable to load. Penalties will be assessed to suppliers for failing to be available during a Shortage Event and will be assessed on a resource-specific basis. On any critical day, a resource can have compensation reduced by up to 10 percent of annual auction payments if it is not available; in any month, a resource can lose up to two and one-half months of its annual FCA Payment.

26. The availability component of the FCM proposal also has a provision that expels capacity resources that perform poorly for an extended period, until availability improves. Prior to clearing a unit to participate in the FCA, ISO-NE will determine whether the resource meets two criteria: 1) in any four-year period, was the resource available during less than 40 percent of the Shortage Events; and 2) did the resource fail to be available for ten or more Shortage Events during the four-year period? If both of these criteria are met, the resource will not be eligible to participate in the FCA. Until the resource achieves an availability score of 60 percent or higher in three consecutive years or has demonstrated to the satisfaction of ISO-NE that the source of the inadequate availability score has been remedied, it will remain ineligible.

27. The FCM contains several rules to address high concentrations of market power, whether held by buyers or sellers. First, the FCM proposes a set of auction rules that curb incentives to manipulate the market and distort capacity prices. Only specified types of bids are eligible to set the capacity clearing price. To ensure that the FCA clearing prices are determined competitively, the FCM is designed to allow new capacity to set the clearing price, thus providing a market-based measure of the cost of new entry. In addition, the FCM has specific market rules that declare the auction to possess insufficient competition, as well as provisions for setting the clearing price under such conditions. If the insufficient competition rule is triggered, new capacity resources are paid the capacity clearing price; existing capacity resources are paid the lower of the capacity clearing price or 1.1 times CONE.

28. Second, the Market Monitor will review bids priced above or below specified price thresholds, which are tied to percentages of CONE. For example, the Market Monitor will review and decide whether to accept into the auction a capacity resource that submits any type of de-list bid (*i.e.*, enabling it to exit the market temporarily or shut down permanently) that is higher than 0.8 times CONE. In such instances, should the Market Monitor determine that the bid is consistent with the resource's net risk-adjusted going-forward and opportunity costs, the bid is incorporated into the auction. In addition, the Market Monitor will review any new capacity or imported capacity bid below 0.75 times CONE, to determine whether the bids are consistent with the long run average costs of that new capacity resource or the opportunity cost (or another reasonable economic measure) for the import.

29. Third, the peak energy rent deduction is intended to help mitigate incentives to create price spikes in the energy market. Settling Parties assert that, while it may be profitable to raise prices in the energy market, the peak energy rent mechanism will remove any profits gained from the rise in prices because the extra revenues earned in the energy market are deducted from capacity payments.

B. Transition Period

30. June 1, 2010 is identified as the first period for which suppliers would receive payments pursuant to the FCA auction mechanism. The Settlement Agreement provides for a transition period—beginning December 1, 2006, ending June 1, 2010—during which, fixed payments will be made to all installed capacity. Below is a table that details the level of the payment as it increases over time during the transition period:

Transition Payments	
Period	Payment (\$/kW-month)
December 1, 2006 - May 31, 2007	\$3.05
June 1, 2007 – May 31, 2008	\$3.05
June 1, 2008 – May 31, 2009	\$3.75
June 1, 2009 – May 31, 2010	\$4.10

Transition payments will be netted against RMR payments and will be considered capacity payments for the purposes of netting in the locational forward reserves market. Settling parties state that no new compensation mechanism has been implemented and, to date, little new generation has been constructed in New England. Settling parties assert that such transition payments serve as a bridge to the implementation of the FCM and as a means to help ensure that existing generators remain available until new resources can be built. There is no locational component to the transition payments, meaning that suppliers in historically constrained regions of New England will receive the same per kW-month payments as suppliers in historically unconstrained regions.

31. Transition payments will be made by unforced capacity (UCAP) obligation holders (load-serving entities). UCAP obligations are determined by ISO-NE and are calculated as the load-serving entity's customers' proportionate share of peak load. Transition payments will be adjusted to account for unit availability. During the 3 1/2 year transition period, transition payments will be adjusted downward according to a modified equivalent demand forced outage rate (EFORd) measurement, which most heavily weights availability during times of greatest need.²⁸

32. The currently applicable RMR agreements in New England are scheduled to terminate upon the implementation or effectiveness of a locational ICAP mechanism. The Settlement Agreement explicitly states that the beginning of the first commitment period (June 1, 2010) will be considered to be the implementation or effectiveness of a locational ICAP mechanism rather than the transition period. The Settlement Agreement states that nothing prejudices the rights of any party to challenge, seek to terminate or support an RMR agreement on any other grounds or restrict any party's rights to seek, agree to or oppose any RMR modifications.

²⁸ EFORd measures the portion of time a unit is in demand, but is unavailable due to forced outages.

33. The Settlement Agreement outlines processes to implement the transition period and FCM following approval by the Commission. Market rules governing the FCM will be developed in detail and filed with the Commission in at least two packages. The first filing, tentatively planned by October 1, 2006, will include rules for implementing the transition provisions on December 1, 2006. The second filing, which must be made by February 15, 2007, will contain the rules for the FCM. The Settlement Agreement provides that market rules will be developed in accordance with NEPOOL's traditional rule review process and will include the opportunity for input from state utility regulators. Parties to the settlement may challenge the market rules only on the grounds that they are inconsistent with, or not necessitated by, the Settlement Agreement.

C. Other Features

34. A critical input into the FCM will be the determination of the installed capacity requirement, which will determine how much capacity will be purchased through the auctions. The Settlement Agreement establishes a general timeline for determining the installed capacity requirement. ISO-NE is currently conducting a stakeholder process to review the process for deriving the installed capacity requirement. ISO-NE hopes to conclude that stakeholder process during the third quarter of 2006 and file a revised process with the Commission, in the latter part of 2006. Based upon the outcome of that filing, the installed capacity requirement for the first auction will be filed during the third quarter of 2007, with a requested effective date of October 1, 2007, enabling the first auction to be conducted no later than early 2008.

35. Settling Parties waive their rights under section 206 of the FPA to seek a change in the Settlement Agreement or the market rules implementing the agreement for the period beginning March 6, 2006 through the earlier of September 5, 2008 or the date on which the prices from the second FCA become final (roughly 2 1/2 years). During this period, ISO-NE will retain its authority under section 205 of the FPA (subject to appropriate stakeholder processes) to file modifications of the market rules that address the terms of the Settlement Agreement. ISO-NE may exercise that authority only where it can demonstrate that failure to implement the proposed change would have a negative effect on 1) system reliability or security, or 2) the competitiveness or efficiency of the forward capacity or forward reserve markets. Were ISO-NE to make such a filing, Settling Parties will retain all of their rights to challenge the proposed modifications before the Commission.

36. The Settlement Agreement states that final prices derived from all auctions and the transition provisions cannot be changed unless required by the public interest under the

Mobile-Sierra standard.²⁹ Settling parties assert that one reason for adopting this standard for final auction prices is to reduce regulatory uncertainty, thus reducing the risk premium new entrants may require. The Settlement Agreement allows parties to challenge key inputs into the auction prior to the running of the auction. Not later than 90 calendar days prior to each FCA, ISO-NE will make an informational filing with the Commission in which it will identify: 1) the capacity zones applicable to that auction; 2) the resources qualified to participate in the FCA or reconfiguration auction specifically; and 3) conclusions of the Market Monitor regarding the acceptability of bids. Interested parties will have 15 days to file comments on or challenges to the determinations in that informational filing. Unless the Commission issues an order to the contrary within 75 calendar days following the informational filing, ISO-NE will use the determinations in the informational filing in the next FCA.

37. Results from FCAs will be filed with the Commission by ISO-NE pursuant to section 205 of the FPA. Parties will have 45 days to file objections to the auction results, and this will be the only means of challenging such results. Once this process is complete, the prices will be subject to the *Mobile-Sierra* public interest standard under section 4.C of the Settlement Agreement. Section 5 of the Settlement Agreement provides that ISO-NE's internal market monitoring unit will issue a full report analyzing the operations and effectiveness of the FCM 180 days after the second FCA and annually in its markets report thereafter.

III. Procedural Matters

38. Comments on the Settlement Agreement were filed by the following parties: Berkshire Power Company, LLC (Berkshire), Consolidated Edison Energy, Inc. (ConEd), EnerNOC, Inc. (EnerNOC), Exelon Generation Company, LLC and Exelon New England Holdings (Exelon), Industrial Energy Consumer Group (IECG), Load Supporters,³⁰ Long

²⁹ See Settlement Agreement at section 4.C and *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 344-45 (1956) (*Mobile*) and *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956) (*Sierra*).

³⁰ Load Supporters are: Connecticut Department of Public Utility Control, Connecticut Office of Consumer Counsel, New Hampshire Public Utilities Commission, Rhode Island Public Utilities Commission, Rhode Island Division of Public Utilities and Carriers, Vermont Public Service Board, Vermont Department of Public Service, and The Connecticut Power and Light Company, by its agent Northeast Utilities Service Company.

Island Power Authority and LIPA (LIPA), Maine Parties,³¹ Objecting Parties,³² PPL EnergyPlus, LLC and PPL Wallingford Energy LLC (PPL), PSEG Energy Resources & Trade LLC (PSEG), Reading Municipal Light Department (Reading), and Select Energy, Inc. (Select). NSTAR Electric and Gas Corporation (NSTAR) filed supplemental comments in opposition to the Settlement Agreement.

39. Reply comments were filed by the following parties: American National Power, Inc., Granite Ridge Energy, LLC and TransCanada Power Marketing Ltd. (American National Power), Calpine Energy Services, L.P. and Calpine Eastern Corporation (Calpine), Capacity Suppliers,³³ Connecticut Municipal Electric Energy Cooperative (CMEEC), ISO-NE, Lake Road Generating Company, L.P. (Lake Road), Load Supporters, Maine Parties, Massachusetts Municipal Wholesale Electric Company and Reading (MMWEC), Milford Power Company, LLC (Milford), National Grid USA (National Grid), New England Power Pool Participants Committee (NEPOOL), New York Independent System Operator, Inc. (NYISO), NRG Companies (NRG),³⁴ Objecting Parties, and PPL. On April 11, 2006, Exelon filed a motion for leave to file reply comments out of time and reply comments. On June 6, 2006, Black Oak Energy, LLC (Black Oak) and EPIC Merchant Energy, LP (EPIC) filed a motion to intervene out of time and a motion to file limited comments out of time.

³¹ Maine Parties are Maine Public Utilities Commission and Maine Public Advocate.

³² Objecting Parties are: Attorney General of the Commonwealth of Massachusetts, Richard Blumenthal, Attorney General for the State of Connecticut, NSTAR Electric and Gas Corporation, NEPOOL Industrial Customer Coalition, and The Energy Consortium (which includes President and Fellows of Harvard College, Brandeis University, Polaroid Corporation, USG Corporation, and Massachusetts Institute of Technology).

³³ Capacity Suppliers are: Boston Generating, LLC, Mystic Development, LLC, Mystic I, LLC, Fore River Development, LLC (collectively, "Boston Gen"), FPL Energy, LLC, Mirant Americas Energy Marketing, LP, Mirant Kendall, LLC, Mirant Canal, LLC, Entergy Nuclear Generation Company, LLC, Entergy Nuclear Vermont Yankee, LLC, Dominion Resources, Inc., Dominion Nuclear Connecticut, Inc. and Dominion Energy Marketing, Inc.

³⁴ NRG includes Devon Power LLC, Montville Power, Connecticut Jet Power and Middletown Power.

40. We will accept Exelon's motion to file reply comments out of time. We deny, however, the motion of Black Oak and EPIC to intervene and file initial comments at this late stage of the proceeding. We find that granting Black Oak and EPIC's motion would be disruptive given that its motion was filed less than a month before the June 30, 2006 date by which the Commission must act on the Settlement Agreement. Moreover, since the comments amount to a protest to the Settlement Agreement, granting the motion would prejudice those supporting the settlement by effectively denying them the opportunity to reply under the Commission's rules. Black Oak's and EPIC's arguments that they were not aware of the Settlement Agreement's impact on their interests are unpersuasive; the Settlement Agreement was filed three months before Black Oak and Epic sought to intervene, and was considered in the New England Power Pool stakeholder process, which should have alerted active participants in the New England markets like Black Oak and EPIC that their interests might be impacted.

IV. Discussion

A. General Comments in Support of the Settlement

41. The following parties filed comments in support of the Settlement Agreement: Load Supporters, Reading, EnerNOC, ConEd, Berkshire, Exelon, Select, and Lake Road. In general, these parties support acceptance of the Settlement Agreement without modification. For the most part, those submitting general comments supporting the settlement emphasize that it is the product of a complex and difficult negotiation and represents a careful and interconnected balancing of interests. Accordingly, most state that modifying any portion of the Settlement Agreement could upset this balance and risk unraveling the settlement entirely.

42. ConEd states that the settlement corrects deficiencies in the current market and is the most likely construct to attract and retain the resources needed for reliability. Exelon supports the request that the settlement be approved in its entirety as just and reasonable and in the public interest. Exelon further states that the forward commitment provision will allow existing generators to make informed decisions and will benefit load by facilitating a robust and cost effective regional planning process. Select asserts that the FCM accommodates various load parties by basing the compensation mechanism on a market outcome.

43. Load Supporters state that the FCM is designed to produce just and reasonable results and is a substantial benefit to New England electricity customers compared with LICAP. Load Supporters state that the FCM contains many of the elements derived from

prior alternatives, including the New England Resource Adequacy Market³⁵ and the New England Locational Resource Adequacy Market,³⁶ as well as the Central Resource Adequacy Market,³⁷ and rests on facts developed in the evidentiary record. Load Supporters state that the settlement resolves several of the material flaws that the parties had with the LICAP proposal by requiring load to purchase only the amount of capacity needed, by facilitating new entrant participation (including demand-side resources) through a three-year forward commitment period, and by using an auction to produce the lowest reasonable cost of new entry. Load Supporters also state that that another important feature of the settlement is that it allows load the opportunity to self-supply or contract bilaterally; thereby providing a hedge against volatility—an important feature for Connecticut, New Hampshire, and Vermont. Load Supporters also state that the Settlement Agreement provides a stakeholder process that includes participation by the New England state regulatory agencies, to determine the installed capacity requirement.

44. More specifically, Load Supporters state that the FCM increases the elasticity of supply, *i.e.*, an upward sloping supply curve, by procuring capacity three years in advance with a minimum one-year commitment period, by enabling potential new entrants to compete with existing suppliers, and by clearly defining the obligations of capacity suppliers. According to Load Supporters, this planning period enables existing capacity to provide quantities responsive to price, provides relief from reliability-based barriers to exit and enables demand-side resources to respond to price as well. They compare this feature to LICAP, which would commit resources only one month in advance of their obligation to perform and commit them for only one month at a time.

45. Load Supporters also state that the FCM procures only the amount of capacity necessary to maintain reliability, compared to LICAP which set a target of 5.4 percent above the installed capacity requirement and would pay suppliers for surpluses up to 15

³⁵ See “Statement in Support of the New England Resource Adequacy Market,” filed by Massachusetts Department of Telecommunications and Energy *et al.* in Docket No. ER03-563-030 (Sept. 13, 2005).

³⁶ See “Four State Commissions’ Proposed Alternative to LICAP”, filed by Rhode Island Public Utilities Commission, New Hampshire Public Utilities Commission, Vermont Public Service Board, Vermont Department of Public Service and Maine Public Utilities Commission in Docket No. ER03-563-030 (Sept. 13, 2005) (describing the proposed New England Locational Resource Adequacy Market).

³⁷ See ISO-NE March 1, 2004 compliance filing in Docket ER03-563-030 at 52.

percent above the installed capacity requirement. Load Supporters stated that this permits capacity in excess of the amount needed to retire, mothball, or sell into other markets. Load Supporters state that, unlike the LICAP's proposed administratively determined demand curve, the FCM sets price through a competitive auction. Load Supporters state that the FCM includes multiple constraints on market power. Load Supporters also state that the ISO-NE Market Monitoring Unit will evaluate the performance of the FCM and will prepare annual reports on the operation of the market.

46. In addition, Load Supporters state that, unlike LICAP, the FCM expressly defines the commitments that supply must make in return for load's substantial capacity payments. Load Supporters also state that the minimum year-long commitment period for capacity resources locks in price and firm obligations giving load certainty over price and reliability while giving suppliers certainty over revenue. They also note that the FCM further reduces risks for new capacity investment by providing 1) an option for new suppliers to lock in a five-year commitment period, 2) annual reconfiguration auctions to cover the risk of non-performance, and 3) a flexible financial assurance policy.

47. Load Supporters argue that the proposal to adjust the monthly capacity payments determined by the FCA not only reduces incentives for suppliers to withhold in the energy market but also provides a hedge for load against energy market price spikes. Load Supporters state that the Shortage Event mechanism will reward resources that perform during periods of system stress and penalize those resources that fail to perform. Load Supporters also state that availability will be improved with the settlement provisions regarding gas delivery.

48. Lake Road states that the settlement should be approved as in the public interest. Lake Road asserts that in the long-term, the FCM will provide a more sophisticated method to encourage the right amount of capacity in the right locations. NEPOOL supports the settlement and, without taking positions on the issues, opposes any change or condition that would upset the negotiated balance of the Settlement Agreement.

B. General Comments in Opposition to the Settlement

49. Comments in opposition to the Settlement Agreement are addressed in detail below.

C. Standard of Review and Commission Conclusions Regarding Overall Justness and Reasonableness of the Settlement

50. In the explanatory statement, Settling Parties note that the Commission ““can approve contested settlements as long as it determines that the proposal will establish just and reasonable rates.””³⁸ They state that the Commission must support its decision to accept a contested settlement with substantial evidence or a finding that there is no genuine issue of material fact as to the contested matter. Noting the four approaches in *Trailblazer*³⁹ that the Commission may utilize to address a contested settlement, Settling Parties urge the Commission to approve the Settlement Agreement as a package under the second *Trailblazer* approach, which (as discussed below) allows the Commission to approve a settlement as a package if it determines that the overall result of the settlement is just and reasonable.⁴⁰ Settling Parties argue that the Settlement Agreement is a complete package that reflects a complex compromise among the affected parties, and that while those parties may oppose some individual components within the agreement, they have agreed to the settlement as a package. Settling Parties contend that changing any aspect of the Settlement Agreement would upset the balance achieved among the parties and result in calls to change other aspects of the agreement. Settling Parties also assert that severing contesting parties (under the fourth *Trailblazer* approach) is inappropriate here because the settlement creates a structure applicable to all generation and load in New England, meaning that objecting parties cannot continue to litigate the transition charges or market design without affecting the rates charged to and received by other parties and upsetting the balance achieved in the Settlement Agreement.

³⁸ Explanatory Statement at 4, citing *New Orleans Public Service, Inc. v. FERC*, 659 F.2d 509, 512 (5th Cir. 1981) (citing *Placid Oil Co. v. FPC*, 483 F.2d 880, 893 (5th Cir. 1973), *aff'd sub nom. Mobil Oil Corp. v. FPC*, 417 U.S. 283, 312-13 (1973)).

³⁹ *Trailblazer Pipeline Company*, 85 FERC ¶ 61,345 (1998), *order on reh'g*, 87 FERC ¶ 61,110 (1999) (*Trailblazer*). The four approaches laid out in *Trailblazer* are: (1) Commission renders a binding merits decision on each contested issue, (2) Commission approves the settlement based on a finding that the overall settlement as a package is just and reasonable, (3) Commission determines that the benefits of the settlement outweigh the nature of the objections, and the interests of the contesting party are too attenuated, and (4) Commission approves the settlement as uncontested for the consenting parties, and severs the contesting parties to allow them to litigate the issues raised.

⁴⁰ In their comments, Exelon and Select, among other commenters, support this request.

