

112 FERC ¶ 61,169
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Midwest Independent Transmission
System Operator, Inc.

Docket Nos. ER05-1083-000
ER04-691-045

Public Utilities With Grandfathered Agreements
in the Midwest ISO Region

Docket No. EL04-104-043

ORDER REJECTING COMPLIANCE FILING AND TARIFF SHEETS

(Issued August 5, 2005)

1. On February 18, 2005, the Commission accepted for filing a settlement agreement among the Midwest Independent Transmission System Operator, Inc. (Midwest ISO) and the transmission owners within its region (Balancing Authority Settlement).¹ The Balancing Authority Settlement allocated between the Midwest ISO and the control areas – now called Balancing Authorities – within its footprint the functional responsibilities, costs and liability associated with the Midwest ISO's role as energy market operator. In today's order, we will reject the Midwest ISO Transmission Owners' (Midwest ISO

¹ *Midwest Independent Transmission System Operator, Inc.*, 110 FERC ¶ 61,177 (Balancing Authority Settlement Order), *clarification granted*, 111 FERC ¶ 61,367 (2005).

TOs)² filing to comply with the Balancing Authority Settlement Order, as well as a concurrent rate filing under section 205 of the Federal Power Act (FPA).³

I. Background

2. In a July 25, 2003 filing (July 25 Filing), the Midwest ISO filed a proposed Transmission and Energy Markets Tariff (TEMT) pursuant to section 205 of the FPA. The July 25 Filing proposed to implement day-ahead and real-time energy markets, as well as a financial transmission rights market, within the Midwest ISO region. The new energy markets would operate under the TEMT, which the Midwest ISO proposed as a replacement for its open access transmission tariff. The July 25 Filing met with numerous protests, and following a stakeholder vote, the Midwest ISO filed a motion to withdraw it.

3. The Commission granted the Midwest ISO's motion to withdraw the proposal. It also provided, on an advisory basis, guidance on a number of issues raised in the July 25 Filing in order to better enable the Midwest ISO to revise and re-file the TEMT.⁴ Among other things, the Commission advised the Midwest ISO and stakeholders to adopt

² The transmission owners are: Ameren Services Company, as agent for Union Electric Company d/b/a Ameren UE, Central Illinois Public Service Company d/b/a AmerenCIPS, and Central Illinois Light Co. d/b/a Ameren Cilco; American Transmission Systems, Inc., a subsidiary of FirstEnergy Corp.; Aquila, Inc. d/b/a Aquila Networks (f/k/a Utilicorp United, Inc.); Cinergy Services, Inc. (for Cincinnati Gas & Electric Co., PSI Energy, Inc., and Union Light Heat & Power Co.); City Water, Light & Power (Springfield, Illinois); Great River Energy; Hoosier Energy Rural Electric Cooperative, Inc.; International Transmission Company; Indianapolis Power & Light Company; LG&E Energy Corporation (for Louisville Gas and Electric Co. and Kentucky Utilities Co.); Michigan Electric Transmission Company, LLC; Minnesota Power (and its subsidiary Superior Water, L&P); Montana-Dakota Utilities Co.; Northern Indiana Public Service Company; Northern States Power Company and Northern States Power Company (Wisconsin), subsidiaries of Xcel Energy Inc.; Northwestern Wisconsin Electric Company; Otter Tail Corporation d/b/a Otter Tail Power Company; Southern Illinois Power Cooperative; Southern Indiana Gas & Electric Company (d/b/a Vectren Energy Delivery of Indiana); and Wabash Valley Power Association, Inc.

³ 16 U.S.C. § 824d (2000).

⁴ See *Midwest Independent Transmission System Operator, Inc.*, 105 FERC ¶ 61,145, *reh'g dismissed*, 105 FERC ¶ 61,272 (2003).

the North American Electric Reliability Council (NERC) Reliability Functional Model (Functional Model) as a basis for discussions on the allocations of responsibilities for reliable market and power system operations.⁵ The Commission also advised that the revised TEMT “state clearly the current responsibilities under each of these categories and the proposed changes in those responsibilities.”⁶

4. The Midwest ISO filed a revised TEMT proposal on March 31, 2004. Section 38.6 of the proposed TEMT assigned responsibility to the Midwest ISO, control area operators, transmission owners, transmission operators and generation owners for three primary roles with authority to carry out reliability functions – Reliability Authority, Balancing Authority and Interchange Authority.⁷ Numerous intervenors filed protests that sought further clarification of the Midwest ISO’s proposed division of functions between itself and other entities within its footprint.

