

FEDERAL ENERGY REGULATORY COMMISSION
Washington, D.C. 20426

August 31, 2005

In Reply Refer To:

Morgan Stanley Capital Group Inc.
Docket Nos. ER94-1384-030,
ER94-1384-031 and ER94-1384-032
South Eastern Electric Development Corp.
Docket Nos. ER99-2329-002,
ER99-2329-003 and ER99-2329-004
South Eastern Generating Corp.
Docket Nos. ER00-1803-001,
ER00-1803-002 and ER00-1803-003
Naniwa Energy LLC
Docket Nos. ER01-457-003 and
ER01-457-004
Power Contract Finance, L.L.C.
Docket Nos. ER02-1485-003,
ER02-1485-005 and ER02-1485-006
Power Contract Financing II, L.L.C.
Docket Nos. ER03-1108-002,
ER03-1108-004 and ER03-1108-005
Power Contract Financing II, Inc.
Docket Nos. ER03-1109-002,
ER03-1109-004 and ER03-1109-005
MS Retail Development Corp.
Docket Nos. ER03-1315-001,
ER03-1315-003 and ER03-1315-004
Utility Contract Funding II, LLC
Docket Nos. ER04-733-001 and
ER04-733-002

Sutherland Asbill & Brennan LLP
Attn: Daniel E. Frank, Esq.
Attorney for the Morgan Stanley Affiliates
1275 Pennsylvania Avenue, N.W.
Washington, DC 20004-2415

Dear Mr. Frank:

1. On November 10, 2003, Morgan Stanley Capital Group, Inc. (Morgan Stanley) filed an updated market power analysis on behalf of itself and South Eastern Electric Development Corp. (SEEDCO); South Eastern Generating Corp. (SEGCO); Naniwa Energy LLC (Naniwa); Power Contract Finance, L.L.C.; Power Contract Financing II, L.L.C.; Power Contract Financing II, Inc.; MS Retail Development Corp.; and Utility Contract Funding II, LLC (collectively, Morgan Stanley Affiliates) pursuant to the requirements of the Commission's orders granting the Morgan Stanley Affiliates authority to sell capacity and energy at market-based rates.¹

2. On March 24, 2005, as amended on June 6, 2005, pursuant to the Commission's April 14 and July 8 Orders² and the Commission's May 13, 2004 implementing order,³ Morgan Stanley filed an updated market power analysis on behalf of the Morgan Stanley Affiliates. Morgan Stanley states that the Morgan Stanley Affiliates in separate filings each submitted revised tariff sheets reflecting the Commission's reporting requirement adopted in Order No. 652⁴ concerning changes in status. Morgan Stanley states that the filings of SEEDCO and SEGCO also include revisions to their tariffs to reflect the

¹ *Morgan Stanley Capital Group Inc.*, 69 FERC ¶ 61,175 (1994); *South Eastern Electric Development Corp.*, 87 FERC ¶ 61,163 (1999); *South Eastern Generating Corp.*, 91 FERC ¶ 61,073 (2000); *Naniwa Energy LLC*, Docket No. ER01-457-003 (Feb. 15, 2001) (unpublished letter order); *Power Contract Finance, L.L.C.*, Docket No. ER02-1485-000 (May 24, 2002) (unpublished letter order); *Power Contract Financing II, L.L.C. and Power Contract Financing II, Inc.*, Docket Nos. ER03-1108-000 and ER03-1109-000 (Sept. 25, 2003) (unpublished letter order); *MS Retail Development Corp.*, Docket No. ER03-1315-003 (Oct. 21, 2003) (unpublished letter order); *Utility Contract Funding II, LLC* (formerly known as CES Marketing II, LLC), Docket No. ER03-206-000 (Jan. 16, 2003) (unpublished letter order).

² *AEP Power Marketing, Inc.*, 107 FERC ¶ 61,018 (April 14 Order), *order on reh'g*, 108 FERC ¶ 61,026 (2004) (July 8 Order).

³ *Acadia Power Partners, LLC*, 107 FERC ¶ 61,168 (2004) (May 13 Order).

