UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Bridgeport Energy, LLC Docket No. ER05-611-002

ORDER DENYING REHEARING

(Issued December 22, 2005)

1. On February 18, 2005, as supplemented on May 20, 2005, Bridgeport Energy, LLC (Bridgeport) filed a proposed unexecuted Reliability Must Run Agreement (RMR Agreement) between Bridgeport and the Independent System Operator New England, Inc. (ISO-NE). In an order issued on July 19, 2005, the Commission conditionally accepted the RMR Agreement for filing, suspended it for a nominal period, and set it for hearing and settlement judge procedures.[1] On August 18, 2005, the Connecticut Parties[2] and Bridgeport submitted timely requests for rehearing of the July 19 Order. In this order, the Commission denies rehearing of the July 19 Order.

Background

2. As we noted in the July 19 Order, the Commission has been addressing issues concerning the sufficiency of New England's capacity markets and the use of RMR agreements since 2003.[3] Bridgeport's RMR Agreement covers charges for reliability services provided by Bridgeport to ISO-NE from Bridgeport's new, 530 MW efficient, gas-fired, combined-cycle generation facility (Facility), comprised of one steam turbine and two combustion turbines operated as a single point of dispatch located in Southwest Connecticut (SWCT). Bridgeport and ISO-NE negotiated the RMR Agreement under

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[1] *Bridgeport Energy, LLC*, 112 FERC ¶ 61,077 (2005) (July 19 Order).

[2] The Connecticut Department of Public Utility Control (CT DPUC), the Connecticut Office of Consumer Counsel and Connecticut Attorney General's Office, and the Connecticut Municipal Electric Energy Cooperative (CMEEC).

[3] *See* July 19 Order at P 2-4.

section 3.3 of Exhibit 2, Appendix A of Market Rule 1.[4] Bridgeport argued in its filing that the RMR Agreement is necessary to permit its Facility to continue providing reliability services as Bridgeport is experiencing a "substantial revenue shortfall from sales at market prices."[5] It noted that ISO-NE made the determination that the Facility is needed for reliable system operation. Bridgeport submitted a supplemental filing in response to a deficiency letter that provided an effective date for the proposed agreement and further clarified cost information and losses sustained in the market.

3. The RMR Agreement submitted by Bridgeport is substantially similar to the *pro forma* Cost of Service Agreement contained in Market Rule 1. The RMR Agreement provides that Bridgeport will be paid a fixed monthly charge for providing reliability services. Under the agreement, Bridgeport is required to submit stipulated bids for the energy and ancillary services generated by the Facility, with any revenues earned by the Facility credited against the fixed monthly charge.

4. In the July 19 Order, the Commission conditionally accepted and suspended the RMR Agreement, and set the RMR Agreement for hearing and settlement judge procedures. In particular, the Commission set for hearing the issue of whether the proposed RMR Agreement is necessary for Bridgeport to recover its facility costs.[6] Further, the July 19 Order determined that if the hearing finds that the RMR Agreement is necessary to prevent the deactivation of the Facility, then the hearing and settlement judge procedures should determine a just and reasonable rate under the RMR Agreement. In determining the just and reasonable rate, the July 19 Order stated that the Commission would consider Bridgeport's full cost of service. The Commission accepted ISO-NE's

[4] Market Rule 1 was approved by the Commission in *New England Power Pool and ISO New England, Inc.*, 100 FERC ¶ 61,287, *reh'g granted in part and denied in part*, 101 FERC 61,344 (2002), *order on reh'g*, 103 FERC 61,304 (2003).

[5] Transmittal Letter at 6.

[6] Facility costs, as defined in the July 19 Order, are the costs ordinarily necessary to keep a facility available, such as fixed operating and maintenance (O&M), administrative and general (A&G), and taxes.

finding that the Facility is necessary to support reliability in New England.[7] Further, the Commission granted Bridgeport's request to waive the 60-day prior notice requirement, and made the RMR Agreement effective June 1, 2005.

<u>Procedural Matters</u>

5. As noted above, Connecticut Parties and Bridgeport filed requests for rehearing of the July 19 Order. Bridgeport filed an answer to Connecticut Parties' request for rehearing, and ISO-NE and CT DPUC filed answers to Bridgeport's request for rehearing. Rule 713(d), of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(d) (2005), prohibits answers to requests for rehearing. We will accept the answers from Bridgeport, ISO-NE and CT DPUC as they provided information that assisted us in our decision-making process.