5. The Commission found that the proposed TEMT appropriately used the NERC Functional Model as a basis for defining roles and responsibilities within the Day 2 energy markets,⁸ and established settlement judge proceedings to address a number of unresolved issues surrounding the allocation of functions between the Midwest ISO and the control areas.⁹ The parties filed an Offer of Settlement, which featured a Balancing Authority Agreement as its principal component, and the Commission accepted the settlement in the Balancing Authority Settlement Order.

⁵ *See id.* at P 46.

⁶ *Id.*

⁷ Reliability Authority refers to performing the functions of ensuring real-time operating reliability, performing transmission security analysis, approving generation and transmission outages, and performing regional and inter-regional coordination. The term “Balancing Authority” is used instead of “Control Area Operator” to reflect the new NERC Functional Model. The Balancing Authority maintains load-resource balance within the Balancing Authority Area. Interchange Authority relates among other things to the responsibility to serve as Scheduling Agent. The TEMT identifies the Midwest ISO as both transmission service provider and Interchange Scheduling Agent.

⁸ *See Midwest Independent Transmission System Operator, Inc.*, 108 FERC ¶ 61,163 at P120-21 (TEMT II Order), *order on reh’g*, 109 FERC ¶ 61,157 (2004)(TEMT II Rehearing Order).

⁹ *See id.* at P 137-38.

6. The Balancing Authority Settlement found that it was reasonable for Balancing Authorities to recover the costs of implementing the Balancing Authority Agreement.¹⁰ As further detailed below, the order approved a new schedule to the TEMT that would permit the Balancing Authorities to recover such costs “together with, and in the same manner as, Schedule 17 costs.”¹¹ Further, the Balancing Authority Settlement Order accepted the Midwest ISO TOs’ offer to provide additional accounting detail to further clarify their proposal to recover Balancing Authority costs under the terms of the Balancing Authority Agreement, and required them to make such a filing.¹²

II. The Midwest ISO TOs’ Filing

7. The Midwest ISO TOs submitted a compliance filing on June 6, 2005, as amended on June 10 and 20, 2005. The filing includes revisions to Schedules 1 and 24 of the TEMT, together with a newly-proposed Schedule 24-A. The revised Schedule 24 includes additional accounting detail for cost recovery, as the Balancing Authority Settlement Order directed. Schedule 24-A, which the Midwest ISO TOs propose to make effective on June 1, 2006, provides detail on the types of costs to be recovered (such as labor costs) and the accounting for such costs. The Midwest ISO TOs seek immediate action on their filing so that the Balancing Authorities can begin to engage in efforts to implement accounting changes to prevent the double recovery of costs. The Midwest ISO TOs state that these changes will take effect immediately; the changes will be reflected in booked amounts from 2005; and the formula to take effect on June 1, 2006 will depend on those booked amounts.

8. In addition, the filing contains a change in rate design that the Midwest ISO TOs submit pursuant to section 205 of the FPA. As described below, the Midwest ISO TOs propose, through Schedule 24-A, to change from a regional rate design to a license-plate, zonal rate design. This change requires a modification to the Schedule 24 language that the Commission accepted in the Balancing Authority Settlement Order. The Midwest

¹⁰ Balancing Authority Settlement Order at P 59.

¹¹ *Id.* at P 16.

¹² Balancing Authority Settlement Order at P 54, 59. Subsequently, the Commission twice extended the deadline for the Midwest ISO TOs to make this compliance filing. *See Notice of Extension of Time*, Docket Nos. ER04-691-002 and EL04-104-002 (Mar. 29, 2005); *Errata Notice*, Docket Nos. ER04-691-002 and EL04-104-002 (Mar. 31, 2005); *Notice of Further Extension of Time*, Docket Nos. ER04-691-002 and EL04-104-002 (May 9, 2005).

ISO TOs represent that more than 75 percent of the Balancing Authorities have approved the tariff change, as the Balancing Authority Agreement requires.

III. Notice, Interventions and Protests

9. Notice of the Midwest ISO TOs' filing was published in the *Federal Register*, 70 Fed. Reg. 35,420 (2005), with interventions and protests due on or before June 27, 2005. Wisconsin Electric Power Company filed an intervention. Basin Electric Power Cooperative (Basin) and WPS Resources Corporation (WPS Resources) filed motions to intervene and protests, as detailed below. The Midwest ISO TOs filed an answer to the protests, and WPS Resources filed an answer to the Midwest ISO TOs' answer.