51. Parties submitting comments on the Settlement Agreement also discussed the applicable standard of review. IECG, Objecting Parties, Load Supporters and American National Power all state that to approve a contested settlement, the Commission “must make ‘an independent finding supported by substantial evidence on the record as a whole’ that the Settlement is just and reasonable[,] . . . produce[s] a reasonable resolution of the proceedings” or that “‘there is no genuine issue of material fact.’”⁴¹ Additionally, IECG states that the fact that a settlement agreement was agreed to by many parties does not guarantee that the result is just and reasonable.⁴² Similarly, Objecting Parties argue that the number of parties supporting a proposed settlement, while a factor to consider, is not dispositive in determining whether to approve the settlement.⁴³ American National Power adds that the Commission has broad discretion when considering contested settlements.⁴⁴

52. Maine Parties, Load Supporters and American National Power all discuss the *Trailblazer* approaches to addressing contested settlements, particularly the second approach. Load Supporters note that the Commission explained the second *Trailblazer* approach in the context of the approval of contested settlements in *Indicated Shippers*⁴⁵ and *Pacific Gas Transmission Co.*⁴⁶ In those cases, the Commission emphasized that to be approved as a package, the settlement rates must be shown to be less than or equal to the just and reasonable rates that would likely result from litigation.⁴⁷ Load Supporters also note that in *Trailblazer*, the Commission stated that when parties ask that a

⁴¹ See, e.g., Comments in Opposition to the Proposed Settlement Agreement of IECG at 2, citing *Mobil Oil Corp. v. FPC*, 417 U.S. 283, 314 (1974) and *San Diego Gas & Electric Company*, 108 FERC ¶ 61,002 at 61,010-011 (2004).

⁴² Comments in Opposition to the Proposed Settlement Agreement of IECG at 3-4, citing *NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158 (D.C. Cir. 1998).

⁴³ See Comments in Opposition to Settlement of Objecting Parties at 12-13, citing *NorAm Gas Transmission Co. v. FERC*, 148 F. 3d 1158 (D.C. Cir. 1998) and *Laclede Gas Co. v. FERC*, 997 F.2d 936 (D.C. Cir. 1993).

⁴⁴ Reply Comments of American National Power at 7, citing *Arctic Slope Regional Corp. v. FERC*, 832 F.2d 158, 164 (D.C. Cir. 1987).

⁴⁵ *Indicated Shippers v. Sea Robin Pipeline Co.*, 81 FERC ¶ 61,146 (1997) (*Indicated Shippers*).

⁴⁶ 82 FERC ¶ 61,289 (1998).

⁴⁷ Initial Comments of Load Supporters in Support of Offer of Settlement at 9-10, citing *Trailblazer*, 85 FERC ¶ 61,345 at 62,342-343.

settlement be considered as a package, it would “‘try to honor the parties’ intent’ and consider the justness and reasonableness of the package in its entirety.”⁴⁸ ISO-NE, in reply to comments opposing the Settlement Agreement, adds that the Commission has previously held that it may approve a contested settlement as a package if the overall result is just and reasonable even if some aspects of the settlement are problematic.⁴⁹ Further, ISO-NE notes that a contested settlement may be approved if, as a whole (considering both contested and uncontested issues), it provides a just and reasonable result.⁵⁰ Finally, it states that “[t]he Commission need only find that the overall package, resulting from the give and take of the bargaining which led to the settlement, falls within” the just and reasonable range.⁵¹

53. IECG asserts that the Settlement Agreement does not provide a just, reasonable or otherwise lawful resolution of the proceeding, and that the Settling Parties have not offered substantial record evidence that the agreement will result in just and reasonable rates or that the settlement will provide contesting parties with a result that is at least as good as the result they could achieve through litigation on the merits. According to IECG, the Settling Parties have only provided a comparison between the rates the Commission might have approved when ruling on the Initial Decision and the transition payments, which it argues is insufficient to support the increased costs contemplated by the transition period or to allow the Commission to conclude that parties opposing the agreement would not be better off through continued litigation.⁵²

54. Maine Parties, focusing on the procedural avenues in *Trailblazer*, argue that the Commission’s only options are to conditionally accept the settlement, sever the contested issues and initiate further proceedings to resolve those issues, or reject the entire settlement and initiate hearing procedures. Like IECG, they contend that the record lacks the substantial evidence necessary to resolve the contested material issues of fact on the

⁴⁸ Initial Comments of Load Supporters in Support of Offer of Settlement at 10.

⁴⁹ Reply Comments of ISO-NE at 16, citing *San Diego Gas & Electric Co. v. Sellers of Energy Ancillary Services*, 108 FERC ¶ 61,002 at 61,011 (2004).

⁵⁰ Reply Comments of ISO-NE at 16, citing *Trailblazer*, 85 FERC ¶ 61,345 at 62,342.

⁵¹ *Id.*, citing *Trailblazer*, 85 FERC ¶ 61,345 at 62,343.

⁵² As discussed further below, IECG notes that the LICAP mechanism recommended in the Initial Decision would have included elimination of RMR agreements, improved availability metrics, and included other features that make a comparison to the transition payments insufficient.

merits, approve the overall settlement as a package, or find that the benefits of the settlement outweigh the objections. Maine Parties also argue that the transition payments cannot be found just and on reasonable based on a comparison to the rates that might have resulted from the Initial Decision, contrary to the arguments of Load Supporters. According to Maine Parties, neither *Trailblazer* nor the precedents it cites suggest that the Initial Decision, which was never reviewed by the Commission and later set aside, should be considered the likely outcome of litigation. Additionally, Maine Parties note that in *Indicated Shippers* (cited by Load Supporters), the Commission, after finding that the parties had raised genuine issues of material fact, went on to determine the issues on the merits after the parties agreed that the record contained substantial evidence upon which the Commission could make a merits determination. Maine Parties also note that in *Indicated Shippers* the Commission engaged in a thorough analysis to determine the likely outcome of litigation, which Load Supporters do not suggest the Commission undertake here.

55. Responding to arguments that the record lacks the substantial evidence necessary to approve the Settlement Agreement, ISO-NE argues that the Affidavits submitted with the Agreement, the written proposals for alternatives to LICAP submitted prior to the oral argument, and the oral argument itself all represent substantial evidence upon which to base approval of the settlement. Moreover, ISO-NE states that the extensive record developed in the LICAP proceeding and the Commission's orders in other proceedings concerning the development of capacity markets provide substantial evidence.⁵³ ISO-NE also states that the Commission has previously held that it is not limited to opinion testimony and may rely on a wide range of materials as substantial evidence, including its own orders, tariffs and certificates on file, and its general policies.⁵⁴

56. Load Supporters, as well as ISO-NE and Capacity Suppliers, also contend that the parties objecting to the settlement have raised no genuine issues of material fact.⁵⁵ ISO-NE argues that factual contentions made by opponents of the Settlement Agreement are

⁵³ ISO-NE notes that the FCM incorporates features of many other models that the Commission has received evidence on in this and other proceedings. *See* Reply Comments of ISO-NE at 18-19.

⁵⁴ *Id.* at 18, citing *Williston Basin Interstate Pipeline Co.*, 68 FERC ¶ 61,357 at 62,432-33 (1994).

⁵⁵ According to ISO-NE, "it is well settled that 'a genuine issue of material fact sufficient to preclude approval of a settlement agreement must be a dispute of the basic facts underlying the settlement.'" Reply Comments of ISO-NE at 12 (citation omitted).

either not valid and thus do not rise to the level of material facts, or are questions of law and policy and not facts themselves.

57. In reply comments, ISO-NE argues that the Commission has broad discretion to make policy determinations on technical matters of market and rate design, and that it has the authority to decide, based on its expertise, that the Settlement Agreement is just and reasonable as a package.⁵⁶ Additionally, in response to arguments from opponents of the Settlement Agreement regarding the weight to be given to the amount of support for the agreement, ISO-NE argues that the Commission's precedent strongly favors settlements, particularly those that have broad support, and that the Commission may approve a settlement even when a particular aspect of it deviates from Commission policy.⁵⁷

Commission Conclusion

58. The Commission has broad authority and discretion under Rule 602(h) of its regulations to address contested settlements.⁵⁸ Courts have confirmed the Commission's authority to approve contested settlements, so long as the proposal will establish just and reasonable rates.⁵⁹ Under Rule 602(h), the Commission may decide the merits of the contested issues if the record contains substantial evidence on which to base a reasoned decision or if the Commission determines that there is no genuine issue of material fact. If the Commission finds that the record lacks substantial evidence or that the contesting parties or issues cannot be severed, the Commission may establish hearing procedures to supplement the record, or it may take other appropriate action.⁶⁰

59. In *Trailblazer*, the Commission explained at length the standards and procedures it employs in ruling on contested settlements. The Commission stated that, in reviewing a

⁵⁶ Reply Comments of ISO-NE at 10-11, *citing in part Elec. Consumers Res. Council v. FERC*, 407 F.3d 1232 (D.C. Cir. 2005); *Fuels Research Council, Inc. v. FPC*, 374 F.2d 842 (7th Cir. 1967); *Entergy Servs. v. FERC*, 319 F.3d 536 (D.C. Cir. 2003).

⁵⁷ Reply Comments of ISO-NE at 20 (citations omitted). ISO-NE also says that this agreement does not deviate from any applicable Commission policy.

⁵⁸ 18 C.F.R. § 385.602(h) (2005).

⁵⁹ *See New Orleans Public Service, Inc. v. FERC*, 659 F.2d 509, 511-12 (5th Cir. 1981), *citing Placid Oil Co. v. FPC*, 483 F.2d 880, 893 (5th Cir. 1973), *aff'd sub nom. Mobil Oil Corp. v. FPC*, 417 U.S. 283, 312-13 (1974).

⁶⁰ *See* 18 C.F.R. § 385.602(h)(1)(ii)(B) (2005). In *Arctic Slope Regional Corp. v. FERC*, 832 F.2d 158, 164 (D.C. Cir. 1987), the court observed that "the breadth of discretion trumpeted by Rule 602(h)(1)(ii)(B) is manifest."

settlement, it must first determine whether the settlement presents an acceptable outcome for the case that is consistent with the public interest. The Commission acknowledged the value of settlements, but stated that some cases may involve an overriding public interest that outweighs the interest in achieving a settlement. In such instances, the Commission has modified those settlements to be consistent with Commission policy.⁶¹

60. If the Commission concludes that a contested settlement provides an acceptable outcome for a case, it must next determine the approach it will employ to address the contested issues. In *Trailblazer*, the Commission explained four approaches it has taken for approving a contested settlement despite the objections of the contesting party. Under the first approach, if there is an adequate record, the Commission can address each of the contested issues on the merits, approving the settlement if the Commission finds that each of the contesting party's contentions lacks merit. This approach is appropriate where the issues are primarily policy issues or the parties have agreed that the record is sufficient to decide the issues on the merits. However, the Commission explained that, even where the settlement cannot be approved under the first approach, it may be approved under other approaches. Thus, under the second approach, even if some individual aspects of a settlement may not be just and reasonable standing alone, the Commission may approve a contested settlement as a package if the overall result of the settlement is just and reasonable. Under this approach, the Commission will not make a merits decision on whether each element of the settlement package is just and reasonable but will determine whether the overall package falls within a zone of reasonableness.⁶² When the Commission takes this approach, it need not find that the settlement rate is exactly the rate the Commission would find just and reasonable on the merits after litigation and need only find that the settlement rate falls within a zone of reasonableness. The Commission must also find under this approach that the contesting party would be in no worse position under the settlement than if the case were litigated.

61. Under the third approach, if the settlement is not found to satisfy the just and reasonable standard, the Commission may approve the settlement where the benefits of the settlement outweigh the nature of the objections, and the contesting parties' interest is too attenuated so that the settlement may be approved under the fair and equitable standard applicable to uncontested settlements. The third alternative usually has included a finding that the contesting party would have another forum in which to raise its contentions. The fourth approach is severance of the contesting party, permitting that party to obtain a litigated result, and approving the settlement as to the consenting parties.

⁶¹ *Trailblazer*, 85 FERC at 62,341.

⁶² *Id.* at 62,342; *order on reh'g*, 87 FERC at 61,440.

The Outcome Under the Settlement Agreement Meets the *Trailblazer* Standards for Approval

62. Pursuant to our *Trailblazer* standards, the Commission first finds that the Settlement Agreement is consistent with the public interest.⁶³ The results, including the long-term FCM and short-term transition mechanisms, resolve the deficiencies in New England's existing capacity market identified by the Commission and the parties to this case. As noted above, the Commission instituted these section 206 proceedings in the April 25 Order in response to the compensation problems faced by generating resources that are needed for reliability but could not obtain sufficient revenues in the markets to continue operation. The Commission stated that its long-term goal was to approve a locational or deliverability mechanism to ensure that capacity resources in New England are appropriately compensated, particularly in highly constrained areas.⁶⁴ In the June 2 Order establishing hearing procedures on ISO-NE's proposed LICAP mechanism, the Commission again found that New England faced significant Reliability Compensation Issues in both the short and long terms, particularly in constrained areas.⁶⁵ In analyzing the proposed LICAP mechanism, the Commission noted that a capacity market mechanism should both provide adequate revenues to appropriately compensate (and keep in service where needed for reliability) existing capacity resources and provide incentive for the development of new infrastructure in areas where it is most needed.⁶⁶

63. Moreover, as the record in this proceeding has developed, both the parties to this case and the Commission have recognized the necessity of a workable capacity market to meet the need for additional infrastructure in New England. While the region has sufficient capacity to meet reliability requirements today, reserve margins are barely adequate, and deficits are predicted in the very near future.⁶⁷ At the oral argument, the

⁶³ See *NAACP v. FPC*, 425 U.S. 662, 670 (1976) (noting that the use of the words "public interest" in the FPA is a "charge to promote the orderly production of plentiful supplies of electric energy and natural gas at just and reasonable rates.")

⁶⁴ April 25 Order at P 37.

⁶⁵ June 2 Order at P 35 *et seq.*, citing *PJM Interconnection, L.L.C.*, 107 FERC ¶ 61,112 (2004).

⁶⁶ See June 2 Order at P 40-43, 49-52; *see also* November 8 Order on Rehearing at P 65-67.

⁶⁷ See, e.g., Executive Summary of the ISO-NE Regional System Plan 2005, attached to Notice of Proposed Speakers and Time Allocation for Oral Argument filed by ISO-NE in Docket No. ER03-563-030 (Sept. 14, 2005).

parties almost unanimously agreed that the status quo presents significant problems that the Commission must address.⁶⁸ The record from the oral argument is replete with virtually unchallenged statements that existing generators needed for reliability are not earning sufficient revenues (and are in fact losing money), and that additional infrastructure is needed soon to avoid violations of reliability criteria.⁶⁹

64. The Settlement Agreement provides necessary solutions to resolve these deficiencies in New England's current ICAP market and the resulting impacts those deficiencies have had on New England's infrastructure, and is well supported both by the record and by Commission policy.⁷⁰ The Settlement Agreement incorporates the primary components of the two alternatives proposed by state entities and discussed at oral argument: a forward resource auction, a descending clock auction, penalties for non-performance, and a phase-in or transition period.⁷¹

65. First, both the FCM and the interim transition mechanism will provide the revenues needed by generators to keep them in operation to preserve reliability.⁷² Below, we discuss in more detail the justness and reasonableness of the transition payments as a short-term measure to ensure that existing generating units remain available. The FCM

⁶⁸ Tr. of Oral Argument at 252:8-12 (Chairman Kelliher noting that "every presenter, other than one, agreed that the Commission has to take some kind of action").

⁶⁹ See, e.g., Tr. Of Oral Argument at 36:21-24; 44:7-11; 76:6-22; 150:9-151:6; 167:1-4; 237:9-12.

⁷⁰ See, e.g., *PJM Interconnection, L.L.C.*, 107 FERC ¶ 61,112 at 15 (noting that the Commission, in addressing Reliability Compensation Issues, will take account of both present circumstances and expected needs).

⁷¹ See, e.g., Tr. of Oral Argument at 148 *et seq.* and 165 *et seq.*; see also "Statement in Support of the New England Resource Adequacy Market," filed by Massachusetts Department of Telecommunications and Energy, Connecticut Department of Public Utility Control *et al.* in Docket No. ER03-563-030 (Sept. 13, 2005); "Four State Commissions' Proposed Alternative to LICAP", filed by Rhode Island Public Utilities Commission, New Hampshire Public Utilities Commission, Vermont Public Service Board, Vermont Department of Public Service and Maine Public Utilities Commission in Docket No. ER03-563-030 (Sept. 13, 2005) (describing the proposed New England Locational Resource Adequacy Market).

⁷² See, e.g., Brief Opposing Exceptions of ISO-NE at 2-3; *ISO-NE 2004 Annual Markets Report* at 111-12, available at http://www.iso-ne.com/markets/mkt_anlys_rpts/annl_mkt_rpts/2004/2004_annual_markets_report_.pdf.

construct, when fully implemented, will provide a market-based mechanism to appropriately value capacity resources based on their location, satisfying cost-causation principles.⁷³ Many of the load representatives were particularly concerned that the LICAP proposal did not “impose any reciprocal obligation on these generators to continue operating over the long-term.”⁷⁴ The FCM addresses these concerns by requiring new capacity that bids in the FCAs to meet milestones regarding project feasibility and an interconnection analysis showing the impact of connecting to the transmission grid. In addition, the forward-looking nature of the FCM will provide appropriate signals to investors when new infrastructure resources are necessary with sufficient lead time to allow that infrastructure to be put into place before reliability is sacrificed.⁷⁵ The locational component of the FCM will ensure that the addition of new infrastructure is targeted to where reliability problems are most imminent.⁷⁶

66. The fact that this Settlement Agreement resolves all of the outstanding issues in a difficult, contentious and lengthy matter also weighs in our decision that the settlement is consistent with the public interest. The Settlement Agreement represents difficult compromises among the diverse parties to this proceeding that, if found just and reasonable, should be honored. From October 2005 until March 2006, over 175 representatives, including representatives from all of the state public utility regulatory agencies, as well as representatives of transmission owners, generators, power traders and marketers, demand response and intermittent resource owners, consumer-owned utility systems and end users, engaged in informal and formal settlement negotiations.⁷⁷ Moreover, the Settlement Agreement, by ending this protracted litigation, will bring a needed measure of stability and allow New England to move forward on other market enhancements. Additionally, the Commission strongly favors settlements, particularly in difficult cases like the instant proceeding.⁷⁸

⁷³ See, e.g., *PJM Interconnection, L.L.C.*, 107 FERC ¶ 61,112 at 19-20; *PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 at P 49-51 (2006).

⁷⁴ Brief on Exceptions of the New England Conference of Public Utility Commissioners at 2.

⁷⁵ See *PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 at P 67-72.

⁷⁶ *Id.* at P 49-51.

⁷⁷ Reply Comments of NEPOOL Participants Committee at 2.

⁷⁸ See, e.g., *Idaho Power Co.*, 109 FERC ¶ 61,308 at P 5 (2004) (stating that the Commission is “strongly in favor of settlements, particularly in cases [that are] hotly contested and complex.”).

67. The Settlement Agreement is also consistent with the public interest because it comports with the recently expressed intent of Congress regarding this case. In section 1236 of the Energy Policy Act of 2005, Congress noted the concerns voiced by the governors of the New England states regarding the LICAP mechanism, and declared that the Commission should carefully consider their objections.⁷⁹ The oral argument held in this proceeding considered the states' objections to the LICAP mechanism and their proposals for alternative capacity market designs. Settlement discussions followed regarding alternatives. This settlement is a product of those discussions, and includes measures to address many of the objections voiced by the states, responding to the sense of Congress in section 1236.