<u>Discussion</u>

A. <u>ISO-NE's Reliability Determination</u>

6. Connecticut Parties argue that the Commission erred in deferring to ISO-NE's reliability determination in concluding that Bridgeport's facilities are needed for reliability and, thus, may be entitled to a cost-of-service rate for reliability services.[8] They state that ISO-NE is a private corporation, and the Commission may not subdelegate any decision-making authority to ISO-NE, except as authorized by statute.[9] Connecticut Parties argue that although Market Rule 1 contemplates that ISO-NE will make some initial decisions about unit eligibility, section 205 of the Federal Power Act (FPA)[10] assigns to the Commission ultimate authority to approve or deny RMR agreements. They emphasize that the Commission must independently examine and

[7] The Commission also accepted Bridgeport's general cost-of-service approach (including fixed and variable costs in the RMR Agreement), but set several components of that cost-of-service for hearing, including treatment of income taxes, Bridgeport's request to set its rates on a non-levelized basis, and Bridgeport's proposed energy management fee.

[8] CMEEC does not join in the request for rehearing on this issue.

[9] *Citing United States Telecom Ass'n v. FCC*, 359 F.3d 554, 566 (D.C. Cir. 2004); *Columbia Gas Transmission Corp. v. FERC*, 404 F.3d 459, 462-62 (D.C. Cir. 2005).

[10] 16 U.S.C. § 824d (2000).

determine on the basis of a factual record whether a unit seeking an RMR agreement is needed for reliability and requires financial assistance to remain available. Connecticut Parties assert that a determination by the ISO-NE will likely err on the side of more reliability and may approve units as "needed for reliability" simply to be on the "safe" side, but with insufficient regard for the resulting cost. Further, the Connecticut Parties argue that the Commission's denial of their request to set this issue for hearing did not allow the Connecticut Parties the opportunity to dispute the facts underlying ISO-NE's reliability determinations and deprives intervenors of their due process rights.

Answer

7. Bridgeport states that in the stakeholder process that approved Market Rule 1, the Connecticut Parties never challenged the authority of ISO-NE to make reliability determinations. Bridgeport argues that it is too late for the Connecticut Parties to raise these claims, as the issues were put to rest two years ago.

Commission Determination

8. We deny Connecticut Parties' request for rehearing of the reliability determination. The reliability determination issue has been addressed in prior RMR orders, including recently in *PSEG*.[11] As we noted in the July 19 Order, the Commission accepts ISO-NE's determination that Bridgeport is needed for reliability as Market Rule 1, the currently-effective rate schedule on file with the Commission, permits ISO-NE to determine whether units are needed for reliability. The Commission's review of the RMR Agreement, under section 205 of the FPA, included a review of the evidence presented by Bridgeport and ISO-NE that the facility is needed for reliability. Connecticut Parties' assertion that ISO-NE has provided no basis for its reliability determination for Bridgeport ignores Appendix E of Bridgeport's initial filing, which included summaries of three ISO-NE System Planning studies to demonstrate that Bridgeport is needed for system reliability. Specifically, these studies show that in 2005, SWCT would be over 430 MW short of capacity without the Facility.

9. With regard to Connecticut Parties' argument that the Commission's denial of their request to set the reliability issue for hearing did not allow them the opportunity to dispute the facts underlying ISO-NE's reliability determinations and deprives intervenors of their due process rights, we disagree. Connecticut Parties had full opportunity to dispute ISO-NE's reliability determination in their protest. They failed, however, to present any evidence to support their assertion that ISO-NE's studies are unreliable, or

[11] *PSEG Power Connecticut, LLC*, 110 FERC ¶ 61,441 (2005) (*PSEG*).

that ISO-NE incorrectly determined, in consultation with the Independent Market Advisor (and reflected in ISO-NE's letter to Bridgeport), that the Facility is needed for reliability. Absent an issue of material fact that is in dispute, the Commission need not hold an evidentiary hearing.[12]

10. Furthermore, the Commission has not delegated its authority under section 205 of the FPA to determine that the RMR agreement filed here is just and reasonable. The Commission has satisfied its responsibilities under the FPA by conditionally accepting the RMR Agreement for filing, suspending it, and setting it for hearing to ensure that the rates contained in any potential agreement are just and reasonable.