IV. Discussion

A. Procedural Matters

1. Interventions and Answers to Protests

10. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2005), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

11. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2005), prohibits an answer to a protest or an answer unless otherwise ordered by the decisional authority. We will accept the Midwest ISO TOs' and WPS Resources's answers because they have provided information that assisted us in our decision-making process.

2. The Midwest ISO TOs' Section 205 Filing

a. Background

12. The Midwest ISO TOs' filing includes both a compliance filing and a rate filing under section 205 of the FPA. The proposed Schedule 24-A adopts a license-plate, zonal rate design methodology, and the revisions to Schedule 24 reference that new methodology.

b. Protests and Answers

13. WPS Resources complains that the Balancing Authority Settlement Order required the Midwest ISO TOs to make specific, limited modifications to their cost recovery proposal – for example, to provide more detail concerning the treatment of costs to ensure that there is no double recovery. It alleges that the Midwest ISO TOs exceeded

the scope of these requirements by modifying the basis on which Balancing Authority costs are to be recovered. The Midwest ISO TOs' filing, WPS Resources claims, violates Commission policy because it mixes a compliance filing with a new rate filing under section 205 of the FPA. WPS Resources urges the Commission to reject the proposed modification and require the Midwest ISO TOs to retain the regional cost recovery provision that they included in their original filing.

14. The Midwest ISO TOs answer that they submitted the June 6 filing as both a compliance filing and a section 205 filing because the approach that they adopted involved a change in the approved rate design and a modification to Schedule 1 of the TEMT. While the Midwest ISO TOs acknowledge that elements of their proposal exceed the compliance requirements of the Balancing Authority Settlement Order, they argue that parties have combined section 205 filings with compliance filings on other occasions, and that none of the cases that WPS Resources cites suggest that the Midwest ISO TOs have violated any policy by doing so.

c. Discussion

15. The Commission generally does not permit public utilities to submit rate filings under section 205 of the FPA together with compliance filings.¹³ The Commission has, however, accepted a section 205 filing in combination with a compliance filing when the compliance directives in question warranted changes to other, related tariff provisions.¹⁴ The tariff changes proposed here are closely and plainly related to the Commission's compliance requirements. In addition, the proposed rate changes show a common factual nexus with the compliance filing and do not undo or contravene the compliance requirements. As such, on these facts we will consider the section 205 filing in this proceeding.

B. Cost Recovery Under Schedules 1, 17, 24 and 24-A

1. The Midwest ISO TOs' Proposal

16. As applicable here, Balancing Authorities may recover their costs under Schedules 1 or 24 of the TEMT.

¹³ See, e.g., *ISO New England, Inc.*, 99 FERC ¶ 61,070 at 61,322-23 (2002).

¹⁴ See *New England Power Pool*, 85 FERC ¶ 61,141 at 61,550 (1998), *order on reh'g*, 87 FERC ¶ 61,043, *reh'g denied*, 88 FERC ¶ 61,276 (1999).

17. Schedule 1 provides that scheduling, system control and dispatch service associated with the Midwest ISO is to be provided directly by the Midwest ISO, and that transmission customers must purchase it from the Midwest ISO. However, to the extent that the control area operators perform this service for the Midwest ISO, charges collected under Schedule 1 represent a pass-through of the control area operators' costs.¹⁵ Cost recovery under Schedule 1 is made "at a single, system-wide rate."¹⁶

18. The Balancing Authority Settlement Order approved a new schedule to the TEMT (Schedule 24), to provide a mechanism for Balancing Authorities to recover costs that related to the implementation of the Balancing Authority Agreement. Under the new schedule, all control area operators shall recover costs incurred as a result of implementing the energy markets and services pursuant to the TEMT, including: (1) daily operation and maintenance costs; (2) administrative and general costs; (3) capital costs; and (4) costs for systems-in-place, training, and from the performance of obligations imposed by the TEMT. All costs to be recovered must relate to control area actions in implementing, or performing obligations under, the TEMT and cannot include costs recovered under the TEMT or otherwise reimbursed by the Midwest ISO. Because the Balancing Authority costs were related to implementation of the energy markets, the Commission approved these costs to be recovered together with, and in the same manner as, Schedule 17 costs.¹⁷

19. The Midwest ISO TOs note that the current Schedule 24 includes a provision that reflects the region-wide rate design of Schedule 17, and they argue that the cost shifts associated with the regional rate design create "too many issues."¹⁸ They thus have

¹⁵ See TEMT, Schedule 1, Second Revised Sheet No. 851.

