UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

ISO New England, Inc. Docket No. ER05-134-000

ORDER ACCEPTING, SUSPENDING, AND REJECTING TARIFF REVISIONS IN PART AND ESTABLISHING EXPEDITED HEARING PROCEDURES

(Issued December 30, 2004)

1. In this order, the Commission accepts for filing, and suspends for a nominal period, to become effective January 1, 2005, certain proposed tariff revisions submitted by ISO New England Inc. (ISO-NE), concerning ISO-NE's collection of its projected calendar year 2005 administrative costs. This order establishes expedited hearing procedures to address the proper rate design for recovery of certain costs. We also reject one portion of the proposed tariff revisions. This order will benefit the New England energy market by permitting ISO-NE to continue to administer energy, ancillary services and other related markets in ISO-NE's control area, while ensuring that filed rates, terms and conditions are just and reasonable.

Background

2. On November 1, 2004, ISO-NE submitted for filing, pursuant to section 205 of the Federal Power Act (FPA),[1] revised tariff sheets (Revised Sheets) for ISO-NE's Tariff for Transmission Dispatch and Power Administration Services (ISO Tariff) to collect its administrative costs for calendar year 2005. The rates in the Revised Sheets accommodate operations by the ISO either as an independent system operator (ISO Scenario) or as the regional transmission organization for New England (RTO Scenario). The Revised Sheets are intended to integrate the substance of the ISO Tariff into the omnibus tariff that will be used by the regional transmission organization.

[1] 16 U.S.C. § 824d (2000).

I. Revenue Requirement

3. ISO-NE states that its revenue requirement for 2004 is approximately $125.1 million, consisting of a core operating budget ($83.7 million) and debt service ($41.4 million). ISO-NE states that the approximate four percent increase[2] in its revenue requirement is due primarily to: (i) the impact of salary increases and increased staffing levels and increased investments in ISO staff to support enhancements to the New England wholesale electricity markets and to support planning, outage scheduling and customer services; (ii) reliability initiatives; (iii) market enhancements provided for in the wholesale markets plan; (iv) Quality Management System implementation; and (v) increased internal and external communications. The ISO-NE Tariff has three core rate schedules: Schedule 1 for Scheduling Service; Schedule 2 for Energy Administration Service; and Schedule 3 for Reliability Administration Service. ISO-NE proposes to add Schedule 4 for Collection of FERC Annual Charges and Schedule 5 for Administrative Expenses of the Regional State Committee.

4. ISO-NE notes that, with the advent of regional transmission organization operations, ISO-NE will take over from the New England Power Pool (NEPOOL) Participants Committee the role of developing and making market rule and non-rate transmission tariff filings under FPA section 205. Accordingly, ISO-NE states that the core operating budget reflects the shift of $1.1 million from the NEPOOL Participants Committee expense budget (which is not currently included in the ISO-NE budget) to carry on this work. Therefore, ISO-NE notes that while the rates in Schedules 1, 2, and 3 for ISO-NE operations for the RTO Scenario are modestly higher than the rates specified for the ISO Scenario, this does not reflect a new expense for New England market participants and transmission customers, but instead simply a change in the entity that incurs and collects those expenses.

5. In support of its filing, ISO-NE notes that its proposed operating budget, including its proposed rate design changes, was reviewed and approved by the NEPOOL Participants Committee, producing a unanimous affirmative vote, with three abstentions, among NEPOOL's stakeholders. ISO-NE also states that the ISO-NE Board of Directors approved the 2005 operating budget at its October 21, 2004 meeting. ISO-NE requests an effective date for its filing of January 1, 2005.

---

[2] ISO-NE notes that the four percent increase excludes exceptional expenses of $2.2 million associated with locational installed capacity litigation ($.7 million), Regional Transmission Expansion Planning implementation ($.5 million), and siting and cost allocation ($1 million).