B. Prior Use of the Facility Costs Test

11. Bridgeport contends that the Commission did not apply the facility costs test in *Milford*[13] or previously in determining RMR eligibility. Specifically, Bridgeport argues that there is no indication in previous Commission orders dealing with RMR agreements that a seller's right to be adequately compensated for providing a jurisdictional service is contingent on the seller being able to show that, absent an RMR agreement, its revenues have failed or would fail to recover its "facility costs," because this measure of costs does not include any return of or on investment.[14] It states that in *Milford*, the Commission focused on "adequate compensation" as it had applied this standard to other RMR facilities, and recognized that generators have to be assured of receiving a reasonable opportunity to recover an adequate amount of their fixed costs. Bridgeport also points out that the term "facility costs" is used for the first time in the July 19 Order, and argues that it was arbitrary and capricious for the Commission to impose this new test by improperly reinterpreting *Milford* after the fact.

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[12] *See, e.g., Kansas Power and Light Company v. FERC*, 851 F.2d 1479, 1484 (D.C. Cir. 1988); *Ohio Power Company v. FERC*, 744 F.2d 162, 170 (D.C. Cir. 1984); *Cities of Batavia v. FERC*, 672 F.2d 64, 91 (D.C. Cir. 1982); *see also Williams Natural Gas Co.*, 53 FERC ¶ 61,060 at 61,188, *order on reh'g*, 53 FERC ¶ 61,231 at 61,966-67 (1990); *Northwest Pipeline Corporation*, 53 FERC ¶ 61,012 at 61,051-52 (1990); *El Paso Natural Gas Co.*, 48 FERC ¶ 61,202 at 61,756-57 (1989).

[13] *Milford Power Company, LLC*, 110 FERC ¶ 61,299 (*Milford*) (2005), *order on reh'g*, 112 FERC ¶ 61,154 (2005).

[14] *Citing Devon Power LLC*, 109 FERC ¶ 61,154 at P 43 (June 2 Order), *order on reh'g*, 109 FERC ¶ 61,154 (2004); *PSEG Power Connecticut, LLC*, 110 FERC ¶ 61,020 at P 18, *order on reh'g*, 110 FERC ¶ 61,441 (2005).

Commission Determination

12. The formal use of the facility costs test for RMR eligibility was necessitated by the recent application for RMR agreements by both Milford and Bridgeport, which are new and efficient baseload generators. As we noted in both *Milford* and the July 19 Order, these proposed agreements presented a unique set of circumstances compared to the prior RMR agreements in New England. The RMR agreements we had accepted before Milford's involved peaking units that were seldom run and frequently subject to mitigation under the current market rules.[15] The concern was that absent a cost-of-service agreement, these peaking units would not continue to operate. As demonstrated by the support provided in those prior filings (including formal requests to deactivate), it was clear that these peaking units were not able to earn sufficient revenues to remain in the market. By comparison, efficient baseload generators, like Bridgeport's and Milford's, with high capacity factors and lower relative variable costs were assumed to possess a greater ability to recover costs through the energy market than peaking units.

13. Bridgeport's argument questioning the Commission's prior use of the facility costs test neglects the Commission's finding in *Milford* that "the facility owners have not earned sufficient revenues in the market to keep the facility in operation."[16] Further, though not formally named "facility costs" until the July 19 Order, this eligibility assessment in *Milford* noted that "in 2004, Milford, after paying its variable fuel expenses, had insufficient revenue to pay the costs ordinarily necessary to keep a facility available, such as fixed O&M, Administrative and General (A&G), and taxes."[17] Therefore, the Commission's use of the facility costs test in the July 19 Order was consistent with *Milford*.

C. RMR Eligibility Determination

14. Bridgeport argues that the Commission's requirement that it demonstrate that it will not be able to recover its facility costs is inconsistent with the Commission's prior holdings that sellers are entitled to a full cost-of-service rate and that depreciation and

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[15] *Milford* at P 40.

[16] *Id.*.

[17] *Id*. n.31.

return on equity are essential components of a just and reasonable rate.[18] Bridgeport states that the just and reasonable standard of the FPA requires that cost-based rates include a return on and of capital and argues that it is of "no significance" that the Commission is "imposing the confiscatory rate through impediments to Bridgeport obtaining its filed rate, rather than through a modification of its filed rate."