The Overall Result of the Settlement Agreement is Just and Reasonable

68. To address the contested issues raised by those opposing the Settlement Agreement, we will use the second approach articulated in *Trailblazer*, as requested by the Settling Parties.⁸⁰ Using this approach here is appropriate for several reasons. First, we find that the record in this proceeding is sufficient to allow us to make a determination that as a package, the settlement is just and reasonable. The record includes, among other items, both written submissions and oral argument testimony concerning various approaches to designing New England's capacity market, data regarding current and projected capacity prices in New England, price projections under both the settlement and various LICAP demand curve proposals, and information regarding the current and projected need to develop new infrastructure in New England. Moreover, with regard to the transition payments (the most heavily protested aspect of the Settlement Agreement), we agree with the presiding Settlement Judge that this record provides a thorough basis for the Commission's decision to approve the Settlement Agreement as a package.⁸¹

69. In addition to honoring the intent of the Settling Parties, the second of the four *Trailblazer* approaches is the most appropriate here. It would be inappropriate to strictly apply the first approach here because the Settlement Agreement contains several complex and interrelated features intended to be considered as an overall package, and altering any of those features will have consequences for other portions of the settlement. We will consider the contested issues below, however, to ensure the overall justness and

⁷⁹ Energy Policy Act of 2005, Pub. L. No. 109-58, § 1236, 119 Stat. 961 (2005).

⁸⁰ See *Trailblazer*, 87 FERC at 61,440 (stating that the Commission will try to honor the parties' intent that a settlement be considered as a package).

⁸¹ *Report on Contested Settlement by Settlement Judge, Devon Power LLC*, 115 FERC ¶ 63,013 (2006).

reasonableness of the settlement as a package. The third approach is unavailable here because while we believe that the settlement, as a package, provides significant benefits that outweigh the nature of the objections raised, the parties raising such objections (which include load representatives of certain states) have more than an attenuated interest. Finally, the fourth approach is not appropriate here because the Settlement Agreement provides a capacity market structure that will apply throughout New England, making it impossible to effectively sever any of the contesting parties to allow them to further pursue the issues they raise, since the resolution of those issues will affect all the parties.

70. Applying the second *Trailblazer* approach here, we find that the parties objecting to the Settlement Agreement would “be in no worse position under the terms of the settlement than if the case were litigated,” and that the Settlement Agreement, as a package, achieves an overall just and reasonable result within a zone of reasonableness.⁸²

71. We find that the Settlement Agreement achieves an overall just and reasonable result for many of the same reasons we articulated above in finding that it provided an acceptable outcome for this case consistent with the public interest. The settlement package, including both the FCM and the interim transition mechanism, resolves the issues raised in this proceeding concerning the under-compensation of capacity resources in New England, and provides the appropriate market structure to ensure that generating resources are appropriately compensated based on their location and contribution to system reliability and provides incentives to attract new infrastructure where needed. As discussed below, the key price-determining parameters of the FCM descending clock auction (such as CONE) are appropriate and adequately supported in the record. “A just and reasonable rate is not a product of any single formula, but is instead a rate within a broad ambit of various rates which may be just and reasonable,” and as we discuss below, none of the parties opposing the Settlement Agreement has shown that the settlement (or any specific aspect of it) is outside of this “range of reasonableness.”⁸³

72. We find that the parties opposing the Settlement Agreement would be no worse off under the settlement than through continued litigation. The affidavits and other evidence provided by the Settling Parties and others in support of the Settlement Agreement show that the settlement, and particularly the transition period, results in rates

⁸² *Trailblazer*, 87 FERC ¶ 61,110 at 61,339.

⁸³ See *Belco Petroleum Corp. v. FERC*, 589 F.2d 680, 689 (D.C. Cir. 1979), citing *Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968); *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944); *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585-86, (1942).

for capacity that are lower than the projected payments under ISO-NE's proposed demand curve (which we note was adopted in the Initial Decision) and that are comparable to the rates under alternative demand curves proposed at the hearing, bringing those rates within a range that we find is just and reasonable.⁸⁴ We address this issue more specifically below with regard to the opposing parties' specific arguments that the transition payments cannot be approved on the basis of a comparison with the rates that would have resulted under LICAP.⁸⁵

73. Further, we note that, while Objecting Parties' are correct that the level of support for the Settlement Agreement is not dispositive, the Commission can give weight to the broad-based support the Settlement Agreement received.⁸⁶ In this difficult, contentious proceeding, the Settlement Agreement was either supported or not opposed by 107 of the 115 parties in the proceeding.⁸⁷ We agree with the Settlement Judge's characterization of this level of support as "quite extraordinary and . . . noteworthy."⁸⁸

D. Specific Issues Raised in Comments on Proposed Settlement Agreement and Reply Comments, and Commission Conclusions

74. As noted above, while we are approving the Settlement Agreement as just and reasonable as a package under the second approach of *Trailblazer*, we analyze below the specific issues raised by parties opposing the settlement to ensure that each, when considered as part of the overall package, meets the standards articulated in *Trailblazer*.

1. Transition Mechanism

75. As noted above, during the transition period, fixed payments will be paid to all installed capacity. These payments are intended to serve as a bridge to the FCM, and are

⁸⁴ See, e.g., Explanatory Statement in Support of Settlement Agreement at 34-40; Attachment 6 to Settlement Agreement (Affidavit of David LaPlante); Comments of Load Supporters and Affidavit of Miles O. Bidwell, Jr., Ph.D.

⁸⁵ For example, we address below Maine Parties' contentions that the Commission should consider a lower LICAP demand curve for Maine when comparing the transition payments to the LICAP mechanism, among other issues.

⁸⁶ See *Laclede Gas Co. v. FERC*, 997 F.2d 936, 946 (D.C. Cir. 1993); *NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158, 1164-65 (D.C. Cir. 1998).

⁸⁷ See *Report on Contested Settlement by Settlement Judge, Devon Power LLC*, 115 FERC ¶ 63,013 at P 15 (2006).

⁸⁸ *Id.*

not locational. All suppliers will receive transition payments, though these payments will be netted against RMR payments as well as adjusted to account for outages.

76. Several parties—IECG, Maine Parties and Objecting Parties—oppose the transition payments for a variety of reasons. First, they argue that there is no evidence to support the level of the transition payments. Objecting Parties assert that there is no record evidence that examined the amount of revenue required to keep existing resources available and nothing to indicate that the transition payments were compared against such a study. Maine Parties assert that there is insufficient evidence in the record on which the Commission may base a just and reasonable finding and that “a hearing would reveal that the transition payments are unjust and unreasonable” as they exceed “what is needed by generators” to supplement revenues from other markets.⁸⁹ IECG asserts that Settling Parties do not make a case that the costs of the transition payments are equivalent to the costs of the transition period. Maine Parties submit that the rationale that lower rates are necessarily just and reasonable is inconsistent with Commission precedent.⁹⁰ Maine Parties also state that ISO-NE has failed to justify that transition payments are necessary to retain existing generation in Maine. Maine Parties submit further that most Maine suppliers would continue to operate without transition payments as they have been setting energy prices.

77. IECG, Maine Parties and Objecting Parties further argue that the transition payments are not connected to an added service or benefit. The parties note that during the transition period, some suppliers will be paid in the locational forward reserves market and some will continue to be paid under RMR contracts. Objecting Parties assert that, rather than target financially distressed generation needed for reliability, the transition payments simply extend capacity payments to all capacity suppliers. Objecting Parties state that the transition payments are “money for nothing”⁹¹ and argue that existing RMR contracts should be eliminated at the beginning of the transition period. IECG similarly notes that there is no restraint upon RMR agreements. IECG states that the transition payments will not result in new entry and will not provide a reliability benefit to consumers as nothing is required of suppliers other than their continued existence. IECG further objects to the notion that many generators that currently receive adequate compensation (whether through ICAP or RMR or locational forward reserves market payments) will also receive transition payments. Objecting Parties assert that transition payments will not prevent entities that earn insufficient revenue during the

⁸⁹ Comments of Maine Parties at 12.

⁹⁰ *Id.* at note 30.

⁹¹ Comments of Objecting Parties at 19.

transition period from filing for RMR agreements and that the new availability provisions will not affect generators behavior. Objecting Parties state that were it not for the preservation of RMR agreements, parties “may decide to advance the proposition that transition payments are needed to maintain existing capacity until FCM payments begin.”⁹²

78. All of the above parties argue that it is inappropriate to compare the transition payments to hypothetical LICAP payments as the Commission never ruled on the LICAP proposal. Objecting Parties contend that the “less than LICAP” arguments many settling parties offer is a “wholly insufficient basis” for supporting the Settlement Agreement.⁹³ Maine Parties and IECG argue that a comparison to the level of LICAP payments as the likely litigated outcome is irrelevant to whether the transition payments are just and reasonable. Objecting Parties and IECG submit that LICAP payments were designed to achieve different objectives. Objecting Parties state that while LICAP rates were designed to elicit new construction, supporters make no such claim in reference to the transition payments. Moreover, Objecting Parties argue that while LICAP payments, however flawed, were based on estimated costs of new construction, there is no cost justification for the transition payments. IECG notes that the LICAP proposal would have eliminated RMR contracts, would have adjusted LICAP payments for peak energy rents and held the potential for a substantial availability adjustment. Maine Parties state that transition payments are not adjusted for PER. Maine Parties and IECG argue that an analysis of comparative savings cannot provide a foundation for finding transition payments just and reasonable. IECG argues that the Commission must determine that the transition payments are just and reasonable. Maine Parties state that the appropriate comparison is to the current vertical demand curve in a locational ICAP market.

79. Objecting Parties argue that the first FCA (held in early 2008) will set a price all existing resources can expect to receive during the commitment period and thus there is no need for a bridge to FCM.

80. Maine Parties state that the transition mechanism disregards location and fails to account for Maine’s capacity surplus. Maine Parties argue that this capacity surplus is unlikely to disappear during the transition period and therefore the price of capacity in Maine would likely not rise to the level of the transition payments. Maine Parties state that capacity payments should reflect the limited value of capacity during the transition period and reflect the unique circumstances of Maine.

⁹² Reply Comments of Objecting Parties at 3.

⁹³ *Id.* at 7-8.

81. Maine Parties also assert that if the Commission accepts the Settlement Agreement, it should modify the transition payments for the Maine zone to \$2.00/kW-month. In the alternative, Maine Parties submit that the issue could be severed from the proceeding and set for hearing. Maine Parties state that this level would be modestly higher than prices in New York, which serve as a reasonable comparison. IECG states that it may be appropriate for some level of transition payments if there is a relationship to the value received; however, parties do not make this case. IECG states that if the Commission accepts the Settlement Agreement, it should reduce the transition payments by 50 percent. Objecting Parties assert that for the transition mechanism to be just and reasonable, transition payments should be paid only to units needed for reliability that are not recovering going forward costs.

82. PSEG, while not opposing the Settlement Agreement, states that the capacity market will not account for the locational value of generation for five years and that the transition payments will not be sufficient to attract new market entry. Therefore, they argue, the transition mechanism will not permit generation, transmission, and demand side to compete.

83. Load Supporters, Select, Berkshire, NRG, Calpine and Lake Road all submitted comments or reply comments supporting the transition payments. Load Supporters state that the transition mechanism is an interim step to improve resource adequacy and reliability for existing suppliers until the FCM can be fully implemented. They argue that the transition mechanism provides predictable capacity payments that are not subject to the existing “all or nothing” capacity market and are not subject to the actions of other generators. Load Supporters also state that the transition mechanism removes uncertainty, provides a six month commitment period, and includes an availability adjustment if a resource fails to perform. Load Supporters state that the transition mechanism will not be subject to the potential for market power and, through the use of transition payments that are lower than the projected LICAP payments together with RMR contracts, will meet its purpose of compensating existing generation sufficiently to remain available until new generation can be constructed. They also state that the record (in particular, ISO-NE’s LICAP price projections during the transition period) shows no difference in prices between Maine and the Rest-of-Pool, and thus there is no basis to differentiate the amount of capacity payments by region, noting that RMR agreements are still paid locally during this period. Under these circumstances a locational aspect to the transition would not serve to promote increased reliability, Load Supporters contend.

84. Load Supporters also contend that the settlement balances short-term and long-term objectives during the transition period and that deconstructing the settlement to alter the transition would create implications for other aspects of the agreement. Load Supporters state that, while it is true that the full benefits of the market will be realized once FCM is fully implemented, the transition period provides superior benefits to load

than either the current regime or the likely litigated outcome. Load Supporters argues the transition mechanism is superior to the Initial Decision which would have adopted a permanent solution. Under the Settlement Agreement, the transition mechanism would apply for the interim until the FCM provides a competitive market. Load Supporters describe the following benefits: the availability metric that will be in place beginning December 1, 2006; capacity resources will be committed seasonally instead of monthly; the fixed capacity payments and the resulting removal of the determination of ICR from the equation during the transition period results in certainty over the amount of capacity load will purchase; and capacity payments are not targeted to financially distressed suppliers.

85. Load Supporters further state that the transition payments have been shown to be less than the capacity payments under the Initial Decision, and that Maine is not making appropriate comparisons. They note that under the status quo, load will be exposed to capacity payments that may approach the \$6.66/kW-month deficiency rate due to forecasted load growth. Load Supporters also state that the transition payments are well below the estimate for the cost of new entry and are premised on the assumption that over the long term, capacity payments should be the cost of new entry.

86. Load Supporters state that Maine Parties have not made arguments that justify different treatment during the transition and states that all of New England has a current capacity surplus, not just Maine. They state that Maine Parties have incorrectly relied on congestion charges in the energy market as a basis for stating that capacity payments should be reduced to \$2.00 per kilowatt-month for Maine, and for assuming that the rest of New England, which is not capacity deficient, will require that an amount of capacity be imported from Maine, sufficient to create a binding transmission constraint.

87. Lake Road states that failure to implement the Settlement Agreement in total, including the transition payments, would have a number of negative effects, including: exacerbating the need for RMR agreements; increasing the likelihood of generator bankruptcies; failing to provide the incentive for the development of infrastructure; and disrupting the functioning deregulated market in New England. Further, Lake Road states that the transition payments are critically important and will provide a badly-needed solution in the short-term. Similarly, Capacity Suppliers state that it is not an option to spend nothing on capacity during the period covered by the transition mechanism.

88. American National Power argues that Objecting Parties' claims that generators should not be paid for capacity conflicts with the Commission's reasoning directing the development of LICAP; *i.e.*, that generators in designated congestion areas be appropriately compensated for reliability. It further states that Objecting Parties' complaint that the transition payments are "money for nothing" does not acknowledge

that capacity is a legitimate product for which existing generators should be paid. American National Power also states that the Commission has distinguished the locational forward reserves market from the capacity market and recognizes that the capacity market ensures there is adequate generating capacity installed on the system. It also takes issue with the conclusions made by Maine Parties that there is a relationship between the energy market and binding transmission constraints in the capacity market. American National Power, as well as Calpine, state that without a technical demonstration of a binding capacity constraint, for which no evidence was presented, a capacity price reduction for Maine is not justified.

Commission Conclusion

89. While the Commission may not consider the transition payments ideal as a single market design element, when considered as part of the larger Settlement Agreement, we find (consistent with the second approach of *Trailblazer*) that they serve as a reasonable transitory mechanism that enables the New England region to shift to the FCM. We note that the FCM incorporates many of the proposed features of alternatives presented at oral argument. We find that the transition payments are a just and reasonable component of the overall package embodied in the Settlement Agreement because: (1) based on record evidence from the hearing, the payments fall within the reasonable range of capacity prices, and contesting parties are in no worse position under the Settlement Agreement than they would be through continued litigation; (2) in the first years, the payments are less than the cost of new entry, accurately reflecting market conditions; and (3) the payments result in just and reasonable rates for existing generators.

90. Over the course of the 10-month hearing in this proceeding, numerous parties filed alternative demand curves to the curve proposed by ISO-NE. The Commission never ruled on the justness and reasonableness of that demand curve or any of the other demand curves proposed in the hearing (although the Initial Decision did adopt ISO-NE's proposal). Nonetheless, for the purposes of addressing the Settlement Agreement as a just and reasonable package, and establishing the justness and reasonableness of the transition payments as part of that package, we can analyze the price projections under the proposed demand curves that were entered into evidence in the hearing and compare them to the transition payments. As we noted above, "[a] just and reasonable rate is not a product of any single formula, but is instead a rate within a broad ambit of various rates which may be just and reasonable."⁹⁴ We disagree with arguments that the Commission

⁹⁴ See *Belco Petroleum Corp. v. FERC*, 589 F.2d 680, 689 (D.C. Cir. 1979), citing *Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968); *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944); *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585-86, (1942).

cannot compare the transition payments to the potential rates that would have resulted from continued litigation over the LICAP mechanism. As we discuss above with regard to our standard of review, under the second *Trailblazer* approach, the Commission must find that contesting parties would be in no worse position under the settlement than if the case were litigated. Comparing the transition payments to the likely outcome of litigation is the most reasonable approach for evaluating this aspect of the Settlement Agreement.

91. The record evidence shows a range of rates that could have resulted from continued litigation. In particular, it is useful to look at the projected prices for Maine and Northeastern Massachusetts/Boston under the demand curve proposed by Maine and Vermont load representatives (one of the lower demand curves) and ISO-NE's proposed demand curve. While other demand curves were proposed at the hearing, the parameters of those curves would have produced prices that were either much higher or much lower. The Maine/Vermont and ISO-NE curves provide a narrow range of rates that provide a reasonable basis for comparison to the transition payments.

92. In direct testimony filed February 10, 2005, ISO-NE witness David LaPlante provided a series of price estimates, for a variety of scenarios, using the ISO-NE-proposed demand curve.⁹⁵ ISO-NE projected prices for each of five LICAP regions previously approved by the Commission: Southwest Connecticut (SWCT), Rest of Connecticut, Northeast Massachusetts/Boston (NEMA/Boston), Maine and the Rest of Pool. ISO-NE developed price estimates for Maine that ranged from \$2.29/kW-month in 2007 to \$4.04/kW-month in 2010; prices for NEMA/Boston were the same.⁹⁶

93. In the same exhibit, ISO-NE also projected capacity prices under a demand curve advocated by Maine and Vermont load representatives.⁹⁷ ISO-NE projected prices for Maine under that curve that ranged from \$1.91/kW-month in 2007 to \$2.53/kW-month in 2010; prices for NEMA/Boston were the same.

94. James Daly, witness for a coalition of parties, including the Attorney General of Massachusetts (AG Mass), NSTAR and The Energy Consortium, also developed a series of price projections using ISO-NE's demand curve. He first provided projections in supplemental answering testimony, filed January 28, 2005. On March 16, 2005, Mr. Daly updated his price projections to reflect an increase in the installed capacity

⁹⁵ Exhibit No. ISO-24.

⁹⁶ *Id.*

⁹⁷ The Maine Public Utilities Commission, Maine Public Advocate, Vermont Department of Public Service and the Vermont Public Service Board.

requirement as approved by the NEPOOL Participants Committee.⁹⁸ Mr. Daly's price projections for Maine ranged from \$7.63/kW-month in 2007 to \$16.16/kW-month in 2010; prices for NEMA/Boston were the same.⁹⁹ Mr. Daly argued that the net cost of ISO-NE's LICAP proposal was \$14.5 billion.¹⁰⁰ Maine Parties and Vermont argued that, using the updated installed capacity requirement, "cost[s] will rise to \$1.2 billion and \$7.3 billion for Maine and Rest of Pool, respectively, for a five-year period."¹⁰¹ In their Reply Brief, Maine Parties and Vermont argued that New England consumers could pay "as much as \$6 billion in LICAP charges" during the first three years of ISO-NE's proposal.¹⁰²

95. In Attachment 6 to the Settlement Agreement, ISO-NE witness David LaPlante provided updated capacity price projections using the demand curve approved in the Initial Decision, which is identical to the ISO-NE-proposed demand curve for which Mr. LaPlante provided projections in February 2005. Mr. LaPlante relied on updated assumptions, including the level of installed capacity requirement approved by the Commission for the 2005/2006 power year, as well as installed capacity requirement projections contained in the most recent ISO-NE Regional System Plan. Mr. LaPlante's price estimates for Maine ranged from \$4.13/kW-month in 2007 to \$7.84/kW-month in 2010; prices for NEMA/Boston were the same.¹⁰³

96. These most recent price projections, using the ISO-NE demand curve, exceed those made by Mr. LaPlante in February 2005. Therefore, it is reasonable to assume that had Mr. LaPlante also updated the price projections for the demand curve proposed by

⁹⁸ The installed capacity requirement is established annually via the NEPOOL stakeholder process, approved by a vote of the NEPOOL Participants Committee and filed with the Commission under section 205 of the FPA.