II. Proposed Rate Design Changes

6. ISO-NE states that its proposed 2005 operating budget utilizes the same core rate design methodology set forth in a Settlement Agreement approved by the Commission in Docket No. ER01-316-000,[3] as modified in terminology to accommodate the introduction of the Standard Market Design in New England on March 1, 2003. ISO-NE notes that the rate design for Schedule 2 was subsequently modified to address ISO-NE cost responsibility of virtual traders.[4]

A. Schedule 3 Alternative Proposal

7. Reliability Administration Service (RAS) is the service provided by ISO-NE to administer the Reliability Markets and to provide other reliability and informational services. Currently, the rate design for Schedule 3 allocates 100 percent of revenues based on customers' Real-Time Non-Coincident Peak Load Obligation. A RAS fee is payable by non-Participant point-to-point transmission service customers. The ISO states that it believes the existing Schedule 3 rate design is just and reasonable, but in response to the concerns of a Participant, it examined alternative rate designs. The NEPOOL Budget and Finance Subcommittee did not reach consensus on whether any change to the rate design is appropriate, so ISO-NE presents in the filing the tariff design currently in place and an alternate rate design for the Commission's consideration.

B. Schedule 4

8. ISO-NE states that the instant filing includes new rate Schedule 4 to account for the obligation of the ISO to pay FERC annual charges once it begins operating as a regional transmission organization. Under Schedule 4, the regional transmission owners will submit to ISO-NE the information necessary to complete the Commission's Reporting Requirement No. 582. ISO-NE will submit a consolidated New England-wide Form 582 to the Commission. When ISO-NE receives its annual charges statement from the Commission, it will bill the regional transmission owners for the amounts necessary to fund ISO-NE's payment of the annual charges.

---

[3] *See New England Power Pool*, 96 FERC ¶ 61,261 (2001).

[4] *See ISO New England Inc*., 106 FERC ¶ 61,294 (2004), *reh'g denied*, 108 FERC ¶ 61,138 (2004), *petition for review filed*, Braintree Elec. Light Dept. v. FERC, Case No. 04-1335 (D.C. Cir., filed October 1, 2004).

9. ISO-NE notes that the operating budget for the regional transmission organization scenario reflects a line item of $6.1 million for those annual charges. Of that amount, ISO-NE states that $6 million is not reflected in Schedules 1, 2, and 3 under the RTO scenario, because the $6 million will instead be collected through the pass-through mechanism in Schedule 4, and does not represent an increase in amounts paid by NEPOOL participants (currently paid indirectly through the transmission owners) for annual charges.

C. Schedule 5

10. ISO-NE also states that the instant filing includes new rate Schedule 5 to account for the possibility that a Regional State Committee will be formed in New England and seeks to justify and collect its rate through the ISO's tariff structure.

Notice of Filing and Responsive Pleadings

11. Notice of ISO-NE's filing was published in the *Federal Register*,[5] with motions to intervene and protests due on or before November 21, 2003. Motions to intervene were timely-filed by USGen New England, Inc. (USGen); Northeast Utilities Service Company (Northeast Utilities); NEPOOL Participants Committee; the Connecticut Office of Consumer Counsel (Consumer Counsel); the Connecticut Department of Public Utility Control (CT CPUC); H.Q. Energy Services (U.S.), Inc. (HQUS); Black Oak Energy, LLC (Black Oak); and the Massachusetts Municipal Wholesale Electric Company, Braintree Electric Light Department, Reading Municipal Light Department, and Taunton Municipal Lighting Plant (collectively, Massachusetts Municipalities). The Attorney General of the Commonwealth of Massachusetts (Attorney General); EPIC Merchant Energy LP (EPIC); and SESCO Enterprises LLC (SESCO) filed motions to intervene out-of-time. In addition, NEPOOL Participants Committee, Attorney General, Black Oak, SESCO, HQUS, Consumer Counsel, and Massachusetts Municipalities filed comments or protests. ISO-NE filed an answer to the protests of Consumer Counsel, Attorney General, and the Massachusetts Municipalities. On December 21, 2004, the Massachusetts Municipalities responded to the answer.

[5] 69 *Fed. Reg*. 67,388 (2004).

