

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

California Independent System Operator Corporation,
California Electricity Oversight Board,
Public Utilities Commission of the State of California,
Pacific Gas and Electric Company,
San Diego Gas & Electric Company, and
Southern California Edison Company

v.

Docket No. EL02-15-000

Cabrillo Power I LLC,
Cabrillo Power II LLC,
Duke Energy South Bay, LLC,
Geysers Power Company, LLC, and
Williams Energy Marketing and Trading Company

California Independent System Operator Corporation,
California Electricity Oversight Board,
Public Utilities Commission of the State of California, and
San Diego Gas & Electric Company

v.

Docket No. EL03-22-000

Cabrillo Power I LLC

ORDER DISMISSING COMPLAINTS

(Issued June 3, 2005)

1. In this order we dismiss the complaints filed by the California Independent System Operator Corporation (CAISO), and others (collectively, Complainants)¹ seeking to have the conclusions reached in an Initial Decision² regarding one component of rates for “reliability must-run” (RMR) service at three power plants in the San Francisco Bay Area,³ applied to other RMR units in California. CAISO and others had reached settlements with the owners of all other RMR units in California concerning all aspects of the rates for their RMR units, but eighteen months later, after the issuance of the RMR Initial Decision, CAISO and others sought to have the Commission find that those settlements were unjust and unreasonable based on the RMR Initial Decision. The Commission recently accepted a settlement agreement that resolved all issues concerning the rates for the Mirant RMR units, and terminated the dockets involved in the RMR Initial Decision without addressing the Initial Decision.⁴ The Initial Decision thus provides no basis on which the Commission can find that the rates for RMR service from other RMR units are unjust and unreasonable.

2. This order benefits customers because it preserves settlements and thus encourages future settlements.

Background

Origins of the RMR Contracts

3. These cases originated from the restructuring process in California. When the integrated electric systems were designed, they were designed to minimize system cost (and thus price to customers). In some cases this meant using generating units to perform tasks which are essentially transmission functions. Because of this design feature, some

¹ In Docket No. EL02-15-000, the other complainants are: California Electricity Oversight Board, Public Utilities Commission of the State of California, Pacific Gas and Electric Company (PG&E), San Diego Gas & Electric Company (SDG&E) and Southern California Edison Company (SoCal Edison). In Docket No. EL03-22-000, the other complainants are the California Oversight Board, the Public Utilities Commission of the State of California, and SDG&E.

² *Pacific Gas and Electric Company*, 91 FERC ¶ 63,008 (2000) (*RMR Initial Decision*).

³ Those three power plants are those owned by what are now Mirant Energy Delta, LLC and Mirant Energy Portero, LLC and are referred to in this order as the Mirant RMR facilities or the Mirant RMR units.

⁴ *San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Service*, 111 FERC ¶ 61,017, *reh’g denied*, 111 FERC ¶ 61,354 (2005) (*Mirant Settlement*).

generating units “must run” at certain times in order to ensure system reliability. Since the beginning of the restructuring process, it has been recognized that certain generating units because of their location and the configuration of the transmission system, are still needed to provide energy and ancillary services during certain hours to assure the reliable operation of the CAISO grid. These certain units are called RMR units. The underlying purpose of the RMR contracts was to assure that the CAISO would be able to call upon the RMR units when it needs them for reliability purposes to manage intra-zonal congestion and that their owners would not be able to exercise market power by withholding the RMR units’ output.

4. After years of negotiation, the parties representing a broad cross section of affected interests, including all of the complainants and respondents in these complaints as well as the parties involved in the RMR Initial Decision, reached a partial settlement (1999 settlement). That 1999 settlement established a *pro forma* tariff governing the terms and conditions under which RMR services are provided. The *pro forma* tariff is structured to include a payment structure consisting of monthly availability payments to recover a percentage of the fixed costs of operation of the RMR facilities.

5. The 1999 settlement provides that RMR units may select to operate under one of two conditions -- Condition 1 or Condition 2. Under Condition 1, the RMR unit owner is paid a combination of several different rates. First, they are paid for their variable costs and for prepaid start-ups. Second, they are paid a Monthly Option Payment which, as detailed in Schedule B of the RMR Agreement, is the sum of the Monthly Availability Payment and Monthly Surcharge, less any Monthly Nonperformance Penalty.