15. Bridgeport argues that the Commission erred in requiring Bridgeport to prove that it has realized true losses each year since 1999 and that an RMR agreement is necessary to prevent deactivation. Bridgeport argues that the Commission did not impose those standards in prior orders and that Market Rule 1 does not impose them. Bridgeport states that the standard is not, as the July 19 Order states, whether the proposed RMR agreement is necessary to prevent deactivation of the Facility, but, as Market Rule 1 states, whether the agreement is "necessary to ensure that the facility will be available."[19] With regard to the latter, Bridgeport states that this standard removes the risk that the subject facility will not remain available for reliability reasons because it is receiving inadequate compensation. By contrast, Bridgeport argues that the Commission standard allows for a cost-based RMR agreement only if the seller can prove that it is sustaining such heavy losses that it would deactivate, but that the word "deactivate" is not found in Market Rule 1.

16. Bridgeport also argues that the Commission erred in determining that it has the authority to restrict Bridgeport's right to file and obtain a cost-based rate. Bridgeport asserts that sellers have the legal right under the FPA to select either a cost-based rate or a market-based rate as a general matter,[20] and have the right to select cost-based rates under Market Rule 1 and under Commission precedent which has held that market-based rates are not compensatory.[21] Bridgeport argues that this statutory right cannot be limited by regulatory mandate, such as the standards that the Commission has imposed on

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[18] *Citing, e.g., Mirant Kendall, LLC and Mirant Americas Energy Market, L.P.*, 109 FERC ¶ 61,227 at P 36 (2004), *reh'g denied*, 110 FERC ¶ 61,272 (2005); *PSEG* at P 30; *Milford.*

[19] *Citing* Market Rule 1, section 3.3.1(C)(iii).

[20] *Citing San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services Into Markets*, 99 FERC ¶ 61,159 at 61,641 (2002) (*SDG&E*).

[21] C*iting* June 2 Order at P 72.

Bridgeport. Bridgeport explains that such an imposition effectively requires that it maintain its existing rate until it demonstrates that its losses are so great as to imperil its existence.

17. Connecticut Parties, on the other hand, argue that the Commission's decision to apply different tests to determine RMR eligibility and cost of service recovery is arbitrary and capricious. They state that new, efficient plants, like Bridgeport's, should have the same requirement for both RMR eligibility and ratepayer-supported cost recovery, which is recovery of non-investment related costs only.

18. Finally, Bridgeport argues that the Commission made an unreasonable and artificial distinction between debt and equity in excluding Bridgeport's cost of equity from an examination of the degree to which Bridgeport is able to obtain adequate compensation in the current market. Bridgeport states that generating facilities are financed both by debt and equity and compensatory rates must include the cost of both. As a result, Bridgeport argues, the cost of equity for a non-leveraged facility is no less a cost of doing business than the cost of debt is for a leveraged facility like Milford. Further, Bridgeport argues that it lacks access to capital markets because it currently has a negative cash flow and that the exclusion of its return of and on capital results in the imposition of a confiscatory rate.

Answers

19. CT DPUC cites *Milford* to argue that the Commission's use of the facility costs test recognizes the Commission's responsibility to examine the unique characteristics of each applicant in determining whether an RMR agreement is appropriate. CT DPUC also argues that the facility costs test is consistent with Market Rule 1, which states that a facility needed for reliability may undertake financial arrangements to ensure that the facility will remain available.[22] Further, CT DPUC argues that the essential purpose of RMR agreements is as a last resort to ensure reliability, not to maximize generator profits or guarantee the recovery of sunk costs. The CT DPUC argues that an RMR agreement is a special tool to be applied in unique circumstances, not a traditional rate case where return of and on capital may be justified.

20. CT DPUC also disputes Bridgeport's definition of "adequate compensation." CT DPUC states that Bridgeport defines adequate compensation as inclusive of all costs, while CT DPUC interprets adequate compensation under Market Rule 1 as only those funds sufficient to prevent unit(s) from shutting down. CT DPUC states that Bridgeport's

[22] CT DPUC cites Market Rule 1, Appendix A, Exhibit 2, § 3.3.1(a).

interpretation of adequate compensation contradicts the Commission's historical view of RMR contracts as tools of last resort and allows a generator to switch at any time between the more profitable of cost-of-service or the competitive market.

21. CT DPUC supports, as consistent with Market Rule 1 and precedent, the Commission's requirement that a generator demonstrate that the RMR agreement is necessary to prevent deactivation. CT DPUC argues that Market Rule 1 specifically states that RMR Cost-of-Service Agreements are for "resources seeking authority permanently to shut-down and identified by the ISO as necessary for reliability."[23] CT DPUC states that Bridgeport's focus on the Commission's prior finding, that a unit is not required to submit a formal application for deactivation, is too narrow. Instead, CT DPUC argues that the Commission has always recognized that Market Rule 1 requires a unit to show that it will be unavailable without an RMR agreement. Finally, CT DPUC states that Bridgeport is arguing semantics in its claim that "unavailable" is materially different from "deactivate," as it is implicit in the Commission's criteria that without an RMR agreement, the unit would no longer be available to provide reliability services.

