UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

FPL Energy Marcus Hook, L.P. Docket No. ER05-316-000

ORDER ACCEPTING RATE SCHEDULE FOR FILING
AND ESTABLISHING HEARING AND
SETTLEMENT JUDGE PROCEDURES

(Issued January 31, 2005)

1. On December 8, 2004, FPL Energy Marcus Hook, L.P. (Marcus Hook) filed a proposed rate schedule specifying its revenue requirement for providing cost-based Reactive Support and Voltage Control from Generation Sources Service (Reactive Power Service) under the PJM Interconnection, L.L.C. (PJM) open access transmission tariff (OATT). For the reasons discussed below, we will accept the proposed rate schedule for filing and suspend it for a nominal period, to become effective February 1, 2005, subject to refund, and the establishment of hearing and settlement judge procedures. This order benefits customers by ensuring a timely inquiry into whether the proposed rate schedule is just and reasonable.

Background

2. Marcus Hook states that it is an indirect subsidiary of FPL Energy, formed for the purpose of owning and operating a 744 MW gas-fired cogeneration facility located in Marcus Hook, Pennsylvania (Marcus Hook Facility).[1] Marcus Hook states that the Marcus Hook Facility is a new facility and that the Reactive Power Service revenue requirement for the facility has never been included in any utility's rates.

[1] On December 27, 2001, in Docket No. EG02-27-000, the Commission granted Marcus Hook status as an exempt wholesale generator. On July 8, 2002, in Docket No. ER02-1903-000, the Commission granted Marcus Hook market-based rate authority for sales of energy, capacity, and ancillary services.

3. Marcus Hook states that on July 31, 2000, in Docket No. ER00-3327-000, PJM filed a revised methodology to determine charges for, and distribute revenues related to, Reactive Power Service. Marcus Hook states that that filing specifically addressed the issue of compensating non-transmission owner generators, such as Marcus Hook, for Reactive Power Service. Specifically, Schedule 2 of the PJM OATT provides that PJM shall pay each generation owner an amount equal to the generation owner's Commission-accepted monthly revenue requirement for Reactive Power Service. Marcus Hook explains that as a consequence it has filed its cost-based revenue requirement for its Reactive Power Service in order to establish a level of compensation it should receive under Schedule 2.

4. Marcus Hook states that it developed its revenue requirement using three cost components: (i) a fixed capability component, representing that portion of the plant fixed costs attributed to is proposed Reactive Power Service; (ii) a heating loss component, allowing for recovery of the increased generator heating losses resulting from producing Reactive Power; and (iii) a lost opportunity cost component, allowing for recovery of lost opportunity costs, as authorized under the PJM Operating Agreement.

5. Marcus Hook states that because it is a non-utility generator not generally subject to traditional rate regulation, it has incorporated a return on equity and overall rate of return based on a proxy, derived from the capital structure and return on equity for PECO Energy Company (PECO), the owner of the transmission system with which it is connected. Marcus Hook proposes an overall rate of return of 10.5 percent, including a return on equity of 12.6 percent, which it states was part of a settlement accepted by the Commission in a letter order dated December 16, 1998, in *PECO Energy Co.*, Docket No. ER97-3189-000. Marcus Hook adds that use of a transmission-owner cost of capital as a proxy is a conservative approach as applied to a competitive merchant plant such as Marcus Hook because, as a merchant provider, it faces greater market risks than those faced by a monopoly transmission service owner such as PECO.

6. With regard to heating losses, Marcus Hook states that when a generator produces Reactive Power, there are significant heating losses associated with the generator and the generator step-up transformer. Marcus Hook states these losses are the real power consumed to produce reactive power, and consequently, are costs directly attributable to the production of reactive power. Finally, Marcus Hook states that under PJM's OATT it is entitled to receive lost opportunity costs if PJM directs Marcus Hook to restrict its real power output to increase Reactive Power support to PJM.