⁴ *Reporting Requirement for Changes in Status for Public Utilities with Market-Based Rate Authority*, Order No. 652, 70 Fed. Reg. 8,253 (Feb. 18, 2005), FERC Stats. & Regs. ¶ 31,175, *order on reh'g*, 111 FERC ¶ 61,413 (2005).

Commission's market behavior rules.⁵ Morgan Stanley states that its other affiliates have already submitted tariff sheets reflecting the Commission's market behavior rules.⁶

3. As discussed below, the Commission concludes that the Morgan Stanley Affiliates satisfy the Commission's standards for market-based rate authority. We also conditionally accept the tariff modifications incorporating the Commission's market behavior rules and the Commission's reporting requirement of Order No. 652 as discussed below.

4. Morgan Stanley states that Morgan Stanley; Power Contract Finance, L.L.C.; Power Contract Financing II, L.L.C.; Power Contract Financing II, Inc.; MS Retail Development Corp.; and Utility Contract Funding II, LLC are each power marketers who do not own or control any generation or transmission facilities.

5. Morgan Stanley states that SEEDCO and SEGCO own generating facilities in the Southern Company control area and that Naniwa owns a generating facility in the Sierra Pacific Power Company control area.

Procedural Matters

6. Notice of the Morgan Stanley Affiliates' November 10, 2003 filing was published in the *Federal Register*, 68 Fed. Reg. 66,088 (2003), with interventions and protests due on or before December 1, 2003. None was filed.

7. Notice of the Morgan Stanley Affiliates' March 24, 2005 filing was published in the *Federal Register*, 70 Fed. Reg. 17,441 (2005), with interventions and protests due on or before April 14, 2005. None was filed.

⁵ *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 105 FERC ¶ 61,218 (2003), *order on reh'g*, 107 ¶ FERC 61,175 (2004) (Market Behavior Rules Order).

⁶ *See Morgan Stanley Capital Group Inc.*, Docket No. ER03-168-001 (Mar. 29, 2004) (unpublished letter order); *Naniwa Energy LLC*, Docket No. ER01-457-002 (Mar. 19, 2004) (unpublished letter order); *Power Contract Finance, L.L.C.*, Docket No. ER02-1485-004 (Mar. 29, 2004) (unpublished letter order); *Power Contract Financing II, L.L.C. and Power Contract Financing II, Inc.*, Docket Nos. ER03-1108-003 and ER03-1109-003 (Mar. 29, 2004) (unpublished letter order); *MS Retail Development Corp.*, Docket No. ER03-1315-002 (Mar. 29, 2004) (unpublished letter order); *Utility Contract Funding II, LLC* (formerly known as CES Marketing II, LLC), Docket No. ER03-206-001 (Mar. 29, 2004) (unpublished letter order).

8. Notice of the Morgan Stanley Affiliates' June 6, 2005 amendment was published in the *Federal Register*, 70 Fed. Reg. 41,393 (2005), with interventions and protests due on or before June 13, 2005. None was filed.

Discussion

Market-Based Rate Authorization

9. The Commission allows power sales at market-based rates if the seller and its affiliates do not have, or have adequately mitigated, market power in generation and transmission and cannot erect other barriers to entry. The Commission also considers whether there is evidence of affiliate abuse or reciprocal dealing.⁷ As discussed below, the Commission concludes that the Morgan Stanley Affiliates satisfy the Commission's standards for market-based rate authority.

10. In *AEP Power Marketing, Inc.*, the Commission adopted two indicative screens for assessing generation market power, the pivotal supplier screen and the wholesale market share screen. Morgan Stanley has submitted a streamlined application addressing the indicative screens, and states that Morgan Stanley; Power Contract Finance, L.L.C.; Power Contract Financing II, L.L.C.; Power Contract Financing II, Inc.; MS Retail Development Corp.; and Utility Contract Funding II, LLC do not own or control any generation.