Discussion

Procedural Matters

12. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,[6] the timely, unopposed motions to intervene filed by USGen, Northeast Utilities, Attorney General, Consumer Counsel, CT DPUC, NEPOOL Participants Committee, HQUS, EPIC, Black Oak, SESCO, and Massachusetts Municipalities serve to make these entities parties to this proceeding. We will grant the motions to intervene out-of-time filed by the Attorney General, EPIC, and SESCO given their interest in this proceeding, the early stage of this proceeding, and the absence of any undue prejudice or delay.

13. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure,[7] prohibits an answer to a protest, unless otherwise permitted by the decisional authority. We find that good cause exists to allow ISO-NE's answer and the Massachusetts Municipalities' response, as they provide additional information that assists us in the decision-making process.

Analysis

I. Overall Revenue Requirement

14. The Attorney General and Consumer Counsel object to ISO-NE's proposed revenue requirement. The Attorney General states that the ISO-NE's revenue requirement, or $110 million, is four times what it was seven years ago, while ISO-NE's staffing has grown from 182 to 402. The Attorney General claims that ISO-NE has not shown that its proposed tariffs represent least cost or are just and reasonable. The Attorney General also notes that ISO-NE has not shown that New England customers are receiving benefits from the costs underlying the revenue requirement. The Consumer Counsel states that it has sought details from ISO-NE about ISO-NE's budget, the process it used for establishing the budget, and the basis for some of the line items in the budget. The Consumer Counsel also claims that the Commission cannot judge the reasonableness of the instant filing without a comparison between the ISO-NE's proposed 2005 budget and the budgets of other Independent System Operators.

15. We will reject the Attorney General's arguments concerning ISO-NE's overall revenue requirement as unsupported. The Attorney General has not identified a single line cost or line item that it believes is unjust or unreasonable. Instead, the Attorney

---

[6] 18 C.F.R. § 385.214 (2004).

[7] 18 C.F.R. § 385.213(a)(2) (2004).

General has objected to the entire ISO-NE filing with no support for its claims. Additionally, the Attorney General has not shown that the increase in ISO-NE's revenue requirement over the past seven years is unjustified. As outlined in ISO-NE's answer, seven years ago, ISO-NE served a region with no centralized markets. Today, ISO-NE serves sophisticated multi-settlement, locational marginal pricing-based markets, executes marketing monitoring activity, develops the demand side of the wholesale market, produces increasing amounts of information for market participants, and provides information concerning regional reliability. Each of these new responsibilities of ISO-NE provides valuable benefits to all New England customers.

16. Similarly, we will reject the Consumer Counsel's request for further details from ISO-NE about ISO-NE's budget. Consumer Counsel offers no specific critique of any specific cost in the instant filing. Consumer Counsel does raise a question about the salaries of ISO-NE employees, but ISO-NE points out, in its answer, that it has provided Consumer Counsel a spreadsheet cataloging the salary information for its employees. We will also reject Consumer Counsel's arguments regarding a comparison between ISO-NE's proposed 2005 budget and the budgets of other Independent System Operators. Independent System Operators face differing challenges and provide different services, depending on the size and make-up of the markets they serve, so a cross-comparison of budgets is not relevant in determining the reasonableness of ISO-NE's proposed 2005 budget.

II. Legal, Lobbying, and Uplift Expenses

17. In the instant filing, ISO-NE has included a section in its budget for its legal department, for which it seeks $7.23 million.[8] The Massachusetts Municipalities and the Attorney General object to specific aspects of the legal expense budget. The Attorney General claims that ISO-NE is seeking to bill New England customers for expenditures on lobbying, governmental relations and litigation costs, much of which may be adverse to the interests of those New England customers. The Attorney General also notes that ISO-NE has not provided a breakdown showing the amounts of these legal costs. The Attorney General also claims that ISO-NE has failed to show the potentially large amount of "uplift" and other out-of-market costs, even though this price signal is needed for customers to respond appropriately.

18. The Massachusetts Municipalities argue that greater transparency must be provided by ISO-NE in order to determine how the legal expenses are being spent. According to the Massachusetts Municipalities, $2 million of the $7.23 million legal expense budget is associated with activities that are not self-evident. Specifically, the Massachusetts Municipalities claim that it is not clear why ISO-NE needs to spend

[8] Instant Filing at Exhibit No. 3, Schedule 3.0 ISO, page 4 of 28.