7. In support of its filing, Marcus Hook states it has performed its cost calculations in accordance with *American Electric Power Service Corp.*[2] Marcus Hook claims that utilizing this methodology, the fixed capability component of its Reactive Power Service has an annual cost of $7,084,073.56 and that it's heating loss component has an annual cost of $392,905.58. Marcus Hook requests waiver of the 60-day prior notice requirement so that the proposed rate schedule becomes effective February 1, 2005.

Notice of Filing and Responsive Pleadings

8. Notice of Marcus Hook's filing was published in the *Federal Register*[3] with interventions and protests due on or before December 29, 2004. PJM filed a timely motion to intervene. In addition, a motion to intervene one-day out of time and protest were filed by Exelon Corporation (Exelon).

9. In its protest, Exelon challenges the overall revenue requirement claimed by Marcus Hook, given the amount of Reactive Power Service that will actually be produced by the Marcus Hook Facility and the actual costs Marcus Hook will incur in producing it. Exelon also questions whether the methodology identified by the Commission in *AEP* is appropriate in this case, given the type of facility at issue.

10. Exelon also argues that Marcus Hook's showing in support of its proposed rate of return is deficient because the proposed proxy components, *i.e.*, PECO's capital structure and capital costs, as developed in a 1998 settlement in Docket No. ER97-3189-000, have not been shown to be an appropriate proxy for the Marcus Hook Facility.

11. Exelon further argues that Marcus Hook's filing relies on unexplained totals for Operations Expense, Maintenance Expense, and Administrative and General Expenses, and fails to include cost data in conformance with the Uniform System of Accounts. Exelon also asserts that Marcus Hook's calculation of its proposed Fixed Charge Rate fails to recognize the existence of Accumulated Deferred Income Taxes (ADIT), contrary to the *AEP* methodology. Finally, Exelon challenges Marcus Hook's proposed power factor and allocation of costs to the generator portion of Marcus Hook's combustion turbine.

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[2] 80 FERC ¶ 63,006 at 65,071 (1997) (*AEP*).

[3] 69 Fed. Reg. 75,945 (2004).

12. On January 14, 2005, Marcus Hook filed an answer asserting, among other things, that in the case of a new merchant plant, *i.e.*, the facility at issue in this case, there are no deferred income tax credits or debits and thus none are reflected in its filing in the form of an ADIT adjustment.

Discussion

Procedural Matters

13. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,[4] the timely, unopposed motion to intervene submitted by PJM serves to make it a party to this proceeding. We will also grant Exelon's motion to intervene one-day out of time. Given its stated interests, the early stage of this proceeding and the lack of undue prejudice or delay, good cause exists to permit Exelon to be a party.[5] Rule 213(a) of the Commission's Rules of Practice and Procedure,[6] prohibits an answer to a protest, unless otherwise permitted by the decisional authority. We will accept Marcus Hook's answer because it has assisted us in our determinations, as discussed below.

Analysis

14. We agree with Exelon that Marcus Hook's proposed Reactive Power Service revenue requirement raises issues of material fact. We also find it appropriate that these issues be addressed in the hearing and settlement judge procedures ordered below. Our preliminary analysis of Marcus Hook's filing indicates that it has not been shown to be just and reasonable, and may be unjust, unreasonable, unduly discriminatory or preferential or otherwise unlawful.

15. Specifically, issues of material fact have been raised with respect to the following: (i) whether Marcus Hook's proposed revenue requirement is excessive given the amount of reactive power produced by the Marcus Hook Facility and the costs Marcus Hook incurs to produce it; (ii) whether reliance on PECO's overall rate of return and its individual components is appropriate; (iii) whether Marcus Hook has adequately supported for its Operations Expense, Maintenance Expense, and Administrative and

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[4] 18 C.F.R. § 385.214 (2004)

[5] *See* 18 C.F.R. § 385.214(d) (2004).

[6] *Id.* at § 385.213(a)(2).