22. CT DPUC argues that the Commission's facility costs test neither prohibits Bridgeport from filing nor diminishes the value of Bridgeport's right to file a cost-based RMR agreement, pursuant to section 205 and Market Rule 1. In support, CT DPUC cites the July 19 Order in which the Commission stated that the use of the facility costs test does not prevent generators from including depreciation and rates of return as part of their filed cost of service rates.[24]

23. ISO-NE seeks to refute two implications from Bridgeport's rehearing request: (1) that the Commission should always ensure that suppliers are guaranteed to recover their costs; and (2) that a generator should be guaranteed to receive the higher of market-based or cost-based rates, at the expense of properly-functioning markets. If these premises are accepted, ISO-NE states, competitive markets will never develop and/or generators would be guaranteed to earn higher profits than they would under the traditional regulated model at the expense of ratepayers. In support, ISO-NE cites

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[23] CT DPUC cites Market Rule 1, Appendix A, section III.A.6.2.

[24] July 19 Order at P 36.

Milford to demonstrate that the Commission views RMR contracts as tools of last resort, appropriate in limited circumstances for facilities needed for reliability that have not earned "sufficient revenues to keep the facility in operation."[25]

24. ISO-NE also argues that Bridgeport makes two inaccurate assertions: that it has a legal right under the FPA to select either a cost-based or market-based rate as a general matter, and that a public utility has a statutory right to just and reasonable rates of its own design, including a cost-based rate. ISO-NE argues that Bridgeport has mischaracterized the Commission's holding in *SDG&E*[26] as supporting a principle that generators "dissatisfied" with market revenues may simply elect to pursue a cost-based rate. ISO-NE states that this holding did not relate to a general entitlement for any generator to seek a cost-based rate, but rather to a specific filing made by generators in California relating to the minimum load costs incurred due to California ISO's must-offer requirement.

25. ISO-NE states that because cost-of-service rates may not always be just and reasonable, the Commission has determined that out-of-market reliability contracts should be utilized only when the market cannot ensure reliability. Citing the ruling in *Elizabethtown Gas Co. v. FERC,*[27] ISO-NE argues that the Commission can approve a functioning competitive market that results in rates below those of a traditional cost-of-service regime. Further, ISO-NE notes that while Bridgeport has the right to make a cost-based rate filing, that fact does not require the Commission to approve the filing.

Commission Determination

26. We deny the requests for rehearing of both Bridgeport and the Connecticut Parties concerning RMR eligibility and the use of the facility costs test. The Commission has an obligation to examine the facts in each instance against the standard of section 205(a) of the FPA that all rates and charges demanded by any public utility for the sale of electric energy subject to the Commission’s jurisdiction shall be just and reasonable.[28] The Commission "consider[s] the *need* for these contracts, and the justness and

[25] *Milford* at P 40.

[26] 99 FERC ¶ 61,159 at 61,141 (2002).

[27] 10 F.3d 866, 870 (1993).

[28] July 19 Order at P 32.

reasonableness of the rates proposed therein, as they are filed."[29] The facility costs test is used only to assess the need for RMR contracts, contracts that the Commission will only approve when no other option exists.

27. The Commission has found that RMR contracts are tools of last resort because reliance on them can cause significant market distortions. Under RMR agreements, generators submit stipulated marginal operating cost bids and receive a cost-based revenue guarantee that is offset by energy market revenues earned. Market clearing prices and energy revenues determined with these stipulated bids may be lower than they would be absent the RMR revenue guarantee and exert pressure on the remaining generators to also seek RMR coverage. The concern is that this pressure to obtain RMR contracts could create a scenario in which RMR cost of service rates establish the recovery floor for generators in the market. With RMR contracts, market clearing prices and energy revenues understate the value of energy consumed and discourage efficient entry and demand response. Further, payments made to RMR generators outside of energy markets are not hedgeable and shift the risk of investment from investors back to consumers.

28. Bridgeport argues that despite having applied for and received authorization to provide generation services under market-based rates, it should have the ability to file for a cost-based rate at anytime, regardless of the regulations of Market Rule 1. Market Rule 1 provides that a generator needed for reliability may file for cost-based rates under section 205 of the FPA. We note that the Commission has not infringed upon Bridgeport's right to make this filing pursuant to section 205 of the FPA, however, Bridgeport’s participation as a generator in the competitive New England market makes Bridgeport subject to both the provisions of Market Rule 1 and to the inherent risk associated with cost recovery in a competitive market, where returns are not guaranteed.