$860,000 for "Government Affairs."[9] The Massachusetts Municipalities also question the difference between $862,000 for "Public Information" and $108,000 for "Public Relations."[10] The Massachusetts Municipalities object to the $295,000 charge for "regulatory affairs," and they question why such regulatory affairs charges were not subsumed in other line items. Finally, the Massachusetts Municipalities object to a line item of $1.4 million for Sullivan & Worcester, one of ISO-NE's outside counsel, without providing a description of the activities that firm will perform or how ISO-NE avoids duplication of effort in the relationship between its outside counsel and in-house staff.[11]

19. The Massachusetts Municipalities also point out that the proposed 2005 budget for ISO-NE in the RTO Scenario also includes an additional line item of $1.26 million in the legal department budget, which is labeled "Miscellaneous."[12] The Massachusetts Municipalities object to this line item since the proposed ISO-NE budget already includes a legal department line item for "Market Rule Changes," which is one of the primary additional responsibilities that ISO-NE was supposed to take on as a regional transmission organization.

20. We do not agree with the Attorney General's concern regarding the recovery of "uplift" and other out-of-market costs. The ISO-NE budget does not include out-of-market costs, and the ISO Tariff is not the vehicle for collecting uplift costs. Uplift costs are collected pursuant to NEPOOL Market Rule 1, which is distinct from the ISO Tariff.

21. In its answer, ISO-NE provides the Commission and the Massachusetts Municipalities with specific justifications for each of the line items criticized by the Massachusetts Municipalities. ISO-NE explains that the $295,000 line item for "Regulatory Affairs" includes work performed to keep all relevant regulatory agencies apprised of the ISO's activities, including system reliability, market operations, and matters pending before the Commission. ISO-NE states that it also includes monitoring the state legislatures and the Executive Branches of each state in New England on pending legislation and regulatory rulemakings that could impact ISO-NE's operations and mission. ISO-NE states that the funds under this line item primarily cover the professional fees paid to outside vendors hired to keep ISO-NE apprised of these activities.

---

[9] *Id.*

[10] *Id.*

[11] *Id.*

[12] *Id.*

22. Regarding the $862,000 line item for "Public Information," ISO-NE explains that the purpose of this function is to communicate ISO-NE's mission, system operations responsibilities, and markets administration functions to the public, media and NEPOOL participants. ISO-NE states that this line item contrasts with the "Public Relations" line item because the "Public Information" line item covers primarily the salary and overhead for ISO-NE employees performing this function. ISO-NE explains that the $108,000 for "Public Relations" covers the production and preparation of external communications, including ISO-NE's annual reports and other public information brochures. ISO-NE states that this line item is distinct from the "Public Information" line item because "Public Relations" covers professional fees ISO-NE pays to outside vendors to produce such reports and brochures.

23. ISO-NE also states that the $1.4 million line item for Sullivan & Worcester covers legal expenses related to general corporate work that may be allocated to this firm. ISO-NE notes, however, that this work may be allocated to another firm, or in-house legal staff, depending on the issue presented and the availability of outside counsel. ISO-NE states that, as a result, there can be no duplication of work because ISO-NE assigns each particular matter to only one law firm or to internal staff.

24. The Commission will accept the justifications for the above line items, including "Regulatory Affairs," "Public Information," "Public Relations," and the Sullivan & Worcester expenses. ISO-NE has provided the Commission and the Massachusetts Municipalities with a full list of the functions that each expense will accomplish, and adequate justification for each of the expenses.

25. Similarly, we will accept the $860,000 line item for "Government Affairs." The Massachusetts Municipalities' and Attorney General's concern that the New England customers are forced to pay for ISO-NE's lobbying costs are unfounded. As ISO-NE points out in its answer, ISO-NE does not attempt to influence public officials to take a specific action on specific legislation. Instead, ISO-NE explains, this line item covers activities related to ISO-NE's general interaction with state and federal government officials regarding the ISO's activities and mission, as well as its work to inform interested public officials on the operation and continued development of New England's wholesale electricity markets. ISO-NE notes that the need to engage in "Government Affairs" activities often arises when public officials ask ISO-NE to clarify information and present an independent, regional approach to complex issues about which individual utilities have provided more individual, parochial views. The Commission finds this explanation to justify the "Government Affairs" line item reasonable, and we note that the Massachusetts Municipalities offer no specific assertions that ISO-NE is engaged in impermissible activities but merely speculate as to the nature of its legal work.