11. Morgan Stanley states that SEEDCO, SEGCO, and Naniwa are exempt from submitting the indicative screens because they qualify under section 35.27 of the Commission's regulations, which provides that a generator need not demonstrate a lack of generation market power with respect to sales from capacity constructed after July 9, 1996.⁸ Morgan Stanley states that construction of the Naniwa, SEEDCO, and SEGCO facilities commenced after July 9, 1996, and, therefore, no generation market power analysis need be performed.⁹

⁷ See, e.g., *Progress Power Marketing, Inc.*, 76 FERC ¶ 61,155, at 61,919 (1996); *Northwest Power Marketing Co., L.L.C.*, 75 FERC ¶ 61,281, at 61,899 (1996); accord *Heartland Energy Services, Inc.*, 68 FERC ¶ 61,223, at 62,062-63 (1994).

⁸ 18 C.F.R. § 35.27(a) (2005). We note that the Commission intends to address as part of the generic rulemaking proceeding in Docket No. RM04-7-000 whether to retain or modify section 35.27(a) of our regulations.

⁹ July 8 Order, 108 FERC ¶ 61,026 at P 110.

12. Morgan Stanley states that under separate scheduling services agreements, Morgan Stanley has certain rights and obligations to schedule Deseret Generation & Transmission Cooperative, Inc.'s (Deseret) resources in the PacifiCorp control area and the North Carolina Electric Membership Corporation's (North Carolina EMC) resources in North Carolina.¹⁰ Morgan Stanley is obligated to schedule Deseret's and the North Carolina EMC's resources to meet the load requirements specified in the scheduling services agreements. Morgan Stanley states that it is obligated to schedule Deseret's resources to meet Deseret's load requirements, in accordance with schedules, guidelines, and instructions provided by Deseret and the terms of the filed scheduling services agreement. Morgan Stanley also states that, under the scheduling services agreements with the North Carolina EMC, Morgan Stanley acts as an agent for the EMCs in scheduling their resources, subject to parameters specified in contracts between the North Carolina EMC and the owners and/or operators of the resources, to meet the EMCs' load. Morgan Stanley states that if the energy scheduled to meet the forecast load exceeds Deseret's or the North Carolina EMC's actual load, then the excess energy is sold to Morgan Stanley, which then sells the excess energy into the market. Conversely, Morgan Stanley states that it is required to sell additional energy to either Deseret or the North Carolina EMC if energy above that produced by their resources is needed to meet the load. Morgan Stanley concludes that, although it schedules resources for Deseret and the North Carolina EMC, it has no authority to withdraw capacity from the market or to direct that resources remain idle and that Deseret and the North Carolina EMC, as owners of the resources, retain the right to dispatch and sell the output from the resources.

13. Based on Morgan Stanley's representations, the Commission finds that the Morgan Stanley Affiliates satisfy the Commission's generation market power standard for the grant of market-based rate authority.

¹⁰ Deseret is an electric cooperative formed by Bridger Valley Electric Association; Dixie-Escalante Rural Electric Association, Inc.; Flowell Electric Association, Inc.; Garkane Energy; Moon Lake Electric Association; and Mt. Wheeler Power, Inc. Morgan Stanley is a party to a Scheduling Service Agreement with Deseret. *Morgan Stanley Capital Group Inc.*, Docket No. ER03-1126-000 (Sept. 8, 2003) (unpublished letter order), *reh'g denied*, 106 FERC ¶ 61,274 (2004).

The North Carolina EMC is the generation and transmission cooperative of which Rutherford Electric Membership Corporation, Piedmont Electric Membership Corporation, Blue Ridge Electric Membership Corporation, and Energy United Electric Membership Corporation (collectively, the EMCs) are member-owners; Morgan Stanley acts as their agent in scheduling their resources under scheduling services and power purchase agreements, subject to certain contract parameters. March 24, 2005 filing at 10.

14. The Morgan Stanley Affiliates state that they do not own or control any transmission facilities other than certain limited facilities specifically used to interconnect their facilities to the regional transmission grid. Based on Morgan Stanley's representation, the Commission finds that the Morgan Stanley Affiliates satisfy the Commission's transmission market power standard for the grant of market-based rate authority.

15. Morgan Stanley explains that none of the Morgan Stanley Affiliates owns or controls any sites for the construction of new generation capacity, interstate or intrastate natural gas transmission lines, construction or engineering firms, or other essential resources or inputs (other than fuel supplies, such as natural gas, in which the wholesale markets are competitive) that could be used to restrict market entry by competing power suppliers. Based on Morgan Stanley's representation, the Commission is satisfied that the Morgan Stanley Affiliates cannot erect barriers to entry.