⁹⁹ Workpaper for Exhibit No. AG Mass-23

¹⁰⁰ Exhibit No. AG Mass-23 at 3.

¹⁰¹ Initial Brief of the Maine Public Utilities Commission, the Maine Public Advocate, the Vermont Department of Public Service and the Vermont Public Service Board at 32.

¹⁰² Reply Brief of the Maine Public Utilities Commission, the Maine Public Advocate, the Vermont Department of Public Service and the Vermont Public Service Board at 5.

¹⁰³ Settlement Agreement, Attachment 6.

Maine and Vermont load representatives, those projected prices would have increased in similar magnitude from the February 2005 projections.

97. This record evidence indicates that the cost of the transition payments to Maine and Massachusetts customers under the Settlement Agreement would be less than the costs of ISO-NE's proposed demand curve. In its Initial and Reply Briefs, Maine Parties¹⁰⁴ made various assertions with regard to the total costs of LICAP to Maine customers, projecting the costs at anywhere from \$734 million to \$1.2 billion through 2010. In his affidavit, Maine Parties' witness Thomas Austin submits that the transition payments as proposed by the Settlement Agreement "will cost Maine consumers about \$300 million over the transition period," which ends in 2010.¹⁰⁵ By the Maine Parties' own admission, the transition payments will impose far fewer costs on Maine customers than the price projections Maine Parties referenced in its Initial and Reply Briefs.

98. An examination of the various price projections illustrated above, using ISO-NE's proposed demand curve as well as Maine Parties' and Vermont's demand curve, shows a range of prices that could have resulted from continued litigation. The chart below shows projections for Maine and for NEMA/Boson, with the transition payments included for comparison:

Range of Projected Prices – Maine \$/kW-month				
	2007	2008	2009	2010
LaPlante - ME & VT Curve (Feb. 2005)*	1.91	1.96	1.64	2.53
LaPlante - ISO-NE Curve (Feb. 2005)	2.29	2.36	4.44	4.04
Transition Payments	3.05	3.05	3.75	4.05
LaPlante - ISO-NE Curve (March 2006)	4.13	5.14	6.39	7.84
Daly - ISO-NE Curve (March 2005)	7.63	10.21	14.26	16.16

* Not updated to reflect current assumptions.

Range of Projected Prices - NEMA/Boston \$/kW-month				
	2007	2008	2009	2010

¹⁰⁴ In briefs on the Initial Decision, Maine Parties were joined by the Vermont Department of Public Service and the Vermont Public Service Board. Both the Vermont Department of Public Service and the Vermont Public Service Board are parties to the Settlement Agreement. They filed in support of the Settlement Agreement as members of Load Supporters.

¹⁰⁵ Affidavit of Thomas D. Austin at 9, filed with Comments of the Maine Parties Contesting the Proposed Settlement, March 27, 2006.

LaPlante - ME & VT Curve (Feb. 2005)*	1.91	1.96	1.64	2.53
LaPlante – ISO-NE Curve (Feb. 2005)	2.29	2.36	4.44	4.04
Transition Payments	3.05	3.05	3.75	4.05
LaPlante – ISO-NE Curve (March 2006)	4.13	5.14	6.39	7.84
Daly – ISO-NE Curve (March 2005)	7.63	10.21	14.26	16.16

*Not updated to reflect current assumptions.

99. As the above data indicate, the record evidence shows that the transition payments fall well within the range of capacity prices projected using the demand curve proposed by ISO-NE, as well as the demand curve proposed by Maine Parties and Vermont during the hearing. The Commission notes that projected prices using the Maine and Vermont-proposed demand curve do not reflect the most recent installed capacity requirement and other updated assumptions. Since those updated assumptions produced a sharp increase in prices under the ISO-NE-proposed demand curve, it is reasonable to assume that the initial projections for the Maine and Vermont-proposed demand curve are too low and would increase in a similar manner. Thus, the transition payments fall at the very low end of this price range.

100. Taken as a whole, we conclude that this evidence establishes the justness and reasonableness of the transition payments as a component of the overall package represented by the Settlement Agreement. Not only does the evidence show that the transition payments fall within the “range of reasonableness,” as discussed above, but the evidence also leads us to conclude (consistent with the second *Trailblazer* approach) that those objecting to the settlement would not reach a more favorable result through continued litigation. The record evidence shows that even had the Commission, in continued litigation, adopted elements from other, lower demand curves proposed at hearing, the transition payments would still be comparable if not significantly lower. Taking into account the expense of continued litigation and its attendant uncertainty, we conclude that contesting parties “would be in no worse position under the terms of the settlement than if the case were litigated.”¹⁰⁶

101. Moreover, the proposed transition payments are significantly less than the estimated cost of new entry of a new peaker, a type of plant whose capital costs are lower than most, if not all, other plants. Thus, the payments are likely to be significantly lower than a cost-of-service payment for most, if not all, new generators. As noted above, the Settlement’s proposed transition payments would be set initially at \$3.05/kW-month and rise to \$4.05/kW-month for 2010. These payments are significantly lower than the

¹⁰⁶ *Trailblazer*, 87 FERC ¶ 61,110 at 61,339.

\$7.50/kW-month CONE used to begin the FCM auction, which, as discussed below, we find reasonable. Thus, the payments are well within the “range of reasonableness.”

102. Additionally, the transition payments are reasonable rates for existing generators until the FCM begins. Comments that the transition payments are unreasonable and inappropriate because they will not provide the incentive for new entry ignore that one of the Commission’s stated goals in this proceeding is to ensure that existing generators are appropriately compensated.¹⁰⁷

103. Finally, the transition payments will require a long-term commitment and will be more closely tied to the availability of a unit, both significant improvements over the existing capacity market (status quo) and the LICAP proposal as approved in the Initial Decision. First, the transition payments will be adjusted to account for unit performance during periods of high demand. Transition payments will also be adjusted by an EFORD score that is weighted according to on-peak hours, seasonal peak hours, and shortage hours (including certain periods of system-wide emergency operations or actions).¹⁰⁸ Second, the commitment period for capacity resources consists of two six-month seasonal periods (section VIII.H), as compared to the monthly period in the current capacity market. Third, during the transition period, suppliers may partially de-list or export their units (section VIII.F), an attribute the Commission previously stated would be desirable.¹⁰⁹

104. The existing capacity market does not provide these features. The current market only adjusts capacity payments for average unit availability (unforced capacity (UCAP)), while the transition period will provide an adjustment to transition payments for suppliers that do not perform that is targeted more effectively to periods of system stress. We also find that the longer commitment period for capacity resources is superior to both the status quo and to ISO-NE’s LICAP proposal. Under the current ICAP market, the commitment period is monthly; the commitment period under ISO-NE’s LICAP proposal was also monthly. During the transition period, supply resources must commit to a six-month seasonal supply of capacity. Taken together, these provisions increase the stability of the market during the transition period and add certainty and price stability for load customers. We find that these features provide enhanced reliability and customer

¹⁰⁷ April 25 Order at P 37; June 2 Order at P 40-43, 49-52; *Devon Power LLC*, 109 FERC ¶ 61,154 at P 65-67 (2004).

¹⁰⁸ Settlement Agreement, section VIII.D

¹⁰⁹ *New England Power Pool*, 100 FERC ¶ 61,287 at P 110 (2002).

protection that is superior to the existing ICAP market, which we have found to be unjust and unreasonable.

105. Maine Parties argue that the transition payments fail to account for locational differences in capacity levels, and that Maine should pay a lower transition payment because it has a surplus of capacity. However, record evidence does not support altering the transition payment for Maine based on its capacity surplus. The most recent price projections provided by Mr. LaPlante exhibit little to no variability in capacity prices across New England regions for the period covered by the transition mechanism. Furthermore, in areas where import constraints do currently exist, RMR agreements have been approved, and the costs associated with those payments are paid locally.¹¹⁰ Therefore, for this limited period, it is reasonable to not include a locational feature in the transition mechanism. The locational feature in the FCM, which we address below, appropriately addresses on a long-term basis issues regarding payments to capacity in constrained regions.

106. We also reject Maine Parties' request that we sever the issue of what level of transition payment Maine should pay. As we concluded above in our discussion of the standard of review, severance is not appropriate in this case because the Settlement Agreement provides a capacity market construct (including a transition period) that will apply throughout New England. Moreover, as Settling Parties note in their explanatory statement, the level of transition payments for the entire region were negotiated at arms length among all of the Settling Parties.¹¹¹ Severing the amount one state will pay would undoubtedly affect that negotiated amount for all parties.

107. The Commission will not reduce the level of the transition payments by 50 percent as suggested by IECG. IECG arrives at 50 percent without demonstrating why that is the appropriate level. Also, the transition payments are a fundamental component of the Settlement Agreement.

108. Finally, we address arguments with regard to the relationship between the Settlement Agreement and the currently-approved RMR agreements below.

¹¹⁰ See Explanatory Statement in Support of the Settlement Agreement at 39.

¹¹¹ *Id.*

2. FCM Design

a. Alternative Price Rule

109. The settlement provides for an alternative price rule that will reset the clearing price under certain conditions. This rule allows load to self-supply their own capacity, but removes the incentive to do so for the purpose of depressing capacity prices. The rule applies when at least some of the offers from new capacity or imports are below .75 times CONE and the Market Monitor concludes that such low offers are not consistent with long run average costs, opportunity costs, or other reasonable economic measures. Capacity submitting such bids is deemed to be “out-of-market.” When any submitted bids are deemed out-of-market, the capacity clearing price will be reset when the following conditions are met: 1) new capacity is needed, either system-wide or in an import-constrained zone; 2) there is adequate supply in the auction; and 3) at the auction clearing price, purchases from out-of-market capacity are greater than the required new entry. If these conditions are met, the clearing price for the applicable capacity zone will be set to the lower of 1) the price at which the last bid from new capacity was withdrawn, minus \$0.01 or 2) CONE.

110. Objecting Parties and IECG argue that the alternative price rule should be rejected because it maintains an artificial price support for incumbents. IECG argues that the alternative price rule interferes with competition between existing suppliers and self-supply by load serving entities. IECG argues that this rule prevents long-term contracting opportunities from effectively competing in the auction process and thus discourages long-term contracting by load serving entities. Objecting Parties argue that the sole purpose of the alternative price rule is to maintain a LICAP level of quantity and price support in the market, which reflects the unbalanced negotiating positions among the parties rather than any rational market mechanism.

111. Capacity Suppliers respond that the alternative price rule does not restrict competition, but rather, curbs the exercise of load’s monopsony power. Capacity Suppliers assert that without this rule, there is no way to restrict load from submitting artificially reduced bids for new capacity, thus driving clearing prices to zero. Capacity Suppliers’ witness Stoddard states that the rule does not interfere with the ability of load to contract bilaterally, but that it prevents loads that may control a small amount of new capacity needed to meet load growth – perhaps one or two percent – from setting the clearing price for the remaining 98 to 99 percent of capacity. Mr. Stoddard argues that when new resources that are under contract to load or otherwise indifferent to the capacity clearing price submit bids below the average cost of new entry, they may be able to set the clearing price; in these instances, the auction price would inaccurately be signaling that there is no need for new generation, while contract market prices would be signaling that there is a need for new generation. ISO-NE contends that, in instances

where new supply is required to meet the Installed Capacity Requirement, the alternative price rule prevents the price from dropping to zero. ISO-NE contends that the alternative price rule sets a methodology that directly ties the clearing price to an actual bid by new capacity or CONE and prevents price volatility, thus providing consumers with price predictability and rate stability.

112. Load Supporters assert that the alternative price rule will exclude bids that do not represent actual costs and thus is designed to ensure that prices over the long run will approximate the true cost of new entry. Load Supporters assert further that as long as a self-supplied resource bids its true costs, it can set the auction clearing price. Load Supporters argue that the rule helps to ensure that the competitive cost of new entry sets the clearing price when entry is needed, and, therefore, provides incentives for investment in new capacity.

Commission Conclusion

113. We find that the alternative price rule is a reasonable provision of the settlement because it helps to ensure that capacity prices will reflect the price needed to elicit new entry when new capacity is needed. In the absence of the alternative price rule, the price in the FCA could be depressed below the price needed to elicit entry if enough new capacity is self-supplied (through contract or ownership) by load. That is because self-supplied new capacity may not have an incentive to submit bids that reflect their true cost of new entry. New resources that are under contract to load may have no interest in compensatory auction prices because their revenues have already been determined by contract. And when loads own new resources, they may have an interest in depressing the auction price, since doing so could reduce the prices they must pay for existing capacity procured in the auction. If the owners of these two categories of resources control more new capacity than the amount of new capacity needed in a capacity zone, their low bids could artificially depress the price in the FCA.

114. To address this potential problem, it is reasonable for the Market Monitor to review offers from new capacity that appear to be unreasonably low. And if the Market Monitor determines that a low offer is not economically justified, it is reasonable to reset the clearing price to a level that would be expected in a competitive market that requires new capacity. The reset price under the alternative price rule is such a price. The alternative price rule provides two options for establishing a reset price. One option is CONE; it is reasonable to expect that the market price would normally approximate the estimated cost of new entry when new entry is needed. Under the alternative price rule, the reset price would never exceed CONE. But under the second option, the price would be less than CONE in those instances when an in-market source of new capacity has indicated through its bid that it is willing to supply capacity at a price less than CONE. In these instances, it is reasonable to reset the price at a level slightly below the last bid

from in-market new capacity that has withdrawn from the auction. Furthermore, under section IX of the Settlement Agreement, ISO-NE will provide an informational filing 90 days prior to the conduct of each FCA; that informational filing will identify any Market Monitor conclusions concerning the acceptability of bids in the FCA, allowing the Commission to review the Market Monitor's actions.

115. We disagree with Objecting Parties and IECG that the alternative price rule would maintain an artificial price support for incumbents; rather, we agree with Capacity Suppliers that the rule would ensure that new capacity, when needed, will receive a reasonable price. We also disagree with IECG that the rule would discourage long-term contracting and interfere with competition between existing suppliers and self-supply by load serving entities. Rather, we agree with Load Supporters that the rule would not preclude self-supply or bilateral contracting. The rule would not eliminate the value of self-supplying or contracting to create a hedge against the uncertainty of auction clearing prices. The rule would merely help to ensure that loads do not use self-supply to artificially suppress the auction's clearing price below the price needed to elicit new entry when new entry is needed.

b. Locational Feature

116. In addition to its concerns regarding the lack of a locational element in the transition period, Maine Parties also express concerns regarding the locational feature of the FCM. As noted above, under the locational feature included in the Settlement Agreement, ISO-NE will determine any separate capacity zones prior to each auction based on its identification of transmission constraints that may bind. This compares to the LICAP proposal, under which the capacity zones would be permanently established in the tariff and would not change prior to each auction absent a tariff change.

117. Specifically, Maine Parties argue that the determination by ISO-NE of whether binding constraints exist (which will then result in separate import constrained zones) is inferior to allowing actual price separation to occur as part of the auction process. In particular, Maine Parties argue that the administrative determination will be made with incomplete information, and could be influenced by entities with greater resources. Maine Parties also argue that this process could result in the region purchasing capacity that is not deliverable to the import-constrained region, leading to higher prices (since more capacity is being paid than can be delivered). Furthermore, Maine Parties contend that a pre-determined conclusion that a constraint will or will not bind is unduly rigid and suppresses market forces that would ordinarily determine the locational value of capacity on their own. Maine Parties conclude that "[t]he failure to model import constraints in

the auction runs counter to the Commission's core interest of ensuring price separation to value capacity properly in import-constrained zones."¹¹²

118. In reply, Load Supporters argue that the Settlement Agreement properly determines the need for separate capacity zones before the auction, and that much of the agreement hinges on this feature. Load Supporters contend that five separate auctions would be inefficient where objective criteria apparent before the auction show no need for the separate zones. Additionally, Load Supporters assert that establishing ISO-NE's determination and criteria in advance allows load to take action to minimize the impact of separate, smaller capacity zones. Load Supporters state that changing this aspect of the settlement could disturb the delicate balance reached in the package as a whole. Furthermore, in response to Maine Parties' suggestion that the locational element could result in the purchase of capacity that is not deliverable, Load Supporters state that the Settlement Agreement includes explicit provisions to maintain local resource adequacy and reliability in a more precise manner than would Maine Parties' suggested modification.

119. ISO-NE, in its reply, explains that the locational mechanism in the Settlement Agreement was a compromise crafted to bring together parties who favored either a locational capacity market or a regional capacity market. ISO-NE states that the need for a locational capacity market is critical to provide an incentive for the right mix of generation in the right locations, and the approach in the settlement was negotiated to ensure that there would be a locational element in the market when and where required. Furthermore, ISO-NE notes that export constraints will be modeled through the auction, making Maine Parties' concern only directed at import constraints. According to ISO-NE, while always including a separate zone in the auction might be a better approach in theory, the approach in the Settlement Agreement will achieve the same result by identifying the need for new capacity or transmission inside an import-constrained zone and then properly pricing it. Additionally, ISO-NE and Load Supporters argue that the zonal determinations will not be subject to undue influence, since the ISO will be required under the settlement to make an informational filing with the Commission, which parties can then challenge.

120. Finally, ISO-NE contends that Maine Parties are incorrect that more capacity may be purchased than can be imported into the constrained zone because under the settlement's "before-the-fact" determination process, the amount of existing capacity and capacity that is committed to be constructed is compared to the capacity needed within the zone (given assumed transmission) and if there is sufficient capacity, no separate zone

¹¹² Comments of Maine Parties at 17.

is modeled. Since the calculation is done each year, changed circumstances are taken into account, and only the retirement of a unit during the auction (without a purchase of replacement capacity) could result in an incorrect calculation. ISO-NE states this scenario is unlikely and is addressed by the retirement rules and market mitigation thresholds under the ISO-NE tariff.

121. National Grid, also in reply, argues that the Settlement Agreement resolves locational concerns more effectively than the LICAP mechanism because it ties the creation of zones directly to the actual current location of load pockets, and is performed on an annual basis to reflect current system conditions, instead of creating rigid and inflexible zones that are changed only with difficulty. Furthermore, it contends that Maine Parties' assertion that ISO-NE will determine the zones by "administrative fiat" is without merit, because ISO-NE will use an objective technical test to identify the zones, and will use local sourcing requirements (*i.e.*, the amount of capacity that must be obtained within each zone) based on a well-defined reliability analysis and a methodology for determining transfer limits between regions that the parties have previously uniformly supported.¹¹³ Additionally, National Grid contends that Maine Parties' proposal to alter the locational feature will present market power concerns, since pre-established zones (such as those in the LICAP proposal) present more of an opportunity to manipulate participation in the auction to force the pre-defined transmission constraints to bind and create price separation, while determining the zones before the auction based on objective factors analyzing the actual state of the system will minimize such opportunities. Finally, National Grid argues that altering this feature could cause a collapse of the settlement.