6. Under Condition 1, an RMR unit owner is paid a certain percentage of the unit’s annual fixed costs, which was the main issue in the proceeding that resulted in the RMR Initial Decision. The Fixed Option Payment is the maximum allowable Monthly Availability Payment summed over the twelve months of the year. This term does not appear in the RMR Contract itself, only in a stipulation that was part of the 1999 settlement. Participants propose Fixed Option Payments in the form of Fixed Option Payment Factors (FOPFs). The FOPF can be calculated by dividing the Annual Fixed Revenue Requirement (that was determined for each RMR facility in the 1999 Settlement) by the Fixed Option Payment. If an RMR unit is available for ISO dispatch up to its Maximum Net Dependable Capacity for all of its Target Available Hours for the year, its Fixed Option Payment will equal the sum of its Monthly Availability Payments. Under the currently-effective RMR Agreements, the owner of a Condition 1 unit retains all revenues earned in the competitive markets for energy and ancillary services. None of these revenues is credited back to the ISO.

7. Alternatively, RMR generators can elect to operate under Condition 2. Under this alternative, the ISO pays 100 percent of the unit’s fixed costs (assuming target availability), and the owner is not allowed to use the unit’s capacity in the competitive

markets for the owner's benefit. However, when the ISO dispatches the unit for reliability purposes, the owner *must* bid all capacity above that dispatched by the ISO into subsequent energy and ancillary services markets at prices determined by formulas in the contract, and the resulting market revenues are credited to the ISO.

8. In a series of settlements entered into in late 1999 and early 2000, further agreements were reached concerning the Fixed Option Payment at various RMR units.⁵ The only units concerning which parties did not reach settlement were the Mirant facilities. The Mirant facilities litigated the Fixed Option Payment. All other California RMR units had negotiated settlements with FOPFs ranging from 20 to 50 percent. The Mirant facilities sought FOPFs between 67 and 97 percent. That litigation resulted in the RMR Initial Decision. In the Initial Decision the judge concluded that the Fixed Option Payment for the Mirant facilities should be determined using a net incremental cost methodology.⁶ Applying the net incremental cost methodology resulted in a FOPF for the Mirant RMR units of approximately 2.7 percent.

Complaints

Docket No. EL02-15-000

9. On November 13, 2001, in Docket No. EL02-15-000 Complainants filed a complaint under section 206 of the Federal Power Act⁷ against Cabrillo Power I LLC, Cabrillo Power II LLC, Duke Energy South Bay, LLC, Geysers Power Company, LLC and Williams Energy Marketing and Trading Company (Williams) (collectively, Generators). Complainants asked the Commission to investigate the current Fixed Option Payments under each Generator's RMR contract with the ISO. Complainants urge that the Fixed Option Payments contained in the RMR contracts were not just and reasonable. Complainants asked the Commission to apply the "net incremental cost" methodology of determining the Fixed Option Payment found by the judge in the RMR

⁵ See, e.g., *Geysers Power Company, LLC*, 90 FERC ¶ 61,096 (2000); *Southern California Edison Company*, 90 FERC ¶ 61,091 (2000), *Pacific Gas and Electric Company*, 90 FERC ¶ 61,023 (2000), *Duke Energy Moss Landing, LLC*, 90 FERC ¶61,073 (2000), *Cabrillo Power I LLC and Cabrillo Power II LLC*, 92 FERC ¶ 61,116 (2000), and *Duke Energy South Bay LLC*, 92 FERC ¶ 61, 155 (2000).

⁶ Net incremental costs are the actual costs incurred by RMR unit owners as a result of RMR dispatches. *RMR Initial Decision*, 91 FERC at 65,113 n.25. Net incremental costs are calculated by subtracting any benefits that an RMR unit owner would not have realized in the absence of RMR dispatches from the total (gross) cost of the dispatches. *Id.*

⁷ 16 U.S.C. § 824e (2000).

Initial Decision to be just and reasonable. The Complainants argued that the RMR Initial Decision presented issues “closely similar, if not identical” to the issue raised by the complaint; the Complainants, therefore, urged the Commission to set a refund effective date of January 1, 2002, but to defer further action on the complaint until the Commission acted on the RMR Initial Decision. The Complainants stated that once the Commission addressed the RMR Initial Decision, it should proceed to adjudicate the complaint because the adjudication would likely “involve the implementation of the method endorsed by the Commission” in addressing the RMR Initial Decision on exceptions.

10. Notice of the complaint was published in the *Federal Register*, 66 *Fed. Reg.* 57,053, with interventions and protests due on or before November 23, 2001.