16. Morgan Stanley states that neither it nor any of its affiliates owns or controls a franchised service territory. Based on this representation, we find that the Morgan Stanley Affiliates satisfy the Commission's concerns with regard to affiliate abuse.

17. Consistent with the procedures the Commission adopted in Order No. 2001, an entity with market-based rates must file electronically with the Commission an Electric Quarterly Report containing: (1) a summary of the contractual terms and conditions in every effective service agreement for market-based power sales; and (2) transaction information for effective short-term (less than one year) and long-term (one year or greater) market-based power sales during the most recent calendar quarter.¹¹ Electric Quarterly Reports must be filed quarterly no later than 30 days after the end of the reporting quarter.¹²

¹¹ *Revised Public Utility Filing Requirements*, Order No. 2001, 67 Fed. Reg. 31,043 (May 8, 2002), FERC Stats. & Regs. ¶ 31,127 (2002). Required data sets for contractual and transaction information are described in Attachments B and C of Order No. 2001. The Electric Quarterly Report must be submitted to the Commission using the EQR Submission System Software, which may be downloaded from the Commission's website at <http://www.ferc.gov/docs-filing/eqr.asp>.

¹² The exact dates for these reports are prescribed in 18 C.F.R. § 35.10b (2005). Failure to file an Electric Quarterly Report (without an appropriate request for extension), or failure to report an agreement in an Electric Quarterly Report, may result in forfeiture of market-based rate authority, requiring filing of a new application for market-based rate authority if the applicant wishes to resume making sales at market-based rates.

18. The market-based rate tariff language proposed by the Morgan Stanley Affiliates does not comply with the market behavior rules as established by the Commission.¹³ Specifically, the parenthetical clause in section (b)(ii) of each of the Morgan Stanley Affiliate's market behavior rules that currently reads "(...or scheduling non-firm service or products sold as firm)" should be corrected to read: "(...or scheduling non-firm service for products sold as firm)..." Accordingly, the Morgan Stanley Affiliates are directed, within 30 days of the date of issuance of this order, to revise their market-based rate tariffs to include such language, without variation, consistent with the Commission's market behavior rules.

19. The Morgan Stanley Affiliates must timely report to the Commission any change in status that would reflect a departure from the characteristics the Commission relied upon in granting market-based rate authority.¹⁴ Order No. 652 requires that the change in status reporting requirement be incorporated in the market-based rate tariff of each entity authorized to make sales at market-based rates. The Morgan Stanley Affiliates proposed tariff language does not comply with the requirements of Order No. 652. Specifically, the word "shall" in the first and last sentences of your filed change in status language should be replaced with "must," as provided below. Within 30 days of the issuance of this order, please revise your tariffs to incorporate the following language, without variation, consistent with Order No. 652:

[insert market-based rate seller name] must timely report to the Commission any change in status that would reflect a departure from the characteristics the Commission relied upon in granting market-based rate authority. A change in status includes, but is not limited to, each of the following: (i) ownership or control of generation or transmission facilities or inputs to electric power production other than fuel supplies, or (ii) affiliation with any entity not disclosed in the application for market-based rate authority that owns or controls generation or transmission facilities or inputs to electric power production, or affiliation with any entity that has a franchised service area. Any change in status must be filed no later than 30 days after the change in status occurs.

¹³ Market Behavior Rules Order, 107 FERC ¶ 61,175 at P 73.

¹⁴ *Reporting Requirement for Changes in Status for Public Utilities with Market-Based Rate Authority*, Order No. 652, 70 Fed. Reg. 8,253 (Feb. 18, 2005), FERC Stats. & Regs. ¶ 31,175, *order on reh'g*, 111 FERC ¶ 61,413 (2005).

20. The Morgan Stanley Affiliates are directed to file an updated market power analysis within three years of the date of this order, and every three years thereafter. The Commission also reserves the right to require such an analysis at any intervening time.

By direction of the Commission.

Linda Mitry,
Deputy Secretary.