Commission Conclusion

122. We will accept the locational feature of the FCM, which (as we explain here) contributes to the overall justness and reasonableness of the Settlement Agreement as a package and satisfies the directive in prior Commission orders that the capacity market take into account location. Transmission constraints in New England can restrict the ability to deliver energy from some locations to others, and a market design for capacity should reflect transmission constraints to send correct price signals for investment. We believe that the settlement provides for a means to recognize transmission constraints that is, on balance, reasonable in light of competing considerations.

123. Under the settlement, separate capacity zones would be established for each yearly FCA in those instances when the ISO determines in advance that transmission constraints

¹¹³ Reply Comments of National Grid at 4-5.

are likely to bind. The Maine Parties argue that determining zones in advance, as proposed in the settlement, is inferior to allowing price separation to occur as part of the auction process. In principle, there may be advantages to the Maine Parties' approach, but the settlement's approach will reduce the incentive to exercise market power in the capacity market. We agree with National Grid that if auction results were used to force local capacity zones/local auctions, as Maine Parties' propose, sellers of capacity would have the incentive to withhold capacity to create price separation and separate capacity zones where they are not necessary.¹¹⁴ These constraints would bind only because of the exercise of market power, and not because of actual physical limitations arising from competitive market conditions. The locational feature of the Settlement Agreement, in contrast, will be based on an objective analysis of actual transmission system constraints.

124. Therefore, we accept the locational feature of the FCM. We note that the settlement provides for the ISO's Market Monitor to post a report analyzing the operations and effectiveness of the FCM no later than 180 days after the second FCA is conducted, as well as annually in its annual markets report. In these reports, the Market Monitor should include an evaluation of the locational element.

c. Level of CONE/"Collar"

125. Under the Settlement Agreement, the beginning price for each FCA will be twice CONE (or \$15.00/kW-month), with the value of CONE for the initial FCA set at \$7.50/kW-month. In subsequent auctions, CONE will be based on preceding values of CONE and preceding auction clearing prices.

126. Objecting Parties argue that the initial CONE of \$7.50/kW-month is excessive and should be set below \$7.00/kW-month. Objecting Parties assert that the combination of an excessive CONE and the price floor established via the collar mechanism will result in load paying excessive capacity charges even in a surplus situation. Objecting Parties note that capacity payments will be netted against reserves payments from the locational forward reserves market. Reserves payments are capped at \$14/kW-month. Objecting parties argue that, given that the beginning price for capacity will be \$15.00/kW-month (two times CONE), there is the possibility that reserves will clear at a lower price than capacity, meaning qualified locational forward reserves markets resources could have to take a financial loss to provide locational reserves.

127. Maine Parties argue that setting the initial CONE at \$7.50/kW-month is too high, particularly for Maine, which has a surplus of generation and limited export capability. Maine Parties assert that the CONE does not reflect the lower cost of new entry in Maine

¹¹⁴ See Reply Comments of National Grid at 7.

relative to other locations in New England. Maine Parties cite LICAP testimony from ISO-NE witness Reed, who determined that several inputs into the totaled installed costs of generation were higher in Southwest Connecticut than in Maine.¹¹⁵ Maine Parties argue that, in the LICAP proceeding, ISO-NE proposed an estimated benchmark cost of capacity for Maine that was \$1.00/kW-month lower than Southwest Connecticut. Thus, Maine Parties assert that a just and reasonable initial CONE for Maine would be \$6.50/kW-month. Maine Parties also argue that the collar mechanism will keep prices artificially high.

128. Capacity Suppliers and ISO-NE argue that neither Objecting Parties nor Maine Parties provide analyses or cite record evidence to support an alternative value for the initial CONE. Capacity Suppliers submit that the primary purpose of CONE is to indicate the auction’s beginning price; actual clearing prices will reflect the market for capacity not CONE. Capacity Suppliers and ISO-NE contrast the proposed \$7.50/kW-month level of initial CONE with the estimated cost of new capacity derived by ISO-NE witness Reed during the LICAP proceeding—\$7.27 in Maine, \$7.70 in Rest of Pool, and \$8.16 in NEMA/Boston. Capacity Suppliers assert that this record evidence substantiates the \$7.50 CONE estimate, which is for the 2010/11 power year.

129. Load Supporters submit that the settling parties made great efforts to balance the risks between resource suppliers and load so that the long-term CONE could assure a steady stream of new competitors willing to offer capacity at the lowest reasonable cost. Load Supporters assert that altering the initial value for CONE would disrupt the settlement’s delicate equilibrium, and may precipitate its collapse.

Commission Conclusion

130. The Commission will not modify the initial value of CONE proposed in the Settlement Agreement. We find that the \$7.50/kW-month CONE is a reasonable estimate of the cost of new entry and basis for the beginning price in the FCM auctions, and we

¹¹⁵ ISO-NE witness John J. Reed derived the following values for the estimated costs of capacity for a benchmark peaking unit (*see* Exhibit No. ISO-3 in Docket No. ER03-563-030):

LICAP Region	NEMA/Boston	SWCT	Rest of Connecticut	Maine	Rest of Pool
\$/Kw-year	\$97.87	\$99.16	\$96.52	\$87.22	\$92.34
\$/kW-month	\$8.16	\$8.26	\$8.04	\$7.27	\$7.70

believe it is supported by substantial evidence in the record. For example, the \$7.50/kW-month CONE is at the lower part of the range of the estimated benchmark costs of capacity produced by ISO witness Reed at the hearing in this proceeding. Further, Capacity Suppliers' witness offers substantial evidence that, after adjusting Mr. Reed's estimates for inflation over four years to 2010, the \$7.50/kW-month level of CONE would be lower than all of Mr. Reed's estimates.¹¹⁶ Additionally, the \$7.50/kW-month figure is not a substantial increase from the existing \$6.66/kW-month deficiency charge currently in place in the ICAP market and approved by the Commission in 2002, given inflation and increases in the cost of capacity.¹¹⁷ Neither Maine Parties nor the Objecting Parties offer any evidence as to why their suggested modifications provide a more reasonable estimate of the cost of new entry.

131. With regard to the issue raised by Objecting Parties' regarding the impact of the FCM on the locational forward reserve market, the Commission notes that, while \$15.00/kW-month is the initial bid price (representing two times CONE), the prices in the descending clock auction will descend until the market clears. Subsequent values of CONE will be "mathematically calculated using the clearing prices of previous auctions"¹¹⁸ and thus the beginning prices in subsequent FCAs will reflect the prices needed to elicit supplies to serve projected demand. Additionally, prices paid to capacity suppliers will be reduced via the peak energy rent deduction and availability metric. We expect that these provisions will appropriately address Objecting Parties' concerns. We note that in the locational forward reserves market proceeding,¹¹⁹ ISO-NE indicated that the locational forward reserves markets settlement rules would accommodate the design of any successor capacity market in this docket. We expect ISO-NE to carefully observe prices in the locational forward reserves markets and FCM markets and to file to correct any problems of overlap.

132. We will not grant Maine Parties' request to reduce CONE for Maine alone. First, we note that CONE is only a starting point for the auction, and changing CONE for Maine alone will not change the actual cost of new entry in Maine. Since it is simply a beginning point for the auction, CONE will not necessarily establish the market clearing price in all FCAs. Moreover, we find that a single value for CONE is just and

¹¹⁶ Supplemental Affidavit of Robert B. Stoddard at 3, Filed with Reply Comments of Capacity Suppliers.

¹¹⁷ See *New England Power Pool and ISO New England, Inc.*, 100 FERC ¶ 61,287 at 62,277-78 (2002).

¹¹⁸ Explanatory Statement to Settlement Agreement at 26.

¹¹⁹ *ISO New England, Inc.*, 115 FERC 61,175 (2006).

reasonable, since the FCM is a region-wide construct with a locational element when transmission system conditions warrant. Additionally, the \$7.50/kW-month CONE differs only slightly from the \$7.27/kW-month estimated cost of capacity for a benchmark peaking unit entered into evidence by ISO-NE witness Reed in the hearing below, even without updating Mr. Reed's figure to reflect inflation and increased fuel costs.¹²⁰ Furthermore, Maine Parties do not address how different CONEs for Maine and for the rest of New England would operate in practice with respect to a single clearing auction.

d. Definition of "New Capacity"

133. Under the Settlement Agreement suppliers that undertake new investment in existing resources (*i.e.*, capacity that is considered to be existing capacity) to increase output may have capacity reclassified as new capacity. A previously existing resource shall be considered new capacity if the supplier undertakes new investment such that: (1) resource output is increased by the greater of 40 megawatts or 20 percent of Summer Seasonal Claimed Capability¹²¹; (2) the resource is repowered at a rate equal to or greater than \$200 (plus appropriate cost escalation) per net kilowatt installed project cost; (3) the resource is upgraded to comply with environmental regulations or permits at a rate equal to or greater than \$100 (plus appropriate cost escalation) per net kilowatt installed project cost. The Settlement Agreement also contains provisions to classify incremental capacity additions as new capacity.

134. Objecting Parties argue that because existing suppliers have both the incentive and ability to withhold capacity, it is important that only "new" resources be allowed to set the auction clearing price. While Objecting Parties acknowledge that there is probably some reasonable uprate threshold for declaring existing capacity "new," they argue that the greater of 20 percent or 40 megawatt threshold included in the settlement is too low. Objecting Parties argue that requiring 100 percent or more is more appropriate; with 100 percent a resource owner would need to add a megawatt of truly new capacity for every megawatt of existing capacity that would be withdrawn from the market and reclassified as "new."

¹²⁰ See Exhibit No. ISO-3

¹²¹ The Seasonal Claimed Capability rating of a generating unit is the maximum dependable load carrying ability, in megawatts the unit and represent the MW value of the resource used in the capacity market. All resources within New England must perform capability audits. Capabilities are calculated for winter and summer.

135. Objecting Parties also argue that the ability of all imports to qualify as new capacity is an additional flaw. Objecting Parties contend that allowing imports to set capacity prices above the CONE creates an unnecessary opening for the exercise of market power, and increases the probability that existing resources will set the clearing price. Objecting Parties argue that enabling existing resources outside the pool to set high clearing prices creates a gaming opportunity for existing resource owners to export and then import a corresponding amount as new for the purpose of influencing prices. All imports, they argue, other than from new transmission or new generation construction, should be treated as “existing” resources in the FCA.

136. Load Supporters, in their reply comments, argue that the 20 percent/40 megawatt threshold promotes competition. Load Supporters and Capacity Suppliers assert that repowering brownfield sites may be completed more quickly and at a lower cost than new construction because the site is already permitted, licensed, and developed for generation use. Load Supporters argue that the FCM is reasonably designed to enable existing resources to improve their sites quickly, to provide substantial value at least-cost to load, and to improve capacity resource reliability and adequacy where needed. Capacity Suppliers state that settling parties agreed that sending market signals to existing units to incur upgrade costs, when economic and efficient, is appropriate. ISO-NE contends that the Settlement Agreement is premised on the notion that an uprate of the sizes identified would require “extremely significant” investment. Load Supporters add that upgrades of at least 20 percent are unlikely to be possible without some period of de-listing. ISO-NE submits that new investment in existing units is precisely the new entry the FCM hopes to attract. ISO-NE states that an uprate of that size would further require new environmental permits, new interconnection and major additions to or replacements of existing components. ISO-NE submits that market rules will assure that capacity from these re-powerings will be unable to exercise market power. NRG argues that investors will not fund output increases without finding that the capacity market will support that investment.

137. In reply, Capacity Suppliers also argues that the ability of imports to set the clearing price was designed to increase competition between proposed new generation and imports and should serve to reduce the FCM clearing price. ISO-NE argues that if external generation is ineligible to set the price, it will sell its output elsewhere.

Commission Conclusion

138. The Commission will not direct the settling parties to reconsider the threshold used to reclassify existing capacity as new capacity. The Commission finds that the threshold provision to which the Objecting Parties refer provides incentives to attract more supply to New England because it will encourage existing suppliers to expand their facilities. We further find that the level of the 20 percent/40 megawatt threshold is

sufficient to provide incentives for significant additions to capacity levels, while preventing existing capacity from being reclassified as new capacity by means of minor additions. We note that both Load Supporters and Capacity Suppliers argue that investment in existing capacity may be more cost efficient than new construction as well as quicker to come online. Results of recent ISO-NE analyses, presented in the 2005 Regional System Plan, show that “New England will likely face an increased risk of operating with less capacity than needed by 2008.”¹²² The 2005 Regional System Plan further states that results indicate that the region “will not have sufficient capacity to meet the IC Requirement in the 2008 to 2010 timeframe, depending on load growth, weather conditions, generator performance and attrition, and the conditions in specific load pockets, such as Connecticut.” Given these projections and that new generation requires two to four years to be built, increased output from existing resources could provide important reliability protection. The Commission thus accepts the 20 percent/40 megawatt threshold agreed to by settling parties as an appropriate means for attracting additional capacity.

139. We note that the Objecting Parties do not oppose the provision generally; rather they propose an alternative level (100 percent) as they believe the 20 percent/40 megawatt level is too low. The Commission finds that a 100 percent threshold level is too high. One of the benefits of the proposed threshold is that it encourages suppliers to add new capacity quickly, far sooner than the time they would need to build new units. We do not believe that a 100 percent threshold provides the same benefit. Moreover, the Settling Parties negotiated and agreed on a threshold level as part of the overall Settlement Agreement, which was approved by a significant majority of the NEPOOL Participants Committee. Given that we find that this provision creates appropriate incentives to bring on potentially cheaper capacity more rapidly, we will accept the 20 percent/40 megawatt provision.

140. New import capacity is capacity that a party without a multi-year contract wishes to bid into the FCA; it will be required to meet the financial assurance as well as physical backing requirements described above. This provision is intended to increase the level of eligible capacity in instances where new capacity is required to meet reliability criteria. Allowing additional imports to bid into the FCM, provided eligibility requirements are met, is reasonable as this increases the supply of capacity available in the auction.

¹²² ISO New England, Regional System Plan 2005 at ES-9.

e. **Capacity Transfer Rights**

141. NSTAR states that the settlement continues a discriminatory allocation of Capacity Transfer Rights (CTR) to municipal entities at the expense of investor-owned utilities. NSTAR states that Pool Planned Units (PPUs) should not be singled out in this manner because they do not support the transmission system at any greater level than other customers. NSTAR states that without this CTR allocation, owners of PPUs will continue to receive their entitlements in the PPUs. NSTAR states that if the Commission allocates CTRs to the municipals, then the investor-owned utilities should be allocated CTRs based on their interest in PPUs at the time they were divested.

142. Reading supports the settlement and states that the right to self-supply by load serving entities is a critical component for vertically integrated utilities such as itself. Reading states that its investment in PPUs and associated transmission upgrades was made prior to the creation of the ISO and were based on the PPUs being fully integrated with load throughout the region. Referencing prior Commission orders that recognize the nature of the pre-existing contracts, Reading states that these life-of-unit contracts are specific entitlements by which they meet their energy and capacity obligations. Reading also states that the Presiding Judge, in the Initial Decision, ruled that the PPU Entitlement holders be allocated CTRs.¹²³

143. MMWEC and Reading submit that were the Commission to modify the Settlement as requested by NSTAR, they would oppose the Settlement. They state that the PPU/CTR provisions contained in the Settlement counterbalance other financial burdens placed on consumers.

Commission Conclusion

144. The Commission will not alter the contractual arrangements relating to the PPUs. Municipal utilities have invested in these assets under a prior standard providing that their output would be fully available to the utilities. The municipals continue to be the original holders of these life-of-units contracts that are an important part of their ability to meet energy needs and to self supply capacity to meet pool obligations from their own resources. The Presiding Judge found in the Initial Decision that this differentiated the municipal entities that remain vertically integrated from utilities such as NSTAR who have divested themselves of these entitlements; and, therefore, found that subsequent holders of these entitlements no longer have the same obligations as the original owners.¹²⁴ We agree with this finding and also find that the proposed Settlement

¹²³ See Initial Decision at P 703.

¹²⁴ Initial Decision at P 704.

Agreement continues to preserve these arrangements consistent with past Commission policy. In its June 28, 2000 Order addressing the proposals to implement a congestion management and multi-settlement system in New England, the Commission recognized these entitlements and awarded Auction Revenue Rights to the entitlement holders to allow them to import the output into the congested NEMA zone for the life of their contracts, noting the circumstances of these pre-existing contracts.¹²⁵ We find that NSTAR has provided no basis that CTRs should be awarded to entities that no longer own these contracts and our June 2000 Order does not contemplate continuation of these rights for contracts that are no longer held.

f. Market Monitor Review of Exports

145. According to LIPA, under section III.D.4 of the Settlement Agreement, the Market Monitor will automatically review export bids by de-listed capacity. LIPA objects to this automatic review unless there is an indication of an exercise of market power. LIPA states that the “automatic review provision...assumes...an attempt to exercise market power” and that this provision is a discriminatory and unjustified disruption of market transactions.¹²⁶ LIPA states that the market rules in this regard should specify criteria that the Market Monitor will apply. LIPA also states that the settlement does not specify the types of actions that the Market Monitor may take regarding export transactions and urges the Commission to modify the settlement to require that conduct and impact criteria be used to trigger action by the Market Monitor and that these criteria be included in the market rules.

146. ISO-NE replies that LIPA has not set forth credible reasons why certain de-listed capacity is entitled to an exemption from independent Market Monitor review. Load Supporters reply that contrary to LIPA’s assertion, the Market Monitor only reviews export bids greater than 0.8 CONE and that this provision provides a reasonable threshold for identifying bids that may warrant review while avoiding an undue burden on market participants.

Commission Conclusion

147. We will not modify the settlement’s provisions regarding Market Monitor review of export bids. An export bid has a similar effect on the capacity market as a bid to de-list, since both bids remove capacity from New England loads. While a bid to export all

¹²⁵ See *ISO New England, Inc.*, 91 FERC ¶ 61,311 at 62,073 (2000).

¹²⁶ Comments of LIPA at 8.

of a suppliers' capacity may not be the exercise of market power (since the seller would not benefit from any increases in prices within New England), a bid to export capacity in tandem with a bid to sell capacity in New England could represent an exercise of market power. Therefore, we agree with ISO-NE that export bids should be reviewed by the Market Monitor in the same manner as de-list bids, to guard against the potential exercise of market power when an export bid is coupled with a bid in the capacity market. LIPA has not provided evidence as to why export transactions should be exempt from review by the Market Monitor and has not provided details as to how the settlement should be modified. Moreover, we will not require the alteration of the settlement in order to accommodate LIPA's concerns over market rules which have yet to be written, vetted through the stakeholder process, or filed with the Commission. The settlement does not represent the detailed market rules which will be filed later. As such, LIPA's concerns regarding the market rules are premature.

g. Assessment of Tie Line Capability

148. LIPA raises concerns regarding the ability of ISO-NE under the Settlement Agreement to impose limitations on capacity import and export transactions by assessing the capabilities of ties to adjoining control areas. Specifically, LIPA is concerned about tie benefits on its two interconnections with New England (the Cross Sound Cable and the 1385 cable) and argues that the FCM market rules should clarify tie benefits since LIPA's ties connect through a constrained region. LIPA requests that the Commission clarify that nothing in this settlement will set a precedent for the appropriate means by which ISO-NE will determine the tie benefits.

Commission Conclusion

149. LIPA has not provided evidence that this issue needs to be addressed here, and has not specified any specific provisions of the Settlement Agreement that give rise to its concerns. To the extent that this issue deals with market rules that have not been submitted to the Commission, it is premature to address this issue at this time.

h. Price Setting Mechanism

150. As discussed above, the FCM will not utilize a downward sloping demand curve like LICAP would have, instead employing a descending clock auction. PSEG states that, without a downward sloping demand curve, FCM will only procure that quantity of capacity sufficient to meet ISO-NE's projected installed capacity requirement. As a result, PSEG argues that the FCM will produce price volatility as well as volatility of reliability. PSEG asserts that only new units will be able to set prices significantly greater than zero and that such bids will be accepted only when shortage conditions are already present or imminent. PSEG contends that the FCM will produce capacity prices

at or near zero until shortages occur. When shortages occur, argues PSEG, prices will reach the CONE, perhaps for a single year, and then drop to zero again. PSEG appears to contend that, without a downward sloping demand curve as well as a mechanism to procure more than 100 percent of the installed capacity requirement, the FCM will not encourage the development and financing of new capacity resources. PSEG maintains that a demand curve mechanism like the LICAP model or PJM's Reliability Pricing Model (RPM) would provide the long-term price stability lacking in the Settlement Agreement.