¹⁶ TEMT, Schedule 1, Second Revised Sheet No. 852.

¹⁷ Schedule 17, Energy Market Support Administrative Service Costs, provides for the Midwest ISO to recover all costs related to its energy markets including costs associated with market modeling and scheduling functions, market bidding support, locational marginal pricing support, market settlements and billing, market monitoring functions, and enabling least-cost, security-constrained dispatch. Schedule 17 specifies that each market participant shall be billed for a share of the Energy Market Support Administrative Service Cost Recovery Adder, depending on the number of megawatts that market participants has injected into, or withdrawn from, the Midwest ISO transmission system in that month. The rate is, therefore, uniform for all market participants in the region.

¹⁸ Midwest ISO TOs Transmittal Letter at 7 (Jun. 6, 2005).

agreed, and propose, to modify Schedule 24 to change from a postage-stamp, or regional rate design (like that of Schedule 17) to a license-plate, zonal rate design, and to add a new Schedule 24-A. Schedule 24-A provides that Balancing Authorities may recover five categories of labor costs associated with implementing the Balancing Authority Agreement, and that Balancing Authorities must directly assign labor costs if they are able to do so. Each Balancing Authority must choose whether to account for labor expenses related to implementation of the Balancing Authority Agreement under Account No. 556 or Account No. 561. These costs include salary and, if the Balancing Authority can establish that there is no duplication of cost recovery, salary-related expenses such as insurance and benefits. If a Balancing Authority contracts for these services with a third party, it may include the costs paid to the third party; however, if the third party is another Balancing Authority subject to Schedule 24, then it must not include costs associated with the services it provides to the Balancing Authority that engages its services.¹⁹

20. The Midwest ISO TOs state that their proposed language for Schedules 24 and 24-A provides for a formula that reflects actual booked costs from the prior year to be collected beginning on June 1, 2006. Under the formula for computing the zonal rate, the Balancing Authority costs from the prior year, less revenue credits, are divided by the annual billing determinants to derive the annual rate. Monthly, daily and hourly rates are derived from the annual rate.

21. Charges are derived on a zonal basis, with generators injecting into the zone and loads within the zone paying the applicable zonal charges. Generators from outside the Midwest ISO, and entities moving power out of the Midwest ISO, will pay an average rate. The Midwest ISO TOs state that this is a standard rate formula that tracks the methodology and timing of Attachment O; thus, they state the proposed mechanism is reasonable. However, in addition to establishing the new zonal rate under Schedule 24, Schedule 24-A offers Balancing Authorities a choice as to whether they book the labor costs associated with energy market implementation under Schedule 24 (a zonal rate design) or Schedule 1 (a regional rate design).²⁰

¹⁹ See Schedule 24-A, section I, Original Sheet No. 1050S.02.

²⁰ Schedule 1 provides that scheduling, system control and dispatch service associated with the Midwest ISO is to be provided directly by the Midwest ISO, and that transmission customers must purchase it from the Midwest ISO. However, to the extent that the control area operators perform this service for the Midwest ISO, charges collected under Schedule 1 represent a pass-through of the control area operators' costs. Cost recovery under Schedule 1 is collected pursuant to a single, system-wide rate based

(continued)

22. Additionally, the Midwest ISO TOs propose to modify Schedule 1 to provide that costs recovered under Schedule 24 via a sub-account to Account No. 561 shall not be included in the costs associated with Schedule 1. Finally, the Midwest ISO TOs state that as a transitional mechanism, the formula will rely on data from April 1, 2005 to December 31, 2005 for the first rate period.

2. Protests and Answers

23. WPS Resources and Basin argue that the filing is unduly discriminatory because it allows each Balancing Authority to choose between cost recovery under Schedule 1 or Schedule 24. Both companies contend that, as a result, loads in zones where Balancing Authority costs are recovered will pay a disproportionate share of Balancing Authority costs. WPS Resources and Basin indicate that all entities across the region that pay Balancing Authority costs will pay their proportionate share of the costs that are recovered under Schedule 1, because Schedule 1 costs are allocated on a regional basis. They believe, however, that entities located in zones where Balancing Authority costs are recovered under Schedule 24 will pay both the regionally-allocated Schedule 1 Balancing Authority costs and all of the Balancing Authority costs that are incurred in their own zone. Basin indicates that the problem of disproportionate cost recovery particularly affects entities like itself, which inject power from outside the Midwest ISO.