29. The Commission does not take the position that designation of a need for reliability from ISO-NE guarantees Commission approval of an RMR contract, especially for a highly efficient merchant generator, capable of earning significant market revenues.[30] While we do not deny Bridgeport's right to file for a cost-based rate, the Commission has no obligation in a competitive marketplace to guarantee Bridgeport its full traditional cost-of-service. Rather, in a competitive market, the Commission is responsible only for assuring that Bridgeport is provided the *opportunity* to recover its

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[29] *Devon Power LLC*, 107 FERC ¶ 61, 240 at P 72 (2004) (Emphasis added).

[30] July 19 Order at P 32.

costs. The Commission's standard for RMR approval is the concern that absent an RMR contract, the facility will be unable to continue operation. By contrast, Bridgeport implies that the test of RMR eligibility should be whether a generator is able to recover its full, traditional cost-of-service at any given time.[31] We find no basis for a generator operating under market-based rates authority to claim that for it to remain available in a competitive market, it must receive energy revenues equivalent to a full cost-of-service, including depreciation and a return of and on capital. The Commission remains committed to comprehensively consider the need for these contracts, and the justness and reasonableness of the rates proposed.[32] This provides further safeguards against an unwarranted expansion of RMR contracts.

30. To assess whether the proposed RMR agreement is just and reasonable, the Commission needs to determine whether Bridgeport was denied the opportunity to recover its costs in the market. This facility costs assessment requires the Commission to examine Bridgeport's cost recovery throughout its operating history. While Bridgeport generally disputes the use of the facility costs test, it also mischaracterizes the July 19 Order. Specifically, the order sets for hearing the issue of whether the Facility has incurred losses each year since 1999. Bridgeport interpreted this as a request to prove losses in each of the years to pass the facility costs test. However, the Commission is not requiring that Bridgeport show six years of losses to demonstrate eligibility for an RMR contract. The purpose of this showing is to further develop the record in the instant filing by verifying Bridgeport's claims concerning historic cost recovery, as many of the costs included in the supplemental filing are not fully explained or supported. Evidence of actual revenues and costs will allow the Commission to determine the Facility's need for an RMR agreement to continue providing reliability service.

31. Bridgeport states that the standard is not, as the July 19 Order states, whether the proposed RMR agreement is necessary to prevent deactivation of the Facility, but, as Market Rule 1 states, whether the agreement is "necessary to ensure that the facility will be available."[33] The Commission clarifies that in using the term "deactivation" we were not attempting to establish a standard that is different than "necessary to ensure that the

[31] Bridgeport argues in its rehearing request at 19 that Bridgeport has a statutory right to file for a cost-based rate, "wholly aside" from whatever independent right it has under Market Rule 1.

[32] *Devon Power LLC*, 110 FERC ¶ 61,315 n.44 (2005).

[33] *Citing* Market Rule 1, section 3.3.1(C)(iii).

facility will be available." We consider these terms interchangeable. We note that the Commission has stated previously that generators do not need to initiate retirement procedures prior to negotiating an RMR agreement.

32. Bridgeport argues that the Commission made an unreasonable and artificial distinction between debt and equity in excluding Bridgeport's cost of capital from an examination of the degree to which Bridgeport is able to obtain adequate compensation in the current market. Bridgeport argues that the cost of equity for a non-leveraged facility like Bridgeport's is no less a cost of doing business than the cost of debt is for a leveraged facility like Milford's. In making this argument, Bridgeport confuses the standard for traditional cost of service rates and the standard for the facility cost test. In *Milford* we stated that, "the facility owners have not earned sufficient revenues in the market to keep the facility in operation." Milford could not continue operations if it ceased to pay its debts. Conversely, Bridgeport could continue operations without distribution of a return on equity. Therefore, the Commission properly found in the July 19 Order that "unlike Milford, Bridgeport is equity financed and, therefore, does not present the same issue concerning its ability to meet its financial obligations."[34]

33. With regard to Bridgeport's assertion that *SDG&E* supports Bridgeport's claim that sellers in functioning markets are entitled to charge cost-based rates, we disagree. ISO-NE is correct to state that the Commission's holding in that case did not relate to a general entitlement for any generator to obtain cost-based rates, but rather to a specific filing made by generators in California relating to the minimum load costs incurred due to California ISO's must-offer requirement.[35]

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[34] *Id*.