Nothing in ISO-NE's explanation leads us to conclude that its budget includes expenditures for any type of political activity that is typically not allowed rate recovery under the Commission's regulations.[13]

26. Finally, the Commission will accept ISO-NE's "Miscellaneous" line item for operations in the RTO Scenario. As ISO-NE explains in the instant filing and in its answer, this line item covers the legal expenses associated with ISO-NE assuming the responsibility of all FPA section 205 filing requirements previously performed by NEPOOL. ISO-NE notes that because no activity—and related activity category for budgeting purposes—had been established at the time of the instant filing, this cost was entered into the "Miscellaneous" line. ISO-NE notes that the ISO-NE legal department currently participates actively in the formulation of ISO-NE and NEPOOL-proposed market rule changes and their consideration in the NEPOOL stakeholder process—irrespective of whether ISO-NE possesses the section 205 filing rights—and in the Commission proceedings that follow a NEPOOL filing of such changes. ISO-NE also explains that the line item, which is $1.1 million higher in the RTO than in the ISO Scenario, is higher because the ISO-NE legal staff will have to take over the full task of developing the rule changes and making the filings, a task currently performed by NEPOOL. ISO-NE estimates that this will involve a shift of approximately $1.1 million from the NEPOOL budget to ISO-NE's budget. The NEPOOL Participants Committee, in its comments, echoes this assertion. The Commission accepts this explanation as justification for the "Miscellaneous" line item in the regional transmission organization budget. The Commission also notes that this transfer of $1.1 million will not result in any additional costs to New England customers, as such costs are currently assessed through NEPOOL.

III. Schedule 2

27. On March 25, 2004, the Commission issued an order accepting a rate design for Schedule 2.[14] The accepted rate design featured two billing determinants for Schedule 2: "Transaction Units" and "Volumetric Measures." The Transaction Units measure the frequency and duration of activity and are indifferent to the size of any particular transaction, while the Volumetric Measures seek to capture a customer's physical reliance on the system administered by ISO-NE and thus the benefit received. The accepted Schedule 2 revenue requirement is allocated in the following manner: 15 percent to Transaction Units, with the number of Transaction Units and the rate for each Transaction Unit to be determined by ISO-NE for each tariff year, and 85 percent to

[13] See Account 426.4, Expenditures for certain civic, political and related activities. 18 C.F.R. Part 101 (2004).

[14] *See ISO New England Inc*., 106 FERC ¶ 61,294 (2004) (March 25 Order).

Volumetric Measures, subject to true-up adjustments, with the number of Volumetric Measures and the rate for each Volumetric Measure to be determined by ISO-NE for each tariff year.

28. In addition, the accepted Schedule 2 rate design featured a three-tiered rate design for the Transaction Unit portion of the Schedule 2 revenue requirement. The three-tiered rate design distinguishes between virtual activity—*i.e.*, increment bids and decrement bids—and physical activity. As a result, Participants engaging in virtual activity are charged lower transaction fees than are Participants engaging in physical activity. In the March 25 Order, the Commission stipulated:

> We will also require ISO-NE to file a report detailing the effect of virtual transactions on the energy markets it administers and whether or not virtual transactions have in fact led to price convergence between the real-time and day-ahead markets. This report must be filed along with ISO-NE's annual filing for approval of its 2005 administrative costs. Plus, the report must address whether virtual trading has led to price discovery, liquidity, and trading options, without adding any appreciable costs. Lastly, the report must address what other factors, if any, are potentially driving price convergence.[[15]]

29. In the instant filing, ISO-NE did not disturb the rate design for Schedule 2 accepted in the March 25 Order. ISO-NE also complied with the March 25 Order by including a Report on Effect of Virtual Transactions on New England Markets. ISO-NE asserts that the modeling suggests that virtual transactions have a generally positive effect on the market price of risk and increase day-ahead to real-time price convergence. ISO-NE also states that virtual trading inherently increases liquidity by increasing the number of entities which are able to participate in the market, and increases trading options by providing substantial additional flexibility to participants in managing their day-ahead market positions.