General Expenses; (iv) whether Marcus Hook has failed to include cost data required by the Commission's Uniform System of Accounts; (v) whether Marcus Hook's proposed rate should reflect an ADIT adjustment; (vi) whether Marcus Hook's proposed power factor has been justified; and (vi) whether Marcus Hook has properly allocated its costs to generator portion of Marcus Hook's combustion turbine. Accordingly, we will accept Marcus Hook's proposed rate schedule for filing, suspend it for a nominal period, to become effective February 1, 2005, subject to refund, and set it for hearing and settlement judge procedures as ordered below. We will grant waiver of the notice requirement to permit Marcus Hook's proposed rate schedule to become effective on that date.[7]

16. We will reject Exelon's request that the appropriateness of applying the *AEP* methodology should be set for hearing. As we have previously determined, and reiterate here, *all* generators seeking to recover a Reactive Power Service revenue requirement based on actual cost data are required to use the methodology employed in *AEP*.[8] We also reject Exelon's request that we summarily rule on Exelon's argument that an ADIT adjustment be required in this case. Marcus Hook asserts in its answer, and we agree, that an adjustment in this case may not be required to the extent that the facility at issue has not commenced operations. Thus, we will set this issue for hearing.

17. While we are setting the above-noted matters for a trial-type evidentiary hearing, we encourage the parties to make every effort to settle their disputes before hearing procedures are commenced. To aid the parties in their settlement efforts, we will hold the hearing in abeyance and direct that a settlement judge be appointed, pursuant to Rule 603 of the Commission's Rules of Practice and Procedure.[9] If the parties desire, they may, by mutual agreement, request a specific judge as a settlement judge in the proceeding;

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[7] *See Central Hudson Gas and Elec. Corp.*, 60 FERC ¶ 61,106, *reh'g denied*, 61 FERC ¶ 61,089 (1992).

[8] *See* WPS Westwood Generation, L.L.C., 101 FERC ¶ 61,290 (2002).

[9] 18 C.F.R. § 385.603 (2004).

otherwise the Chief Judge will select a judge for this purpose.[10] The settlement judge shall report to the Chief Judge and the Commission within 60 days of the date of this order concerning the status of settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions or provide for the commencement of a hearing by assigning the case to a presiding judge.

The Commission orders:

(A) The proposed rate schedule is hereby accepted for filing, and suspended for a nominal period, to become effective February 1, 2005, subject to refund, as discussed in the body of this order. Waiver of the notice requirement is hereby granted.

(B) 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 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 the proposed rate schedule. However, the hearing will be held in abeyance to provide time for settlement judge procedures, as discussed in paragraphs (C) and (D) below.

(C) Pursuant to Rule 603 of the Commission's Rules of Practice and procedure, 18 C.F.R. § 385.603 (2004), the Chief Administrative Law Judge is hereby directed to appoint a settlement judge in this proceeding within fifteen (15) days of the date of this order. Such settlement judge shall have all powers and duties enumerated in Rule 603 and shall convene a settlement conference as soon as practicable after the Chief Judge designates the settlement judge. If the parties decide to request a specific judge, they must make their request to the Chief Judge by telephone within five (5) days of the date of this order.

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[10] If the parties decide to request a specific judge, they must make their request to the Chief Judge by telephone at 202-502-8500 within five days of the date of this order. The Commission's website contains a listing of Commission judges and a summary of their background and experience (www.ferc.gov - click on Office of Administrative Law Judges).

(D) Within sixty (60) days of the date of this order, the settlement judge shall file a report with the Chief Judge and with the Commission on the status of the settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions, if appropriate, or assign this case to a presiding judge for a trial-type evidentiary hearing, if appropriate. If settlement discussions continue, the settlement judge shall file a report at least every 30 days thereafter, informing the Chief Judge and the Commission of the parties' progress toward settlement.

(E) If settlement judge procedures fail, and a trial-type evidentiary hearing is to be held, a presiding administrative law judge, to be designated by the Chief Administrative Law Judge, shall convene a prehearing conference in this proceeding, to be held within approximately fifteen (15) days of the date on which the Chief Judge designates the presiding judge, in a hearing room of the Federal Energy Regulatory Commission, 888 First Street, N.E. Washington, D.C. 20426. Such conference shall be held for the purpose of establishing a procedural schedule. The presiding administrative law 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.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.