Commission Conclusion

151. In this order we find that the Settlement Agreement is just and reasonable as a package and, therefore, we are not proposing modifications that would mandate the development of a demand curve in addition to the FCM. As the Commission recently stated in its order on PJM's proposed RPM mechanism, "there is not a single just and reasonable method for satisfying capacity obligations."¹²⁷ PSEG does not oppose the Settlement Agreement, and does not explain how the downward sloping demand curve should be integrated into the FCM.

i. Availability Metric/Compatibility With Adjoining Markets

152. As described above, the Settlement Agreement includes an availability metric that will reduce capacity payments to account for availability during designated periods of system stress (*i.e.*, Shortage Events). PSEG states that ISO-NE and capacity purchasers have argued that performance incentives assure that capacity resources are providing reliability benefits when the system needs them most. PSEG argues, however, that sufficient incentives already exist for generators to come online or to provide reserves during periods of peak demand. PSEG argues that generators will add a risk premium to capacity offers (to protect against outages) in response to the shortage events approach to measuring availability. PSEG argues that neither ISO-NE nor other proponents have demonstrated that the resulting higher costs to consumers justify enhanced system reliability.

153. PSEG and LIPA argue that the shortage events proposal redefines the nature of the capacity product. Both NYISO and PJM currently measure generator availability based on EFORD. PSEG and LIPA assert that adoption of the shortage events proposal would implement a capacity product that differs greatly from neighboring markets, and would

¹²⁷ *PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 at P 103 (2006).

create an undesirable seam between New York and New England. LIPA notes that during the transition, the value of capacity will be adjusted by the weighted EFORD availability metric which is not done in NYISO and PJM. LIPA asserts that the Initial Decision found that availability of generation in New England should continue to be applied and measured using the EFORD approach, based on Commission precedent and conformity with the NYISO and PJM. LIPA argues that the Commission should require ISO-NE to demonstrate that the use of this new standard of availability will be consistent with the EFORD measure. LIPA adds that modifications to the current capacity product should be left for broader regional discussions. PSEG asserts that PJM's RPM approach to resource adequacy provides a superior alternative to the FCM design, and the Settlement Agreement should not serve as a model for markets outside of New England. LIPA urges the Commission to ensure that the market rules, when filed, are compatible with neighboring capacity markets and also urges the Commission to require that ISO-NE file an implementation report that details how external transactions will be integrated with FCM.

154. NYISO, in reply, requests that the Commission not take action that would require significant changes to the New York ICAP market but give full consideration to any unintended consequences of FCM on trade between the markets, and require an explanation and analysis of compatibility as the settlement is more fully developed.

155. In its answer, ISO-NE asserts that the interim EFORD proposal (for use during the transition period) and the FCM shortage events proposal are designed to ensure tradability across regions. ISO-NE states that during the interim period and thereafter, it will continue to calculate EFORD for all generating units in New England and thus trade between New York and New England will not be impeded. ISO-NE states that although capacity would be bought and sold in a way that is slightly different from the method used in New York, ISO-NE proposes to translate between these two different capacity products.

156. Load Supporters submit that the shortage event proposal provides more effective incentives for generators to supply resources to be responsive during stress periods than EFORD. Load Supporters also support the availability provisions that would expel underperforming units from the capacity markets, stating that the units will be replaced by better-performing resources. Load Supporters argue that the Settlement Agreement's availability metric does not create an insurmountable trade "seam." Load Supporters contend that the shortage event proposal satisfies the reliability and resource adequacy needs for New England load and that the EFORD metric that LIPA advocates does not. Capacity Suppliers indicate that it accepts the "shortage events" methodology as part of the settlement package.

Commission Conclusion

157. ISO-NE's LICAP proposal contained an approach to measuring a generator's availability that differs from the conventional EFORD method. EFORD calculates "average availability over all hours of the year."¹²⁸ A generator's EFORD score is reduced only for forced outages.¹²⁹ In the LICAP proceeding, ISO-NE's proposed method for measuring a generator's availability was based on "shortage hours," which were hours in which ISO-NE was short of operating reserves, rather than EFORD. There, ISO-NE argued, EFORD would treat a generator outage during a cool spring afternoon the same as an outage during the hottest day of the summer, and would send a price signal that power is worth the same whether the level of demand is very high or very low.

158. Many of the parties representing load supported ISO-NE's shortage hours proposal. This element of the LICAP proposal was contested vigorously in the LICAP hearing and subsequent briefs. The Initial Decision stated that while ISO-NE had successfully shown that EFORD was "not perfect and that the Shortage Hours approach may provide a better overall availability metric," ISO-NE had not successfully shown that the EFORD approach is so imperfect as to be unjust and unreasonable.¹³⁰ In the Initial Decision, the Presiding Judge concurred with the Capacity Suppliers and other suppliers that it was not an opportune time to replace EFORD with a new metric. However, the Presiding Judge stated that the revised availability metric held promise and emphasized that "availability should continue to be defined using the EFORD metric *at this time*."¹³¹ The Commission also provided an opportunity for ISO-NE to further develop its shortage hours approach, directing ISO-NE to file that proposal in a compliance filing.¹³²

159. The Commission will accept the shortage events method proposed in the Settlement Agreement. We find that it is a more appropriate measure of availability, and provides an appropriate incentive for generators to provide reliable service during the periods of system stress, which preserves reliable service. The evidence offered in the hearing and in post-hearing briefs suggests that the current EFORD measurement (as contrasted to the modified measurement proposed for the transition period) may not

¹²⁸ Brief on Exceptions of ISO-NE at 9.

¹²⁹ *Id.*

¹³⁰ Initial Decision at P 546.

¹³¹ *Id.* at P 548 (emphasis in the original).

¹³² *Devon Power LLC*, 113 FERC ¶ 61,075 (2005).

appropriately measure the availability of capacity resources during times when they are most needed, and therefore deserving of full compensation for the service they provide. The Commission believes that it is reasonable for market participants to elect to measure availability in a manner that emphasizes hours of high demand. Moreover, the Commission believes that achieving resolution in the settlement discussions would have been very difficult without a revised measurement tool for availability; modifying the shortage event mechanism at the request of PSEG and LIPA, neither of which formally oppose the Settlement Agreement, would be unreasonable.

160. With regard to transactions with neighboring markets, ISO-NE states that it will continue to calculate EFORD for all generating units in New England during the transition period and thereafter. We find that this will adequately address LIPA's and PSEG's concerns and will continue to allow exports and imports of capacity between ISO-NE and neighboring markets.

j. Relationship to RMR Agreements

161. Objecting Parties argue that the Settlement Agreement is defective in that 1) it does not immediately terminate existing RMR agreements and 2) does not prohibit the filing of new RMR agreements for several years. Objecting Parties argue that the Settlement Agreement should provide for a re-determination of RMR eligibility in light of the transition payments. Objecting Parties assert that the transition payments are so large that many, if not all, entities now charging RMR rates would be ineligible for those rates.

162. Objecting Parties submit that the locational forward reserves market, which is to be implemented in fall 2006, is devoted to compensating seldom-run resources that are needed for contingency support, particularly in congested areas.¹³³ Objecting Parties believe that the locational forward reserves markets and other market revisions should render an installed capacity market superfluous. Thus, Objecting Parties argue, all RMR contracts that have been granted since the April 25 Order should terminate on the first day of the locational forward reserves market. Objecting Parties argue that the Commission should modify the transitional provisions of the Settlement Agreement to provide for the termination of all Commission-approved RMR contracts. Objecting Parties argue that, after termination of the RMR agreements, holders would be permitted

¹³³ The locational forward reserves market (LFRM), was proposed to the Commission in a filing on February 6, 2006 (Docket No. ER06-613-000) and approved in a Commission order issued May 12, 2006. *ISO New England, Inc.*, 115 FERC 61,175 (2006).

to reapply for new agreements only upon a showing that, even with interim payments, their receipts would be less than going-forward costs and make clear that any future RMRs would be limited to going-forward costs.

163. PSEG argues that the FCM design will not reduce the need for RMR contracts and may encourage the use of RMR contracts. PSEG argues that existing generation that is unable to set clearing prices may have to retire; where that generation is required for reliability, the only alternative would be to seek an RMR contract. PSEG also argues that the shortage event proposal will impose greater risks on older units that may be needed to maintain reliability. PSEG contends that, as such, the proposed FCM design encourages the retirement of these older units, and RMR agreements will be necessary to retain them. PSEG believes that PJM's RPM proposal provides a superior alternative and should serve as the model for future capacity markets.

164. Milford Power argues that Objecting Parties' arguments regarding RMRs contain several impermissible collateral attacks on prior Commission orders. Milford Power and ISO-NE argue that, with regard to termination, the Commission has ruled in several proceedings that RMR agreements should terminate only upon the implementation of a locational capacity mechanism. ISO-NE argues that a party may file a section 206 complaint to terminate any RMR agreement based on changed circumstances (*e.g.* demonstration that there is no longer a financial need). ISO-NE also notes that the Settlement Agreement states that nothing therein "prejudices the rights of any party to challenge, seek to terminate or support an RMR agreement on any other ground or restrict any party's rights to seek, agree to, or oppose any RMR modifications."¹³⁴ Concerning limiting RMRs to going forward costs, Milford Power argues that the Commission has repeatedly ruled that an eligible RMR unit is entitled to recover its full cost of service.

165. ISO-NE submits that locational forward reserves market revenues only go to approximately 2,000 to 3,000 megawatts of generation out of a total of 32,000 megawatts of generation. ISO-NE states that while the locational forward reserves markets is an important market enhancement, it is only a partial remedy for revenues that need to be restored through a capacity market. Berkshire Power states that the Settlement Agreement recognizes that the fixed transition payments will not be adequate to compensate ICAP resources operating under an RMR agreement. CMEEC and MMWEC disagree and argue that the Commission should reject any such interpretation. CMEEC and MMWEC argue that the Settlement Agreement does not recognize anything with respect to the adequacy of transition payment revenues to compensate any or all

¹³⁴ Settlement Agreement at VIII.F.

RMR resources, or that the termination of existing RMR agreements cannot be sought for any legitimate reason.

Commission Conclusion

166. The Commission will not require the termination of existing RMR agreements prior to the full implementation of the FCM and will not require RMR holders to reapply for new RMR agreements. The Commission has consistently accepted RMR agreements for a term that expires upon implementation of a locational capacity mechanism.¹³⁵ FCM will not result in the purchase of capacity until the beginning of the first commitment period in June 2010. Therefore, the June 2010 termination date of RMR agreements is consistent with the express terms of the RMR agreements and the Commission's intent that those contracts terminate when a capacity market mechanism is fully implemented.¹³⁶ The Commission notes that the transition payments will be netted against RMR revenues, which will protect against over-recovery. Furthermore, the Settlement Agreement explicitly states that participants do not waive their rights to challenge the need for RMR contracts, given changes in a generator's compensation or changes to system infrastructure.¹³⁷

167. Objecting Parties' arguments regarding the forward reserves market are misplaced in this proceeding, and accordingly, we reject them. This proceeding focuses solely on the capacity market, and the Commission has already ruled on issues related to

¹³⁵ See, e.g., *Devon Power LLC*, 106 FERC ¶ 61,264 (2004) (*Devon Power*); *Mirant Kendall, LLC and Mirant Americas Energy Marketing, L.P.*, 109 FERC ¶ 61,227 (2004), *order on reh'g*, 110 FERC ¶ 61,272 (2005); *PSEG Power Connecticut, LLC*, 110 FERC ¶ 61,020, *order on reh'g*, 111 FERC ¶ 61,441, *order on reh'g*, 111 FERC ¶ 63,023 (2005); *Milford Power Company*, 110 FERC ¶ 61,299, *order on reh'g*, 112 FERC ¶ 61,154 (2005); *Bridgeport Energy, LLC*, 112 FERC ¶ 61,077, *order on reh'g*, 113 FERC ¶ 61,311 (2005), *reh'g rejected*, 114 FERC ¶ 61,265 (2006); *Berkshire Power Company, LLC*, 112 FERC ¶ 61,253 (2005), *reh'g denied*, 114 FERC ¶ 61,099 (2006), *reh'g rejected*, 115 FERC ¶ 61,253 (2006); *Consolidated Edison Energy Massachusetts, Inc.*, 112 FERC ¶ 61,263 (2005); *reh'g pending*; *Pittsfield Generating Company, L.P.*, 115 FERC ¶ 61,059 (2006), *reh'g pending*.

¹³⁶ See *Id.*

¹³⁷ See Settlement Agreement at section XIII.F.

the implementation of the forward reserves market.¹³⁸ As the Commission noted in its order approving the implementation of that market, “markets for capacity and operating reserves are separate, distinct and non-duplicative.”¹³⁹

168. The Commission disagrees with the comments made by PSEG regarding the potential for the FCM to induce additional RMR agreements. While existing units may not be able to set the clearing price in all auctions, they will receive revenues from the capacity market that, combined with other revenues, will provide them more of an opportunity to recover their costs than the current “all or nothing” capacity market. Moreover, PSEG voted not to oppose the Settlement Agreement and “[does] not request any specific modifications thereto.”¹⁴⁰ PSEG’s statement that PJM’s RPM proposal provides a superior alternative suggests that it is using this proceeding to indicate its support for PJM’s RPM proposal. This is not the appropriate forum.

169. With regard to Berkshire Power’s comments, the Commission agrees with CMEEC and MMWEC: there is nothing in the Settlement Agreement that explicitly states that fixed transition payments will not be adequate to compensate ICAP resources operating under RMR agreements. Again, if this change in circumstances warrants termination of an RMR agreement, parties retain their rights to challenge the continued need for the contract.

k. Implementation of Scarcity Pricing

170. PPL believes that the FCM (and the transition period) alone will not be effective in solving New England’s long-term reliability problems. PPL recommends that ISO-NE be required to install enhanced scarcity pricing in the energy market in addition to the FCM proposal. PPL argues that scarcity pricing would permit prices to reflect the value of energy based on supply and demand conditions, increase the amount of price responsive demand, and provide incentives for long-term contracts and generation construction (in both peaking and baseload facilities). PPL believes that the FCM model is compatible with enhanced scarcity pricing in the energy market. Maine Parties

¹³⁸ *New England Power Pool and ISO New England, Inc.*, 115 FERC ¶ 61,175 (2006).

¹³⁹ *Id.* at P 78.

¹⁴⁰ Comments of PSEG at 1.

contend that PPL's request is beyond the scope of the proceeding and that the proper approach for seeking market changes is through the stakeholder process and/or a filing pursuant to section 206 of the FPA.

Commission Conclusion

171. The Commission agrees with Maine Parties that these arguments are beyond the scope of this proceeding. We encourage PPL to pursue its interests within the stakeholder process.

3. Other Issues

a. "Public Interest" Standard of Review for Prices and Modifications

172. Section 4.C of the Settlement Agreement states:

From the Effective Date, absent the agreement of all Settling Parties to the proposed change, the standard of review for: (i) challenges to the Capacity Clearing Prices derived through the FCA and prices resulting from reconfiguration auctions provided for in the Settlement Agreement and in the Market Rules addressing the terms of the Settlement Agreement that are approved or accepted by the FERC pursuant to section 3, and (ii) proposed changes to section 11, Part VIII below (Agreements Regarding Transition Period) and the Market Rules implementing that part, shall be the "public interest" standard of review set forth in United Gas Pipe Line Co. v. Mobile Gas Service Corp., 350 U.S. 332 (1956) and Federal Power Commission v. Sierra Pacific Power Co., 350 U.S. 348 (1956) (the "Mobile-Sierra" doctrine), whether the change is proposed by a Settling Party, a non-Settling Party, or the FERC acting *sua sponte*. This Settlement Agreement does not impose the Mobile-Sierra standard on any provision of this Settlement Agreement or the Market Rules that address the terms of the Settlement Agreement except as expressly provided in this section 4.C.

173. IECG opposes this provision, arguing that it represents an attempt by the settling parties "to write a broad exception to the statutory provisions of the FPA, not only for themselves . . . but also as a broad disenfranchisement of non-Parties from the protections against unjust and unreasonable rates provided in the FPA."¹⁴¹ Additionally, it argues that this provision improperly amends the NEPOOL Participants Agreement by

¹⁴¹ Comments of IECG at 16.

restricting the authority of ISO-NE to protect customers except in the case of exigent circumstances (pursuant to section 11.2 of the Participants Agreement). Accordingly, IECG argues, acceptance of this provision by the Commission would lead to imprudent and unlawful results.

174. More specifically, IECG asserts that as a policy matter, the Commission is not bound to follow any particular methodology when setting rates as long as the resulting rate is just and reasonable. Section 4.C of the Settlement Agreement would alter this regulatory paradigm, IECG contends, by adopting a particular rate methodology in advance of the actual results of the as-yet untested market mechanism. It further argues that the New England RTO Governance Process and the Commission's continued authority to assure the justness and reasonableness of rates address any fears of uncertainty that this settlement provision may be intended to resolve. Furthermore, IECG suggests that tying the hands of ISO-NE, NEPOOL and the Commission to respond to unexpected developments of a matter of such importance may encourage market participants to search for and seek to benefit from design flaws.

175. Additionally, IECG states that section 4.C of the Settlement Agreement would unlawfully amend the Participants Agreement and Regional Transmission Organization (RTO) governance procedures that specifically allow participants to make proposals for changes to the market rules (and have those proposals considered in the NEPOOL Committee process and, with support, by the Commission), and entitle participants to the faithful and independent execution by ISO-NE of its duties.¹⁴² According to IECG, these procedures explicitly do not permit market rules or procedures to be adopted outside of the NEPOOL advisory framework. IECG argues that ISO-NE and NEPOOL may not abrogate the procedural rights of market participants under the governing framework to make proposals for changes to the market rules through the insulation of particular market rules under a settlement. Further, IECG notes that section 17 of the Participants Agreement sets forth a process for amending the rights of parties under that agreement that was not observed. IECG maintains that accepting a waiver of this process through the joining of a settlement by ISO-NE or NEPOOL would invite a dismantling of the carefully balanced governance structure in New England.

176. Last, IECG asserts that section 4.C attempts to revoke the section 206 protections given to non-parties, and notes that the Commission has rejected such attempts in the

¹⁴² See *Id.* at 18-19, citing section 11 of the NEPOOL Participants Agreement.

past.¹⁴³ Even if the Settlement Agreement could be characterized as a contract, IECG argues, the parties have no legal ability to revoke the statutory protections of section 206. According to IECG, in analogous circumstances the Commission has rejected an attempt by the signatories to an agreement to limit the ability of non-parties to file challenges under section 206.¹⁴⁴

177. In reply, several parties note that this provision only applies the *Mobile-Sierra* public interest standard to limited provisions of the Settlement Agreement, namely (i) challenges to the clearing prices in the FCA and any reconfiguration auctions provided for in the market rules adopted pursuant to the Settlement Agreement, and (ii) proposed changes to the provisions of the settlement regarding the transition period and the market rules implementing those provisions. Capacity Suppliers argue that it is not unusual for parties to a settlement to use *Mobile-Sierra* to provide greater price certainty, which will in turn provide lower prices for consumers. ISO-NE agrees, arguing that use of the *Mobile-Sierra* provision in this instance will reduce regulatory uncertainty and the risk premium that may be required by new entrants. According to Capacity Suppliers, the market would suffer if the final auction clearing process were in jeopardy each time a consumer thought prices were too high or a seller thought prices were too low. Similarly, NEPOOL states that this provision was intentionally limited and crafted with the narrow purpose of providing certainty during the transition period and price certainty and finality to the auction prices.¹⁴⁵

¹⁴³ Comments of IECG at 21-22, citing *Carolina Power & Light Company and North Carolina Electric Membership Corporation*, 67 FERC ¶ 61,074 (1994) and *Northeast Utilities Service Corporation*, 66 FERC ¶ 61,332 (1994).