30. ISO-NE points out that, while virtual trading affects price convergence, many other factors also drive convergence, including unexpected equipment outages, fuel price volatility, and extreme weather and demand levels. ISO-NE notes that the market monitoring unit was not able to quantify the incremental costs of introducing virtual transactions to the market because they were part of the original Standard Market Design, which PJM Interconnection, LLC (PJM) developed. ISO-NE states that, since the base Standard Market Design software incorporated the ability to handle virtual transactions, it

[15] March 25 Order at P 31.

is estimated that maintaining that functionality did not add appreciable costs, though ISO-NE cautions that these conclusions are based on both limited data and relatively simple modeling efforts.

31. We will accept the proposed rate design for Schedule 2, including the three-tiered rate design for the Transactions Units. Based on our discussion below, the Commission concludes that there is no reason to change the current Commission-accepted three-tiered rate design for Schedule 2.

32. Massachusetts Municipalities assert that there is no correlation between the rate paid and the participation of virtual marketers in the market. They point out that ISO-NE's report on virtual transactions did not show a significant decrease in virtual trading when virtual bidders and physical bidders paid the same per-transaction rate, compared to the period in which the three-tiered rate design was in place. ISO NE's report did not speculate as to the reason for this. But, it is entirely possible that the virtual traders' continued participation was due to the fact that the rates they were paying were subject to refund (and therefore may be lowered), and that such rates were reasonably anticipated to be in effect for a relatively brief period of time (as they requested expedited Commission determination on this issue). We do know, however, that Financial Marketers have asserted that if they were required to pay the same per-transaction rates as the physical traders, it would have the effect of deterring, if not precluding, their participation in the markets.[16] As the Commission pointed out in the March 25 Order,[17] the current per-virtual bid charge forces virtual bidders to share some of the fixed costs of ISO-NE operation, yet is not so excessive as to reduce the amount of virtual trading and the exit of virtual traders from the New England Market.

33. ISO-NE asserts that the three-tiered rate design had a positive effect on the market price of risk and increased price convergence. According to ISO-NE, the availability of virtual transactions has increased participation, and therefore liquidity, in the New England market, expanding trading options, and has not added appreciable costs. ISO-NE also asserts that virtual transactions did not hamper price discovery in the New England market. The New England benchmark model, a simulation of the New England market conducted by ISO-NE, was used to simulate the day-ahead prices that would be observed with and without virtual transactions. The simulation model results suggest that virtual transactions both improve day-ahead to real-time price convergence and reduce the market price of risk.

---

[16] *See* March 25 Order at P 5, 11.

[17] March 25 Order at P 29-30.

34. Virtual trading also provides generators and load-serving entities with the flexibility to manage their financially binding day-ahead commitments at the hourly level. While supply offers and demand bids have restrictions on the number of offers, trading locations, and the type of participant who can submit physical trades, virtual transactions have no such limitations. They allow participants to optimally shape their supply offers and demand bids. Virtual transactions also allow entities other than generators and load-serving entities to participate in the day-ahead market. In theory, virtual transactions improve multi-settlement market efficiency by allowing participants to arbitrage systematic differences between day-ahead and real-time prices. Virtual transactions may also increase options and flexibility for managing physical production and delivery, in addition to permitting purely financial participation.

35. Therefore, we continue to believe that the three-tiered allocation is just and reasonable, given the benefits that virtual trading can bring to the marketplace as a whole, and the distinct possibility that a higher per-bid charge would reduce the bidding by virtual traders, with the resultant reallocation of uncollected costs to the other market participants. The Commission will accept the rate design for Schedule 2, as filed, and will require ISO-NE to continue to monitor the effect of virtual transactions on the New England market, and to file another report in its 2006 budget filing, addressing the same virtual trading issues outlined in the March 25 Order.