[35] In *SDG&E*, the Commission explained that generators should not be fully compensated for capacity reserve service under the must-offer obligation because a generator would receive some contribution to fixed costs when dispatched. 99 FERC ¶ 61,159 at 61,641. The Commission then stated that "[g]enerators who were dissatisfied with this finding regarding cost recovery of only minimum load status costs may propose cost-based rates for their generating units with cost support including a reasonable rate of return on investment that reflects the unique conditions in California." If Bridgeport demonstrates that the facility needs an RMR contract to remain available, then the cost-based rate it will obtain will include a reasonable rate of return on investment.

D. Cost of Service

34. Connecticut Parties argue that the Commission erred in accepting Bridgeport's cost-of-service approach that permits Bridgeport to recover all of its fixed and variable costs if the need for the proposed RMR Agreement is established. They state that because the Facility is new and highly efficient, it has not been significantly depreciated. Consequently, Connecticut Parties argue that by approving a traditional cost-of-service approach, the Commission will give Bridgeport a significant windfall. Connecticut Parties assert that awarding Bridgeport its full cost of service, including recovery of and on rate base, will permit Bridgeport to over-recover its costs during the presumptively short term of its RMR agreement compared to what it would earn as a merchant generator. They state that the Commission should either limit RMR cost recovery to going-forward costs or require a form of levelized costs that more nearly emulates the recovery of a merchant generator in a competitive market. Connecticut Parties assert that at a minimum, the Commission should set all issues related to the cost recovery methodology for hearing so that the parties can develop a record on the appropriate approach to address the unique circumstances of this case.

Answer

35. Bridgeport cites Market Rule 1 to support its claim that generators that are needed for reliability yet unable to recover their costs in the market have the right to a cost-of-service rate. Bridgeport also notes in its answer that the Commission has affirmed full cost of service recovery on at least six prior occasions. Further, Bridgeport notes that the Commission has refused to mandate the use of a levelized rate, typically including this as an issue for hearing. Bridgeport states that Connecticut Parties have raised no arguments to support a change in this policy.

Commission Determination

36. The Commission has historically recognized cost-of-service recovery for generators under RMR agreements. As we noted in *PSEG II*, this approach is appropriate under RMR agreements because providing only minimum, marginal and variable cost recovery to these units may not allow them to be maintained in a manner in which they can continue to operate reliably, and it would defeat the purpose of the contracts to ensure that the units are "available" to support reliability.[36] The determination of RMR eligibility (which employs the facility costs test) and any subsequent cost of service recovery (which may include return of and on investment) are distinct. Additionally, the

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[36] *PSEG Power Connecticut, LLC*, 110 FERC ¶ 61,441 (2005) (*PSEG II*) at P 21.

cost of service approach is appropriate for RMR agreements that mirror the *pro forma* Cost of Service Agreement in Market Rule 1, because any infra-marginal revenues or "other" revenues earned by these units in the market are credited against the monthly charges. Providing only variable and marginal costs to these units could also limit their ability to operate reliably as in-merit resources and impair their ability to earn market revenues to be credited against monthly reliability charges.

E. Termination Date

37. Connecticut Parties argue that the Commission's determination to allow Bridgeport's RMR agreement to expire when the locational installed capacity (LICAP) mechanism is implemented is arbitrary and capricious because LICAP could be deferred indefinitely. They argue that such an open-ended term is inconsistent with Market Rule 1, which provides that the term of RMR agreements "shall be one year from the effective date" and "shall provide for renewal for additional one-year terms so long as the ISO determines that the Resource continues to be an RMR Resource." Connecticut Parties argue that the Commission should set a specific end for the RMR agreement – one year from its effective date – in the event LICAP is not implemented as currently planned and, to the extent that any RMR agreement is then needed, require Bridgeport to justify its costs at that time, based on the more current experience that will then be available.

Answer

38. Bridgeport states that the Commission has previously affirmed at least six times that the proper termination date for RMR agreements is upon the implementation of LICAP. Also, Bridgeport states that since the Commission has deferred LICAP implementation to October 1, 2006 at the earliest, the need for RMR compensation will continue until an appropriate market mechanism is in place.