11. Answers were filed by each of RMR generators that were the named respondents to the complaint. In addition, a number of interventions were filed.

12. The Generators argued that the Complainants, by seeking to have the methodology recommended by the administrative law judge in the RMR Initial Decision applied to other RMR generators, is collaterally attacking the order of the Chief ALJ providing for individualized hearings on the FOPF issue. The Generators point out that the prior rulings of the Chief ALJ ordered that the Fixed Option Payment for each generator was to be set in an individual proceeding taking into account the unique factual circumstances of each RMR unit. They further argued that Complainants, who had settled the Fixed Option Payment for all units other than the Mirant units, were seeking to abrogate the many settlements entered into in good faith upon receiving a better deal through litigating the Fixed Option Payment for RMR units of a single owner. Finally, the Generators argued that a challenge to the Fixed Option Payments in these circumstances is barred by the *Mobile- Sierra* doctrine.

13. On October 31, 2003, the Commission approved an uncontested settlement agreement in Docket Nos. ER02-91-000 and ER2-303-000 involving Williams’ RMR units. Pursuant to the settlement, the FOPF applicable to Williams’ RMR units would remain at 27 percent for one unit and 32 percent for another unit until April 30, 2002, and then be reduced to 15 percent for both units, but subject to being increased pursuant to a “Most Favored Nation” provision. The settlement was contingent upon the Commission approving a motion to dismiss Williams from the complaint proceeding in Docket No. EL02-15-000. The Commission granted the motion to dismiss Williams from Docket No. EL02-15-000, over PG&E’s objection.⁸

⁸ *Williams Energy Marketing & Trading Company*, 105 FERC ¶ 61,165 (2003).

Docket No. EL02-20-000

14. On November 13, 2001, the CAISO, California Electricity Oversight Board, and the Public Utilities Commission of the State of California filed a complaint against PG&E challenging the Fixed Option Payments contained in RMR contracts between the CAISO and PG&E. The complaint asked the Commission to set a refund effective date of January 12, 2002 and defer further action until the Commission had ruled on the exceptions to the RMR Initial Decision.

15. Notice of the complaint was published in the *Federal Register*, 66 *Fed. Reg.* 58,134, with interventions and protests due on or before December 3, 2001.

16. PG&E filed an answer claiming that due to changed circumstances in the California market, there was then no way for the Commission to apply the CAISO's net incremental cost methodology to PG&E's RMR units. PG&E therefore urged the Commission to dismiss the complaint. If the Commission did not dismiss the complaint, PG&E asked the Commission to set a refund effective date and then to hold the proceeding in abeyance until the Commission acted on the RMR Initial Decision, at which time the Commission could then address the complaint and the unique facts presented by PG&E's RMR units.

17. The complaint in Docket No. EL02-20-000 was resolved by an uncontested settlement that was approved by the Commission on March 23, 2005.⁹

Docket No. EL03-22-000

18. On October 30, 2002, CAISO, SDG&E, the Public Utilities Commission of the State of California and the California Electricity Oversight Board filed a complaint asking the Commission to investigate the Fixed Option Payment contained in an RMR contract between CAISO and Cabrillo Power I LLC (Cabrillo I) with respect to Unit 4 of the Encina generating plant in Carlsbad, California. The complaint states that since the filing of the complaint in Docket No. EL02-15-000, the Encina 4 Unit was identified as needed for local area reliability and eligible to be designated as a "must-run" unit. The complaint seeks the same relief as in Docket No. EL02-15-000, and also asks that the Commission set a refund effective date of January 1, 2003 and defer further action until the Commission has ruled on the exceptions to the RMR Initial Decision.

19. Notice of the complaint was published in the *Federal Register*, 67 *Fed. Reg.* 67,609, with interventions and protests due on or before November 19, 2002.

⁹ *Pacific Gas & Electric Company*, 110 FERC ¶ 61,308 (2005).

20. An answer was filed by Cabrillo I. Cabrillo I asks the Commission to reject the net incremental cost pricing theory for RMR units and to dismiss the complaint.

Mirant Settlement

21. On January 31, 2005, a settlement was filed with the Commission that settled a number of proceedings in which Mirant was a party including the RMR proceedings that resulted in the RMR Initial Decision. Under the terms of the settlement, Mirant would not be affected financially by any Commission decision ruling on the exceptions filed to the RMR Initial Decision. However, the settlement provided that following the Commission's approval of the settlement, PG&E and Mirant would cooperate to file a request that the Commission rule on the merits of the RMR Initial Decision.