IV. Schedule 3

36. Black Oak, HQUS, and SESCO all object to the current RAS fee as unjust and unreasonable and support the adoption of the Alternative Design. Black Oak and SESCO argue that the current RAS fee[18] is excessive. ISO-NE witness Gary W. Pire explains in his testimony that, under the current rate design for Schedule 3, and using 2004 rates, a 100 MW export with a one-hour duration incurs an RAS fee of approximately $10,000. Pire explains that this occurs because, if the exporting Participant had only one transaction during the month, the volume associated with that transaction becomes its non-coincident peak, and the charges under Schedule 3 apply accordingly.[19]

37. In addition to being excessive, the protesters argue that the current RAS fee eliminates almost all arbitrage opportunities between ISO/RTO markets. Black Oak and SESCO note that the fee serves as a prohibitive market barrier to those participants who only engage in one or a few physical transactions each month. This is because the current RAS fee is applied without regard to the number of trades that are made in a month.

---

[18] Specifically, 9.52 cents/kW.

[19] *See* Testimony of Gary Pire, ISO-NE Exhibit 3 at 45.

38. Moreover, Black Oak and SESCO point out that the current rate design for Schedule 3 is inconsistent with the design of the equivalent tariffs in both the PJM and New York ISO systems. Protesters claim that this inconsistency frustrates competition between regions because the existing RAS rate design acts to prevent significant amounts of electricity from being exported out of New England.[20]

39. Protesters argue that the alternative RAS rate design[21] proposed by ISO-NE would fairly resolve competitive problems and eliminate existing seams caused by the current RAS rate design for Schedule 3. Protesters claim that this would be accomplished by putting New England's tariffs on a comparable basis with those of the New York ISO and PJM. Protesters point out that, as the ISO-NE filing states, the alternative RAS rate design would both substantially reduce the Schedule 3 cost per transaction and provide transaction price certainty.

40. In their comments, Massachusetts Municipalities argue that the Commission should reject the alternative RAS rate design and maintain the current RAS rate design for Schedule 3. Massachusetts Municipalities claim that the alternative RAS rate design is an unsupported subsidy for financial marketers. Massachusetts Municipalities note ISO-NE's claim that the adoption of the alternative RAS rate design would result in an approximate $2.8 million cost shift from export activity to other non-coincident peak load activity that is not export-related. Massachusetts Municipalities argue that New England load would be forced to pay for ISO-NE charges for export activity that provides New England load with no demonstrated benefit, and is therefore an inversion of cost causation principles. Furthermore, Massachusetts Municipalities note that the alternative RAS rate design never made it past the NEPOOL Budget and Finance Committee, and therefore was never presented to the NEPOOL Participants Committee.

41. Black Oak and SESCO claim that the aforementioned $2.8 million cost shift is fully warranted for four reasons: (1) the existing RAS rate imposes approximately 14 percent of the total annual budget on export transactions even though exports represent less than 2.4 percent of total loads; (2) the change does not permit any participant to receive a free ride on the ISO system, as all participants engaging in physical trading will continue to pay RAS-related costs; (3) the alternative RAS rate

---

[20] ISO load data show that ISO-NE imports more than twice as much electricity as it exports.

[21] Under the alternative rate design, ISO-NE would bifurcate the RAS rate into both a demand charge (which would continue to be based on non-coincident peak load obligation, as is the present rate design, but exclude the element of load correlating with exports) and an hourly rate component based on a dollar per MWh fee, that is only imposed on export activity-related load.

design acts to eliminate much of the unreasonable results associated with the current rate design; and (4) the alternative RAS rate design was fully considered and discussed by the participants through the NEPOOL Committee Process.

42. Black Oak and SESCO also point out that the alternative RAS rate design did not pass the NEPOOL Committee process because those participants that are negatively and unfairly affected by the current RAS rate design for Schedule 3 are in the minority among NEPOOL participants. Black Oak and SESCO claim that the majority of participants would impose higher costs to support a change to the alternative RAS rate design. Black Oak and SESCO seek Commission protection from the NEPOOL Participant majority.