¹⁴⁴ Comments of IECG at 22, citing *PJM Interconnection LLC*, 96 FERC ¶ 61,206 (2001).

¹⁴⁵ NEPOOL states that this provision is far more limited than that standard that would be applied under the Commission's Notice of Proposed Rulemaking in Docket No. RM05-35-000. See *Standard of Review for Modifications to Jurisdictional Agreements*, 71 Fed. Reg. 303, FERC Stats. & Regs. ¶ 32,596 (2006). According to NEPOOL, if adopted, under those regulations *Mobile-Sierra* protections would serve as a default for review by the Commission of jurisdictional agreements (including settlement agreements) that are not signed by all signatories and are otherwise silent regarding the standard of review.

178. Further, Capacity Suppliers note that the *Mobile-Sierra* provision will not remove the risk of legal challenges, and the Commission cannot cede its authority under the FPA to ensure just and reasonable rates. Nevertheless, Capacity Suppliers contend, the Supreme Court allows parties to agree (via a *Mobile-Sierra* clause) that a stronger showing must be made before contract rates can be changed. Additionally, it argues that “[t]here is . . . ‘no Commission or court precedent that supports a finding that a non-signatory [such as IECG] may unilaterally seek changes to a *Mobile-Sierra* ‘public-interest’ contract under the ‘just and reasonable’ standard of review.’”¹⁴⁶ Similarly, NEPOOL states that contrary to IECG’s arguments, the Commission has consistently approved the use of the *Mobile-Sierra* standard for rates and terms established under a settlement agreement, and has consistently held that *Mobile-Sierra* protection does not “unjustly deprive a non-settling party from statutory rights to seek revisions to the terms or conditions of a filed settlement agreement.”¹⁴⁷ American National Power also argues that section 4.C is fully consistent with recent Commission policy, noting that the Commission has on several occasions approved similar *Mobile-Sierra* provisions applying the public interest standard of review for both signatories and non-parties.¹⁴⁸ As a result, American National Power states that there is no justification for deleting the provision from the settlement, particularly where doing so would threaten to undo the efforts of the parties to achieve a broadly-supported settlement.

179. Capacity Suppliers and ISO-NE also explain that the Settlement Agreement contains several provisions permitting challenges to the auction prices before they become final. First, they note that section 3.B of the settlement permits parties to challenge the market rules that are filed with the Commission to the extent that they are inconsistent with the settlement. Second, under Part IX of the Settlement Agreement, ISO-NE must make an informational filing with the Commission 90 days before an FCA runs, specifying any separate zones that will be employed, the bids that qualify for participation in the market, and the Market Monitor’s conclusions regarding the acceptability of bids in the auction. Interested parties have 15 days to file comments on this filing, and the Commission may order changes to the planned auction within 75 days. Finally, Capacity Suppliers and ISO-NE state that section 11 of Part II.G.3.b requires ISO-NE to file the results from the primary auctions under section 205 of the FPA, and parties will have 45 days to file objections to those auction results. Thus, they contend, the Settlement Agreement provides parties with “extraordinary protection” to voice their

¹⁴⁶ Reply Comments of Capacity Suppliers at 32, citing *Midwest Independent Transmission System Operator, Inc.*, 110 FERC ¶ 61,380 at P 24 (2005).

¹⁴⁷ Reply Comments of NEPOOL at 17-18 (citations omitted).

¹⁴⁸ Reply Comments of American National Power at 15-16 (citations omitted).

concerns regarding the justness and reasonableness of the auction prices while appropriately balancing a need for price certainty by giving the auction prices *Mobile-Sierra* protection once final.¹⁴⁹

180. Capacity Suppliers also assert that IECG does not raise any specific argument as to why the transition provisions should not be afforded *Mobile-Sierra* protection. It argues that IECG and others are already challenging these provisions under the just and reasonable standard through their settlement comments, and thus should not be afforded another opportunity to challenge those provisions at a later date.

181. NEPOOL asserts that IECG has misconstrued the impact on the stakeholder process of the limited *Mobile-Sierra* protections in the Settlement Agreement. Rather than “paralyzing” the stakeholder process as IECG contends, NEPOOL argues that the settlement specifically calls for the development of market rules within the stakeholder process in the NEPOOL Participants Agreement and through consultation with state agencies. Under this framework, ISO-NE retains its independent judgment and participants may support alternative market rules if support exists among the stakeholders. IECG and all other market participants, NEPOOL contends, are not limited by the *Mobile-Sierra* provision in their ability to vote in support of or in opposition to the market rules that are developed under the Settlement Agreement. Finally, NEPOOL argues that nothing in the NEPOOL Participants Agreement prohibits ISO-NE or NEPOOL from agreeing to a *Mobile-Sierra* provision in a settlement agreement, and that such a limitation on NEPOOL’s ability to settle contested matters would be ill advised.

Commission Conclusion

182. IECG appears to interpret section 4.C more broadly than it is intended to apply. Our reading of the provision indicates that, as several reply commenters note, the “public interest” standard will only apply to (1) the final clearing prices in the FCA and any reconfiguration auctions permitted under the market rules, and (2) the transition mechanism. The *Mobile-Sierra* provision does not apply to the market rules that will be developed and filed with the Commission under the Settlement Agreement or to any other aspect of the settlement not specifically mentioned in section 4.C. Therefore, IECG’s concerns that the *Mobile-Sierra* clause will broadly eliminate the ability of parties to exercise their rights under the FPA are misplaced.

183. The Commission will not require the Settling Parties to revise the limited *Mobile-Sierra* provision included in the Settlement Agreement. As NEPOOL, Capacity

¹⁴⁹ Reply Comments of Capacity Suppliers at 33; Reply Comments of ISO-NE at 53.

Suppliers and American National Power correctly state, the Commission has routinely permitted the use of similar provisions in settlement agreements, including contested settlements.¹⁵⁰ Moreover, as the Commission has stated on several recent occasions, “there is no Commission or court precedent that supports a finding that a non-signatory may unilaterally seek changes to a *Mobile-Sierra* ‘public interest’ contract under the ‘just and reasonable’ standard of review.”¹⁵¹ Therefore, as an initial matter, we conclude that the *Mobile-Sierra* provision is fully consistent with current Commission policy.

184. Furthermore, we find this *Mobile-Sierra* provision reasonable because it does not operate to the detriment of the parties who have not signed on to the Settlement Agreement. Those parties are still protected in several ways. First, as the court explained in *Northeast Utilities I*, “the most attractive case for affording additional protection . . . is where the protection is intended to safeguard the interests of third parties.”¹⁵² The court noted there that “[t]he *Mobile-Sierra* doctrine itself allows for intervention by FERC where it is shown that the interests of third parties are threatened,” noting that the standard articulated by the Supreme Court in such cases “is the protection of outside parties from ‘undue discrimination’ or imposition of an ‘excessive burden.’”¹⁵³

¹⁵⁰ See, e.g., *Midwest Independent System Operator, Inc.*, 115 FERC ¶ 61,174 (2006); *Midwest Independent System Operator, Inc.*, 110 FERC ¶ 61,177 (2005); *Midwest Independent System Operator, Inc.*, 110 FERC ¶ 61,380 (2005); *Pennsylvania-New Jersey-Maryland Interconnection*, 105 FERC 61,294 (2003), *reh’g denied*, 108 FERC ¶ 61,032 (2004); *Vermont Electric Cooperative, Inc.*, 114 F.E.R.C. ¶ 61,220 (2006); *Calpine Construction Finance Company, L.P.*, 114 F.E.R.C. ¶ 61,217 (2006); *Hermiston Power Partnership*, 114 F.E.R.C. ¶ 61,204 (2006); *Central Maine Power Company*, 114 F.E.R.C. ¶ 61,184 (2006); *San Diego Gas & Electric Company*, 114 F.E.R.C. ¶ 61,158 (2006); *Wisconsin Power & Light Co.*, 106 FERC ¶ 61,112 (2004).

¹⁵¹ *Pennsylvania-New Jersey-Maryland Interconnection*, 108 FERC ¶ 61,032 at P 7, citing *Public Utilities Commission of the State of California*, 105 FERC ¶ 61,182 at P 50 (2003).

¹⁵² *Id.*

¹⁵³ *Id.*, citing *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 344-45 (1956) (*Mobile*) and *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956) (*Sierra*). See also *Papago Tribal Utility Authority v. FERC*, 723 F.2d 950, 953 n.4 (D.C. Cir. 1983) (*Papago*) (recognizing that the Commission’s ability under the *Mobile-Sierra* doctrine to address undue discrimination under section 206 of the FPA includes the ability to address rates, terms and conditions of utility service that are “unduly discriminatory or preferential to the detriment of purchasers who are not parties to the contract.”).

Additionally, in *Northeast Utilities II*, the court rejected the notion, expressed in *Papago*, that the public interest standard is “practically insurmountable.”¹⁵⁴ Therefore, even under the “public interest” standard of review, the Commission retains significant authority to protect non-parties to the settlement from harm.

185. As several entities point out in the reply comments summarized above, the Settlement Agreement itself provides for thorough review of the final auction clearing prices. In particular, the Settlement Agreement provides that ISO-NE will make both an informational filing prior to the auction that includes information regarding the zones to be used and qualifying bids, and a section 205 filing following the auction containing the results. The limited *Mobile-Sierra* provision in section 4.C does not apply to these filings, and thus the Commission will review them under the just and reasonable standard. All parties will have the ability to comment on such filings, as set forth in the Settlement Agreement.

186. In conclusion, we believe that this limited *Mobile-Sierra* provision appropriately balances the need for rate stability and the interests of the diverse entities who will be subject to the FCM. Stability is particularly important in this case, which was initiated in part because of the unstable nature of ICAP revenues and the effect that has on generating units, particularly those who are critical to maintaining reliability. “The court has repeatedly emphasized the importance of contractual stability in a number of cases involving the *Mobile-Sierra* doctrine.”¹⁵⁵ The Court’s statement in *Mobile* that “all agree . . . [that] the stability of supply arrangements . . . is essential to the health of the natural gas industry” is no less true with regard to the health of New England’s electricity infrastructure.¹⁵⁶ At the same time, we must ensure that rates for capacity meet our legal requirements. This limited *Mobile-Sierra* provision achieves that balance.

b. Due Process

187. Objecting Parties argue that opponents of LICAP have not been afforded due process. First, they note that ISO-NE, when it originally filed LICAP, committed to conduct a “regional dialogue,” which began only with the recent settlement discussions.

¹⁵⁴ *Northeast Utilities Service Co. v. FERC*, 55 F.3d 686, 691 (D.C. Cir. 1995) (*Northeast Utilities II*), citing *Papago*, 723 F.2d at 954. The court “noted that neither *Mobile* nor *Sierra* stated or intimated that the ‘public interest’ doctrine was ‘practically insurmountable.’” *Northeast Utilities II*, 55 F.3d at 691.

¹⁵⁵ *Potomac Electric Power Co. v. FERC*, 210 F.3d 403, 409 (D.C. Cir. 2000) (citations omitted).

¹⁵⁶ *Mobile*, 350 U.S. at 344.

According to Objecting Parties, the settlement discussions only offered generators an attractive alternative (*i.e.*, the LICAP mechanism) to a negotiated settlement. Objecting Parties assert that the Presiding Judge during the hearing procedures should have been given the opportunity to consider alternatives to the LICAP mechanism. Following the oral argument, Objecting Parties continue, the Commission could have structured a fair and balanced settlement process. Instead, they contend that “the Commission offered a Hobson’s Choice,” structuring a settlement process that gave generators all the leverage when it stated in the October 21 Order that “if the parties cannot agree upon a workable alternative, the Commission will be prepared to move promptly to consider the existing record and the Initial Decision.”¹⁵⁷ This process, they argue, “forced load to buy its way out of the LICAP mechanism.”¹⁵⁸ To rectify this problem, Objecting Parties assert that the Commission should provide a fresh start, and give parties the opportunity to decide whether the FCM is appropriate, free of the threat that the Commission will implement LICAP.

188. In reply comments, Capacity Suppliers state that the Commission should reject these claims. First, Capacity Suppliers argue that the Commission did not issue a “settle or LICAP” ultimatum as Objecting Parties claim, but simply noted that it was prepared to act on the record and Initial Decision before it. Second, Capacity Suppliers assert that the level of support for the settlement among load parties,¹⁵⁹ and the fact that the settlement contains much of what load parties argued for at the oral argument, confirms load’s equal or superior leverage.¹⁶⁰ Finally, Capacity Suppliers argue that Objecting Parties’ claims that the Commission violated their due process rights by not considering alternatives are without merit. They note that the Commission rejected alternatives originally offered in

¹⁵⁷ Comments of Objecting Parties at 18, *citing* October 21 Order at P 10.

¹⁵⁸ Comments of Objecting Parties at 18.

¹⁵⁹ NEPOOL, in its reply comments, also states that the support of Load Supporters for the settlement contradict Objecting Parties’ claim of a lack of bargaining power.

¹⁶⁰ Reply Comments of Capacity Suppliers at 6 (noting that the settlement includes a forward capacity market with no demand curve and an availability metric, which load parties argued for at the oral argument).

response to the initial LICAP proposal, and subsequently “bent over backwards” to give load parties the opportunity to present their arguments by permitting oral argument and establishing additional settlement procedures at the request of load representatives.¹⁶¹

189. Similarly, ISO-NE states that NSTAR (one of the Objecting Parties) and others, in an October 7, 2005 letter to Chairman Kelliher, supported the institution of the settlement procedures they now protest as unbalanced, and did not indicate at the oral argument that a settlement procedure would be biased or unworkable. Further, it notes that the Connecticut and Massachusetts Attorneys General (also members of the Objecting Parties) supported the procedural proposal filed by CMEEC and MMWEC prior to the oral argument, which included a settlement process mediated by a Commission Administrative Law Judge of the parties’ choosing that would conclude on February 1, 2006. Moreover, ISO-NE notes that load representatives achieved almost unanimous political consensus that LICAP should not be adopted, and their efforts resulted in a provision in the Energy Policy Act of 2005 urging the Commission to carefully consider the states’ objections. These actions do not evidence a lack of bargaining power or leverage, ISO-NE argues. Additionally, ISO-NE contends that the fact that almost all of the elements of the market design advocated by NSTAR and the Energy Consortium prior to and at the oral argument were adopted in the Settlement Agreement, and that the Objecting Parties do not quarrel with the overall design of the FCM, shows that their arguments are “a strategy of delay.”¹⁶² Finally, ISO-NE asserts that claims that LICAP opponents were not given an opportunity to present alternatives are now moot, since an alternative was adopted through the settlement procedures.

Commission Conclusion

190. “[C]onstitutional due process requires that a party affected by a governmental action be given ‘the opportunity to be heard at a meaningful time and in a meaningful manner.’”¹⁶³ We agree with Capacity Suppliers and ISO-NE that this standard was more than satisfied in this proceeding. Through the course of this proceeding, parties have

¹⁶¹ *Id.* at 6-7. Capacity Suppliers note that no load parties opposed the proposal to establish settlement procedures or sought rehearing of the procedures set forth in the October 21 Order.

¹⁶² Reply Comments of ISO-NE at 24. *See also* Reply Comments of NEPOOL at 11.

¹⁶³ *See City of Anaheim, California, City of Riverside, California*, Opinion No. 483, 113 FERC ¶ 61,091 at P 153 (2005) (*citing Mathews v. Eldridge*, 424 U.S. 319, 333 (1976)), *reh’g denied*, 114 FERC ¶ 61,311 (2006).

been given numerous opportunities to present evidence and lodge their objections to the various proposals for dealing with the deficiencies identified in the ICAP market. As recounted in the background and procedural history of this order, the Commission: (1) addressed requests for rehearing of the April 25 Order initially establishing these section 206 proceedings; (2) provided notice and opportunity for comment on ISO-NE's proposed LICAP mechanism, and addressed those comments in the June 2 Order setting portions of that proposal for hearing;¹⁶⁴ (3) established hearing procedures regarding specific critical aspects of the LICAP mechanism, giving all interested parties the opportunity to fully litigate those matters; (4) took the rare step of providing the parties with opportunity for oral argument before the Commission to present their arguments regarding the LICAP mechanism and to advance potential alternatives to the LICAP mechanism; (5) established settlement procedures to allow the parties an opportunity to develop an alternative to the LICAP mechanism; and (6) is now addressing comments regarding the Settlement Agreement. It is unclear to us what more process could have been provided consistent with constitutional principles, and Objecting Parties have not stated what additional procedures should have been provided, instead simply seeking to have the Commission abandon the Settlement Agreement and provide a "fresh start."

191. Moreover, Objecting Parties' misread the October 21 Order as establishing a "settle or LICAP" ultimatum. That order merely recognized that in light of the need for the Commission to address the status quo (which the parties to this case agree is failing), its only option outside of a settlement agreement providing an alternative to LICAP was to consider the extensive existing record in the case. The Commission did not suggest what action it would take regarding the Initial Decision. It simply acknowledged that review of the record and the Initial Decision was the next procedural step available if settlement talks failed. Finally, the Commission did not "structure" the settlement procedures at all, but simply provided the parties with additional time and the assistance of a Commission-appointed settlement judge (who was requested by the parties) to help the parties reach agreement on an alternative. This procedure did not give any party leverage in the settlement discussions.

¹⁶⁴ As we noted in the March 23 Order I (in response to rehearing requests that the Commission might otherwise have rejected as untimely), the Commission considered alternatives to LICAP in the June 2 Order to the extent they were presented. March 23 Order I at P 18.

c. **Commission Jurisdiction over the Proposed Settlement Agreement**

192. Objecting Parties argue that the Commission lacks jurisdiction to approve the Settlement Agreement. First, they note that section 202(a) of the FPA¹⁶⁵ encourages voluntary formation of power pools and grants the Commission jurisdiction over such pools, including the reserve sharing mechanisms proposed by pool members. Nevertheless, Objecting Parties contend, section 202(a) does not trump the limits on the Commission's jurisdiction in section 201 of the FPA, which leaves to the states "plenary authority over generation, including the determination of how much generation individual utilities must own or control to reliably serve retail customers."¹⁶⁶

193. According to Objecting Parties, installed capacity has nothing to do with wholesale transmission of electric energy and is only tangentially related to wholesale sales of electricity. Objecting Parties note that the Commission has previously acknowledged, in both Order No. 888¹⁶⁷ and its orders in this proceeding, that matters related to the assessment of reliability and "resource adequacy" (or the amount of capacity necessary to serve loads) are within the interest and authority of the states.¹⁶⁸ Objecting Parties state that the Commission has previously respected this jurisdictional divide, under which power pool members are responsible for proposing and determining the justness and reasonableness of methods to share reserves.

194. Here, however, Objecting Parties state that the Commission has overreached the boundaries of its jurisdiction by directing ISO-NE to develop a new reserve sharing mechanism and has violated the limits of its jurisdiction in three respects. First, they contend that the Commission did not find the existing capacity market unjust and

¹⁶⁵ 16 U.S.C. § 824a(a) (2000).

¹⁶⁶ Comments in Opposition to Settlement of Objecting Parties at 26, *citing* 16 U.S.C. § 824a (2000).