Commission Determination

39. The Commission will deny rehearing on this issue. The termination date issue has been addressed in several prior RMR orders, including in *PSEG II*. In the July 19 Order, we noted that the termination date was consistent with the termination date for other RMR agreements.[37] At this point, it has not been shown that an RMR contract is necessary to ensure that Bridgeport remains available to provide reliability services. If it is eventually demonstrated that an RMR contract is necessary for Bridgeport, then the RMR termination date will reflect the resolution of issues present in the current New

[37] *See* July 19 Order at P 63.

England capacity market. Regarding the Connecticut Parties' concerns of Bridgeport's potential for future overrecovery of costs due to changed circumstances, we note that Commission acceptance of the proposed RMR Agreement does not preclude the Connecticut Parties from filing for relief under section 206 should circumstances change.

F. Prior Rates and Revenues

40. Bridgeport argues that the Commission erred in considering Bridgeport's historic revenues in determining whether Bridgeport is presently entitled to a just and reasonable rate. Bridgeport asserts that the Commission must address the costs the filed tariff seeks to recover; it may not adjust or condition the current rate by taking into account a rate for service in the past; and it is prohibited from looking to the past when determining whether a utility's currently filed rate is just and reasonable.[38]

41. Bridgeport argues that to the extent historic revenues are used, those revenues must, at the very least, be limited to the period following April 25, 2003, the date of the order in which the Commission first found the existing New England market design to be unjust and unreasonable.[39]

Answers

42. ISO-NE states that while it takes no position on a specific time frame for consideration, it "strongly disagrees" with Bridgeport's notion that it can choose when to take a cost-based rate and when to take a market-based rate and that by making such choice, neither the parties nor the Commission can review revenues or earnings outside the period for which cost-based rates are sought.

43. CT DPUC states that Bridgeport's rehearing request based upon the Commission's consideration of historic revenues should be denied. CT DPUC states that Bridgeport's request appears to rest on the filed rate doctrine's corollary, the retroactive ratemaking doctrine. CT DPUC states that this doctrine holds that a utility may not set rates to recoup losses, nor may the Commission prescribe rates on that principle.[40] CT DPUC

[38] *Citing Associated Gas Distributors v. FERC*, 898 F.2d 809, 810 (D.C. Cir. 1990).

[39] *Devon Power, LLC*, 103 FERC ¶ 61,082, *order on reh'g*, 104 FERC ¶ 61,123 (2003).

[40] *Citing City of Piqua v. FERC*, 610 F.2d 950, 954 (D.C. Cir. 1979).

argues that neither the facts in this case nor the facility cost test invoke that doctrine because the Commission must determine whether Bridgeport has realized true losses to assess Bridgeport's availability for reliability purposes. CT DPUC states that Bridgeport acknowledges this standard in its filing where it maintains that its continued operation and availability for reliability purposes cannot be ensured.

44. CT DPUC argues that even if the retroactive ratemaking doctrine were to apply here, the cases Bridgeport cites do not aid the Commission's decision-making. Instead, CT DPUC states that a dynamic, market-based regime produces a range of rates, and a company's complete financial picture is necessary to assess its availability.

45. CT DPUC avers that the Commission should deny Bridgeport's request to restrict consideration of its historical performance to a limited period. CT DPUC cites the July 19 Order to argue that without a full and complete picture, the Commission will be unable to determine whether Bridgeport's historical returns satisfy the Commission's standard for RMR approval.

Commission Determination

46. The Commission will deny rehearing on this issue. We note that the historical cost recovery assessment (facility costs test) does not establish a cost of service RMR rate, and thus is not in conflict with the retroactive ratemaking doctrine. Rather, the facility costs test is used only to determine a generator's eligibility for a cost of service RMR rate. As noted previously, if a generator is found to be eligible for an RMR contract, the subsequent RMR cost of service rate is determined based upon the current cost of service for that generator, without consideration of prior cost recovery.

47. We find no basis for arbitrarily limiting the consideration of Bridgeport's historical cost recovery to the period following April 25, 2003. The purpose of the historical cost recovery assessment is to determine whether an RMR contract is necessary to keep Bridgeport available to provide reliability service. This consideration is not tied to any specific date, but to the general ability of Bridgeport to recover its costs. It is reasonable and expected in a competitive market that there will be periods where full cost recovery is not realized. In a competitive market, the Commission does not have an obligation to guarantee cost recovery, especially for a highly efficient merchant generator, capable of earning a significant portion of available market revenues. Instead, the Commission is responsible for assuring that Bridgeport is provided the opportunity to recover its costs.

The Commission orders:

The requests for rehearing are hereby denied.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.