43. Based on our review of the pleadings, the Commission will accept the continuation of the Schedule 3 rate design, subject to suspension and hearing. The Commission is concerned that the rate design for Schedule 3 contains unduly discriminatory and excessive fees that serve as barriers to market participation. Also worrisome to the Commission is the possibility that the rate design for Schedule 3 frustrates competition between ISO-NE and NYISO and PJM. The protesters have provided sufficient information and arguments that raise material issues of fact regarding the rate design for Schedule 3. Accordingly, we will accept for filing and suspend for a nominal period ISO-NE's proposed rate design for Schedule 3, to become effective January 1, 2005, and set this issue for hearing. Because this case involves a possible change in rate design, any changes that may result from the hearing will be applied on a prospective basis. [22] Finally, the Commission requires that this matter be expedited. Therefore, we direct the Administrative Law Judge to issue an Initial Decision by May 27, 2005.

V. Schedule 5

44. ISO-NE has included a new Schedule 5 in the instant filing. Schedule 5 is a placeholder which would allow a Regional State Committee (RSC) to submit, justify, and collect its administrative costs should such a committee be formed in the context of the regional transmission organization.[23]

45. The Massachusetts Municipalities argue that Schedule 5 is premature and legally indefensible. According to the Massachusetts Municipalities, any possible Regional State Committee should not be funded by wholesale electric customers, but instead should be

---

[22] *Consumers Energy Company*, 89 FERC ¶ 61,138 at 61,397, Opinion 429-A (*reh'g denied* in Opinion 429-B, 95 FERC ¶ 61,084).

[23] This rate schedule is proposed as a placeholder because the recovery of expenses for a Regional State Committee is pending in Docket No. EL04-112-000.

funded through the states' normal appropriations and funding mechanisms. The NEPOOL Participants Committee notes that it is currently impossible to determine whether a separate Schedule 5 is appropriate or desirable, or whether there are preferred means to pay the administrative costs of any Regional State Committee. The NEPOOL Participants Committee asks the Commission to defer taking any action on ISO-NE's proposal to include a Schedule 5 until a more complete proposal is actually presented for consideration.

46. We will reject Schedule 5 as unnecessary and premature. The Petition for Declaratory Order with respect to the formation of a RSC for New England is a matter pending in Docket No. EL04-112-000. The Commission does not believe that it is appropriate to provide a placeholder for the recovery of costs of a RSC that does not yet exist. We also believe that it is unnecessary for ISO-NE to recover any future costs it may incur for a RSC under a separate rate schedule; such costs should be included along with other regulatory costs in ISO-NE's budget. Schedule 5 is therefore rejected.

The Commission orders:

(A) ISO-NE's proposed revisions to its Tariff for Transmission Dispatch and Power Administration Services are hereby accepted for filing in part and rejected in part, as discussed in the body of this order, effective January 1, 2005.

(B) ISO-NE is hereby directed to submit a compliance filing removing Schedule 5 from the Tariff for Transmission Dispatch and Power Administration Services within 30 days from the date of issuance of this order.

(C) ISO-NE's proposed rate design for Schedule 3 is accepted for filing, subject to suspension and the outcome of an evidentiary hearing, to become effective on January 1, 2005, as discussed in the body of this order.

(D) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Energy Regulatory Commission by section 402(a) of the Department of Energy Organization Act and by the Federal Power Act, particularly sections 205 and 206 thereof, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the Federal Power Act (18 C.F.R., Chapter I), a public hearing shall be held concerning the justness and reasonableness of ISO-NE's proposed 2005 rate design for Schedule 3.

(E) A presiding judge, to be designated by the Chief Judge, shall, within fifteen (15) days of the date of the presiding judge's designation, convene a conference in this proceeding in a hearing room of the Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, DC 20426. Such conference shall be held for the purpose of establishing a procedural schedule. The presiding judge is authorized to establish procedural dates, and to rule on all motions (except motions to dismiss) as provided in the Commission's Rules of Practice and Procedure.

(F) The evidentiary hearing is limited to the issues raised in this order, and the entire proceeding, including the issuance of an Initial Decision, shall be completed by May 27, 2005.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.