22. The Commission stated that it would not entertain such a request, saying:

Because the RMR Initial Decision is only binding upon the Mirant RMR units, and the Settlement resolves all claims with respect to the Mirant Parties that are addressed in the RMR Initial Decision, the issues addressed in the RMR Initial Decision are now moot. Accordingly, a further Commission order on the merits is not appropriate.

In effect, PG&E and Mirant propose that the Commission issue an advisory opinion based upon the RMR Initial Decision. We see no reason to do so. In this regard, the Commission finds that, in the CAISO's revised market structure, the use of RMR contracts will change significantly. The record that the RMR Initial Decision was based upon is now more than five-years old and is thus stale. Moreover, because the RMR Initial Decision was fact-specific to the Mirant RMR units, it is not a useful vehicle for setting a generic Commission policy on RMR contract issues. Under these circumstances, the Commission will not entertain a request by PG&E and/or the Mirant Parties that the Commission issue a guidance order in Docket No. ER98-495-000, *et al.*, regarding the RMR Initial Decision. [¹⁰]

23. The Commission terminated the proceedings that resulted in the RMR Initial Decision. PG&E and others sought rehearing of the Commission's decision to terminate the proceedings that resulted in the RMR Initial Decision. On rehearing, PG&E and others argue that the Commission erred in finding that the issues decided in the RMR Initial Decision are now moot and the Commission erred in deciding not to issue an advisory opinion based on the RMR Initial Decision. In an order issued concurrently

¹⁰ Mirant Settlement, 111 FERC ¶ 61,017 at P19-20 (*footnote omitted*).

with this order,¹¹ the Commission denied the requests for rehearing of the Commission's termination of Docket No. ER98-494-000, *et al.*

Discussion

24. We will dismiss the complaints. What we are being asked to do in the complaints is to initiate an investigation into the justness and reasonableness of one component of rates for California RMR units. The component complainants urge us to investigate is the Fixed Option Payments for RMR units operating under Condition 1. Complainants argue that the Commission should investigate these rates based on a finding in the RMR Initial Decision that the Fixed Option Payment for the Mirant RMR units operating under Condition 1 was unjust and unreasonable. Complainants, recognizing that the Commission had not at the time the complaints were filed endorsed the theory on which the RMR Initial Decision was based, asked the Commission to set a refund effective date, and to defer further action on the complaints until the Commission ruled on the then-pending exceptions to the RMR Initial Decision. As noted above, the proceedings that resulted in the RMR Initial Decision were settled by the parties and the proceedings were terminated without the Commission's addressing the RMR Initial Decision. Initial Decisions do not constitute binding Commission precedent.¹² Moreover, as we stated in *Mirant Settlement*, the RMR Initial Decision was fact-specific to the Mirant RMR units and is not a useful vehicle for setting a generic Commission policy on RMR contract issues,¹³ the record on which it was based is stale, and in the revised CAISO markets the use of RMR contracts will change significantly.¹⁴ Under these circumstances, we find that the RMR Initial Decision provides no basis on which to initiate an investigation into the Fixed Option Payments for RMR units in California operating under Condition 1.

¹¹*San Diego Gas & Electric Company v. Sellers of Energy and Ancillary Service*, 111 FERC ¶ 61,354 (2005).

¹² *Southern Company Services, Inc.*, 61 FERC ¶ 61,339 at 62,334 n.56, 62,335 n.59 (1992), *reh'g denied*, 63 FERC ¶ 61,217 (1993); *Illinois Power Company*, 62 FERC ¶ 61,147 at 62,062 n.17 (1993).

¹³ In this regard we note that in the settlements setting the Fixed Option Payment for each unit, the parties agreed to some unique terms and conditions for each unit so that there are substantial differences among the terms and conditions contained in the contracts for various RMR units in California. For example, in the settlements the Complainants ask us to investigate some of the RMR unit owners retain the right to choose between Condition 1 and Condition 2 operations on an annual basis, while others relinquished the right to choose Condition 2 and must operate under Condition 1.

¹⁴ *Mirant Settlement*, 11 FERC ¶ 61,017 at P 20.

The Commission orders:

The complaints filed in Docket Nos. EL02-15-000 and EL03-22-000 are hereby dismissed.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.