¹⁶⁷ *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, 61 FR 21540 (May 10, 1996), FERC Stats. & Regs. ¶ 31,036 at 31,682 (1996), *order on reh'g*, Order No. 888-A, 62 FR 12274 (March 14, 1997), FERC Stats & Regs. ¶ 31,048 (1997), *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).

¹⁶⁸ Comments in Opposition to Settlement of Objecting Parties at 26-27.

unreasonable, finding only that RMR agreements were distorting the wholesale market. According to Objecting Parties, the underlying cause of the increase in RMR agreements was a lack of local operating reserves in critical areas, which has been addressed by the locational forward reserves market. Moreover, Objecting Parties contend that the record does not show that all generators in NEPOOL need additional revenue through a revised capacity market or that all generators are earning insufficient revenues. Rather, they contend that the record shows that certain types of generators (coal and nuclear) are earning sufficient returns, making additional payments a windfall. Furthermore, they contend that the record shows that New England has a surplus of capacity, making it irrational to build new capacity (except in locally critical areas, which it argues the locational forward reserve market will address).

195. Second, Objecting Parties state that while RMR agreements are within the Commission's wholesale market jurisdiction, the Commission may not mandate minimum requirements for capacity and then dictate the prices for that capacity as a remedy for the proliferation of RMR agreements. Objecting Parties argue that the Commission oversteps its jurisdiction with regard to voluntary power pools by "mandating a scheme that is directed to determining how much generation needs to be available to meet local load requirements, and sets forth the basis upon which owners of generation are to be compensated."¹⁶⁹ Moreover, Objecting Parties state that the Commission's lack of authority over the method by which a utility satisfies its reserve requirements requires that participation in any new capacity market construct must be voluntary.¹⁷⁰ Despite the provision in the Settlement Agreement permitting participants to self-supply capacity, they charge that the FCM "essentially requires [load serving entities] to meet their generation capacity reserve obligations through the FCM mechanism." Thus, Objecting Parties argue that if the Commission approved FCM, it would be imposing a resource adequacy requirement on New England utilities in contravention of the FPA.

196. Third, Objecting Parties argue that to the extent the current capacity market is flawed, ISO-NE may not make a proposal to correct those flaws because it is not a member of NEPOOL. They contend that directing ISO-NE to make a proposal amounts to a prohibited evisceration of the voluntary nature of power pools under section 202(a) of the FPA.

¹⁶⁹ *Id.* at 29.

¹⁷⁰ Objecting Parties also contend that states should be able to expressly opt out of the FCM and have their load serving entities be responsible for procuring capacity and reserves.

197. In reply comments, Capacity Suppliers respond that “the current ICAP market is without a doubt broken.”¹⁷¹ They note that the Commission has made several prior findings that the current capacity market is unjust and unreasonable.¹⁷² Further, they contend that the record contains substantial evidence showing that existing resources are not recovering sufficient revenues, noting that even the evidence of those opposing LICAP showed that generators were recovering only 10 percent of what they would recover under the LICAP mechanism as approved by the Initial Decision.

198. Capacity Suppliers argue that the Commission has jurisdiction to approve the settlement, and that state regulators, having taken the steps to form a tight power pool and organized electricity markets, may not “pick and choose” which market design elements they will cede to Commission jurisdiction and which they will reserve to state jurisdiction. Capacity Suppliers assert that federal courts have confirmed the Commission’s authority to allocate the costs of capacity among members of a power pool, even in the face of opposition from state regulators.¹⁷³ Capacity Suppliers contend that as the Commission has previously held in these proceedings, while the capacity market may impact state regulatory programs, the design of the capacity market itself is not within the jurisdiction of the states. Finally, they note that the Energy Policy Act of 2005 increases the Commission’s jurisdiction over electric system reliability.

199. ISO-NE contends that Objecting Parties have ignored the Commission’s prior determination on the issue of state jurisdiction over resource adequacy. In particular, ISO-NE argues that the Commission acknowledged its jurisdiction over issues

¹⁷¹ See Reply Comments of Capacity Suppliers at 17, *citing* Oral Argument Tr. At 252:8-14 (Chairman Kelliher’s closing remarks, noting that “[t]here does seem to be consensus around a threshold issue that there is a problem under the status quo that needs to be addressed.”)

¹⁷² Reply Comments of Capacity Suppliers at 17-18.

¹⁷³ *Id.* at 40-41, *citing* *Mississippi Industries v. FERC*, 808 F.2d 1525, 1543 (D.C. Cir. 1987) (holding that the Commission had the authority to reallocate the costs of a nuclear generating facility among affiliated operating companies “pursuant to its exclusive rate authority over wholesale transactions and its remedial authority as set forth in sections 205 and 206” of the FPA.)

concerning the capacity market when it set the initial LICAP proposal for hearing, and has approved ISO-NE's authority to set installed capacity requirements, finding that doing so did not infringe on the state's resource adequacy jurisdiction.¹⁷⁴

200. American National Power argues in reply that Objecting Parties' claims are an attempt to relitigate issues already decided by the Commission in these proceedings.¹⁷⁵ Additionally, American National Power argues that the Supreme Court has ruled "that the States cannot circumvent FERC's authority over the interstate transmission of electricity and wholesale electric sales by using their retail ratemaking authority."¹⁷⁶ It asserts that the issue in this proceeding is the price for wholesale capacity, which is clearly within the Commission's jurisdiction.

Commission Conclusion

201. The Commission has ample jurisdiction to consider and approve the Settlement Agreement. The settlement does not in any way alter the method by which resource adequacy requirements (particularly the installed capacity requirement) are determined or direct that a particular amount of capacity be installed, areas that the Commission has historically left to the states.¹⁷⁷ Also, as noted above, the Settlement Agreement contains provisions permitting load serving entities to self-supply their capacity obligations.¹⁷⁸ The Settlement Agreement and the tariff provisions that will follow it establish a mechanism and market structure for the purchase and sale of installed capacity at wholesale in interstate commerce and to determine the prices for those sales, bringing it squarely within the Commission's jurisdiction under the FPA.¹⁷⁹ Courts have confirmed

¹⁷⁴ Reply Comments of ISO-NE, *citing* June 1 2004 Order at P 58; *ISO New England, Inc.*, 111 FERC ¶ 61,185 at P 32 (2005).

¹⁷⁵ Reply Comments of American National Power at 19-20.

¹⁷⁶ *Id.* at 21, *citing* *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354, 373 (1988).

¹⁷⁷ Currently, ISO-NE calculates capacity requirements to achieve "Objective Capability," or the total amount of capacity required by the system to meet peak load plus a reserve margin. Objective Capability is determined each year in accordance with Northeast Power Coordinating Council (NPCC) standards. *See* March 23 Order I at P 30.

¹⁷⁸ *See* Settlement Agreement, Part III.O.

¹⁷⁹ 16 U.S.C. § 824(b)(1) (2000) ("The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce.")

that the Commission has jurisdiction under the FPA to regulate the charges for capacity in wholesale markets.¹⁸⁰ Objecting Parties do not point to any provision in the Settlement Agreement that establishes a resource adequacy requirement, or explain why the Commission does not have jurisdiction over the wholesale prices charged for the capacity product in New England. Objecting Parties' argument that load-serving entities are required to participate in the FCM (thus mandating participation in a resource adequacy program contrary to the FPA's limitations) fails because the provisions in the Settlement Agreement permit parties to self-supply their capacity obligations, and Objecting Parties have not explained why these provisions are insufficient.

202. Furthermore, the Commission fully addressed the issue of its jurisdiction in prior orders in this proceeding regarding the LICAP mechanism, and made clear that it did not intend to usurp the authority of the states' "central role in determining resource adequacy."¹⁸¹ In its March 23 *Order on Rehearing and Clarification*, in particular, the Commission explained that the issue in this proceeding is not how the capacity requirement is calculated or how the responsibility for meeting that requirement is divided among load serving entities.¹⁸² Instead, the issue is how prices for capacity are determined, to remedy identified flaws in the market.¹⁸³ As the Commission explained there, "the effect of this proceeding is not to impose a regional resource adequacy requirement, but merely to change the pricing."¹⁸⁴

203. Objecting Parties are also incorrect in their assertion that the Commission did not find the existing capacity market unjust and unreasonable, as required by section 206 of the FPA. As the Commission explained in the June 2 Order, the April 25 Order directed revisions to the ISO-NE tariff "pursuant to section 206 of the [FPA]" to "implement . . . location or deliverability requirements in the ICAP or resource adequacy market . . . so

¹⁸⁰ See *Municipalities of Groton v. FERC*, 587 F.2d 1296 (D.C. Cir. 1978) (holding that the Commission had jurisdiction over the installed capability charge in New England, a precursor to ICAP); *Mississippi Industries v. FERC*, 808 F.2d 1525 (D.C. Cir. 1987) (holding that the Commission could exercise jurisdiction over the allocation of the costs of capacity among four utility operating companies of a holding company under "its undisputed authority over the wholesale rates of electric generating facilities in interstate commerce.").

¹⁸¹ November 8 Order on Rehearing at 70.

¹⁸² *Devon Power LLC*, 110 FERC ¶ 61,315 at P 29-32 (2005).

¹⁸³ *Id.*

¹⁸⁴ *Id.* at P 32.

that capacity within [designated congestion areas] may be appropriately compensated for reliability.”¹⁸⁵ In the July 24 Order, the Commission further clarified that it was acting under section 206 of the FPA and formally stated that it “found that Market Rule 1 created an unjust and unreasonable result” because RMR agreements, and the need for such agreements, caused an extensive disruption to wholesale markets.¹⁸⁶ Additionally, Objecting Parties’ argument that the locational forward reserves market has addressed the underlying deficiencies in the capacity market is misplaced here, and is nonetheless unsupported by evidence.¹⁸⁷ To avoid any ambiguity, we reiterate here our prior finding that the existing ICAP market is unjust and unreasonable.

204. Further, we find without merit Objecting Parties’ claim that the record does not show that generators are earning insufficient revenues. We agree with Capacity Suppliers that the record contains substantial evidence regarding the inability of generators to earn sufficient revenues in the current market, both to continue operating or to support new investment.¹⁸⁸ Moreover, as we have stated previously, the increase in RMR agreements in New England provides further substantial evidence that generators are failing to recover their costs and require additional revenues.¹⁸⁹

205. Finally, we reject Objecting Parties’ contention that ISO-NE may not make a proposal to correct the flaws in the existing capacity market. The provisions pertaining to the existing capacity market are contained in ISO-NE’s tariff, and ISO-NE is the entity that is responsible under the NEPOOL Agreement for administering the regional markets. As a result, it is the proper entity to propose remedies to address the identified deficiencies in the current capacity market. In any event, the Settlement Agreement achieved a 78.46 percent favorable vote from the NEPOOL Participants Committee, far above the percentage vote necessary to permit ISO-NE to file market rule changes.¹⁹⁰

¹⁸⁵ June 2 Order at P 29, *citing* April 25 Order at P 33, 37.

¹⁸⁶ June 2 Order at P 29, *citing* July 24 Order at P 33.

¹⁸⁷ Additionally, the Commission recently reiterated that “the markets for capacity and operating reserves are separate, distinct, and non-duplicative.” *See New England Power Pool and ISO New England Inc.*, 115 FERC ¶ 61,175 at P 78 (2006); *see also New England Power Pool and ISO New England Inc.*, 105 FERC ¶ 61,204 at P 27 (2003).

¹⁸⁸ *See* Reply Comments of Capacity Suppliers at 18, *citing* Exh. ISO-23 (Rebuttal Testimony of David LaPlante in hearing); *see also supra* P 63.

¹⁸⁹ *See Devon Power LLC*, 110 FERC ¶ 61,315 at P 16 (2005). *See also supra* note 139 (listing recent Commission cases approving RMR agreements).

¹⁹⁰ *See* NEPOOL Participants Agreement, section 11.

d. Level of Support for the Settlement Agreement

206. Objecting Parties assert that the level of support for the Settlement Agreement is actually less than it first appears, and that the 78.46 percent vote in favor of the agreement in the NEPOOL stakeholder process masks the level of opposition to the agreement. In particular, they note that both Massachusetts and Maine (representing 53.4 percent of NEPOOL's peak demand) oppose the agreement, as do representatives of load from other states (including the Connecticut Attorney General). They also note that the Alternate Resources, End User and Publicly Owned Entity sectors of NEPOOL represented 40.27 percent of the 78.46 percent vote in favor (or more than 50 percent of the total NEPOOL support). According to Objecting Parties, due to flaws in the membership of these sectors, and the disproportionate weight given to the Publicly Owned Entity sector, true customer satisfaction with the settlement is misrepresented.¹⁹¹

207. NEPOOL states in reply that Objecting Parties' assertions regarding the opposition of Massachusetts and Maine are factually misleading. In fact, NEPOOL argues, most of the Massachusetts parties either support or did not oppose the Settlement Agreement, including Associated Industries of Massachusetts (representing the largest energy consumers in Massachusetts), transmission-owning utilities National Grid USA and Western Massachusetts Electric Company, and 38 publicly-owned entities. Similarly, Capacity Suppliers note that the Massachusetts Department of Telecommunications and Energy did not file comments in opposition to the settlement, nor did many of the load-serving entities in Massachusetts. NEPOOL notes that two distribution companies in Maine (Central Maine Power and Bangor Hydro Electric Company) did not file any comments in opposition, thus waiving any opposition they may have. NEPOOL notes that no competitive supplier from Massachusetts or Maine has filed comments in opposition. Further, it contends that Objecting Parties' statement that parties representing load from other states also oppose the settlement completely ignores the support of state regulators in Connecticut, New Hampshire, Rhode Island and Vermont, as well as the fact that the Connecticut Office of Consumer Counsel (the statutory representative of retail customers in Connecticut) is a settling party. Last, NEPOOL argues that the voting structure that Objecting Parties now challenge was created at the insistence of the Commission to ensure that individual entities like NSTAR would not have

¹⁹¹ See Comments in Opposition to Settlement of Objecting Parties at 14-16.

disproportionate voting weight, and that this structure represents a rejection of Objecting Parties' implicit argument that NEPOOL voting should be more reflective of economic interests.¹⁹²

208. CMEEC and MMWEC characterize Objecting Parties' arguments as a collateral attack on the NEPOOL voting process, and argue that it should play no role in the Commission's decision on the Settlement Agreement.¹⁹³ If the Commission decides to consider these issues, CMEEC notes that it also shares concerns with regard to the NEPOOL stakeholder process, arguing (in contrast to Objecting Parties) that the process gives too little weight to consumer interests and too much weight to sectors populated by investor-owned companies whose interest is to maximize shareholder returns and not ensure just and reasonable rates.

Commission Conclusion

209. We reject Objecting Parties' attacks on the NEPOOL stakeholder process and the NEPOOL stakeholder vote in favor of the settlement. Objecting Parties' arguments are misplaced. As NEPOOL, CMEEC and MMWEC correctly point out, those stakeholder processes were confirmed in other Commission proceedings, and issues regarding their effectiveness or fairness are outside the scope of this proceeding.

The Commission orders:

The proposed Settlement Agreement is hereby accepted, as discussed in the body of this order.

By the Commission. Commissioner Kelly concurring with a separate statement attached.

(S E A L)

Magalie R. Salas,
Secretary.

¹⁹² Reply Comments of NEPOOL at 9, *citing New England Power Pool*, 86 FERC ¶ 61,262 (1999).

¹⁹³ MMWEC also states that this stakeholder process was approved by the Commission in *New England Power Pool*, 88 FERC ¶ 61,079 (1999), and reconfirmed when the Commission approved New England's RTO arrangements in *ISO New England, Inc.*, 106 FERC ¶ 61,280 (2004).

Appendix A – List of Settling Parties

American National Power, Inc.
Associated Industries of Massachusetts
Boston Generating, LLC
Calpine Eastern Corporation
Calpine Energy Services, L.P.
Cape Wind Associates, LLC
Central Vermont Public Service Corporation
Connecticut Department of Public Utility Control
The Connecticut Light and Power Company
Connecticut Municipal Electric Energy Cooperative
Connecticut Office of Consumer Counsel
Conservation Services Group
Consolidated Edison Energy, Inc.
Dominion Energy Marketing, Inc.
Dominion Nuclear Connecticut, Inc.
Dominion Resources, Inc.
Duke Energy North America, LLC
Energy Management, Inc.
EnerNOC, Inc.
Entergy Nuclear Generation Company
Entergy Nuclear Vermont Yankee, LLC
Exelon Generation Company, LLC
Exelon New England Holdings, LLC
Fitchburg Gas & Electric Light Company
FFL Energy, LLC
Granite Ridge Energy, LLC
HQ Energy Services (U.S.), Inc.
ISO New England, Inc.
Lake Road Generating Company, LP
Long Island Power Authority (LIPA)
MASSPOWER
Milford Power Company, LLC
Mirant Americas Energy Marketing, LP
Mirant Canal, LLC
Mirant Kendall, LLC
Mystic Development, LLC, Mystic I, LLC. and Fore River Development, LLC
National Grid USA (on behalf of itself and its subsidiaries that are intervenors in this proceeding)

NEPOOL Participants Committee
New Hampshire Electric Cooperative, Inc.
New Hampshire Office of Consumer Advocate
New Hampshire Public Utilities Commission
NRG (Devon Power, LLC, Middletown Power LLC, Montville Power LLC, Norwalk Harbor, LLC, and NRG Power Marketing)
Pinpoint Power
Public Service Company of New Hampshire
RI Division of Public Utilities and Carriers
RI Public Utilities Commission
Select Energy
Sempra Trading
TransCanada Power Marketing Limited
The United Illuminating Company
Vermont Department of Public Service
Vermont Public Power Supply Authority
Vermont Public Service Board

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Devon Power LLC	Docket Nos.	ER03-563-030 ER03-563-055
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(Issued June 16, 2006)

KELLY, Commissioner, *concurring*:

Price mitigation in energy markets, coupled with capacity payments that did not recognize transmission limitations that prevent some generation from reaching some areas and lack of adequate transmission investment to address those limitations, ultimately led to increased proliferation of cost-based RMR agreements as generation that should have been permitted to retire had to be kept on for local reliability. The Commission issued orders finding the existing situation unjust and unreasonable and directing ISO-NE to propose a solution. In response, ISO-NE developed the LICAP proposal with its sloping demand curve and other features. The proposal stirred up great controversy and even Congress addressed it in the Energy Policy Act of 2005.

Following the ALJ's issuance of the LICAP initial decision, we granted requests to hold an oral argument on LICAP and on proposed alternatives and ultimately delayed issuance of an Opinion on the initial decision pending the outcome of settlement procedures among the parties.

To my surprise and delight the vast majority of the parties reached a settlement that they believe will meet their broad and varied interests in an acceptable manner. Moreover, my examination of their settlement proposal shows it to be a balanced and reasonable way to address the underlying problems the Commission identified in earlier orders.

For these reasons, I am pleased to be able to vote for this settlement despite the fact that it includes a limited application of the Mobile-Sierra public interest standard. For the reasons I have previously set forth in *Wisconsin Power & Light Co.*, 106 FERC ¶ 61,112 (2004), I do not generally believe that the Commission should depart from its precedent of not approving settlement provisions that preclude the Commission, acting *sua sponte* on behalf of a non-party, or pursuant to a complaint by a non-party, from investigating rates, terms and conditions under the "just and reasonable" standard of section 206 of the Federal Power Act at such times and under such circumstances as the Commission deems appropriate.

Therefore, I have generally dissented in part from orders that accept for filing settlements that provide that the Mobile-Sierra "public interest" standard of review will apply to Commission action pursuant to section 206. However, I believe that no such dissent is warranted here due to the settling parties' decision to apply the Mobile-Sierra public interest standard in a very constrained and time-limited manner; specifically, applying it only to the stated transition period prices and the annual prices generated each year by the FCM auctions. Customers are protected due to the time-limited nature of this application and the fact that everything else is covered by the just and reasonable standard.

Suedeem G. Kelly