24. WPS Resource and Basin aver that the only difference between a customer that will pay only Schedule 1 Balancing Authority costs and one that will pay both Schedule 1 and Schedule 24 Balancing Authority costs is the zone in which those customers are located. This, WPS Resources concludes, does not justify the different exposure to Balancing Authority costs.

25. Next, WPS Resources submits that the cost recovery option is unjust and unreasonable because it does not comply with the TEMT II Order or the Balancing Authority Agreement, and because it unnecessarily complicates the process of auditing Balancing Authority costs and charges to ensure that no double recovery occurs. WPS Resources alleges that, because the Commission required the Midwest ISO and the control area operators to adopt the NERC Functional Model and to develop a mechanism for the recovery of Balancing Authority costs, the Commission implicitly recognized that

on all costs booked to FERC Account No. 561 less the sum of all charges assessed under this schedule to firm transactions of less than one year, including non-firm transactions, divided by the Attachment O divisor for Drive-Out and Drive-Through Transmission Service. Such rate is calculated and put into effect on June 1 of each year, based on data for the prior calendar year.

Balancing Authority costs were no longer recoverable under Schedule 1. Because the cost recovery option permits recovery of costs under Schedule 1, Schedule 24 or both, however, WPS Resources argues that it violates the TEMT II Order.

26. WPS Resources also states that permitting Balancing Authority cost recovery under Schedule 1 is inconsistent with the Balancing Authority Agreement. It recalls that the Balancing Authority Agreement provided Schedule 24 to enable Balancing Authority cost recovery separate from the recovery of non-Balancing Authority control area costs under Schedule 1. WPS Resources also states that, in their compliance filing to the TEMT II Order, the Midwest ISO TOs stated that there was no tariff mechanism for the recovery of Balancing Authority costs, that a separate rate schedule was needed to provide for cost recovery, and that all Balancing Authority costs were to be recovered under Schedule 24, per the schedule's own terms. The Commission should not, WPS Resources adds, be persuaded by suggestions that the Midwest ISO TOs intended to permit Balancing Authority cost recovery under either Schedule 1 or Schedule 24 when they filed the Balancing Authority Agreement. WPS Resources argues that, by admitting in their earlier compliance filing that a mechanism was needed to prevent under-recovery of Balancing Authority costs, the Midwest ISO TOs asserted that those costs should no longer be recovered under Schedule 1; otherwise, a separate Schedule 24 would not have been necessary.

27. WPS Resources further argues that the cost recovery option makes cost recovery less transparent and more complex to audit, and that the Midwest ISO TOs' compliance filing does not comply with the Balancing Authority Settlement Order's requirements regarding transparency and audits. WPS Resources states that the cost recovery option allows control area operators to collect Balancing Authority costs under either Schedule 1 or Schedule 24, and that it does not prohibit them from varying the method from year to year. According to WPS Resources, tracking Balancing Authority costs in order to determine whether they are over-collected would become an "auditing nightmare" if the Midwest ISO TOs' proposal is adopted.²¹

28. WPS Resources argues that all recoverable Balancing Authority costs should be recovered only on a regional basis, through a single schedule. It states that the Commission should require control area operators to: (1) identify costs collected under Schedule 1, or any other schedule, that are currently incurred to perform the Balancing Authority functions; (2) modify their rates to eliminate those costs from any schedule other than Schedule 24; (3) recover those costs pursuant to Schedule 24 only; and (4) recover those costs on a regional, not a zonal, basis. Further, WPS Resources

²¹ WPS Resources Protest at 15.

advocates that the Commission monitor the process of correcting the errors in the Balancing Authority Agreement provisions through the settlement process rather than allow the Midwest ISO TOs to continue to try to achieve a just and reasonable result. It states that the Midwest ISO TOs' efforts to comply with the Balancing Authority Settlement Order so far have made worse the issues that the Commission ordered the Midwest ISO TOs to resolve, and that the Balancing Authority Agreement may not be modified without the approval of three-quarters of the Balancing Authorities or a Commission finding that the modification is in the public interest.

29. Basin suggests that the Commission do one of two things: (1) require the Midwest ISO TOs to recover their Schedule 24 costs on a regional basis; or (2) require that all control area operators move all of their Balancing Authority costs from Schedule 1 to Schedule 24. The former option would make it irrelevant whether Balancing Authority costs were recovered under Schedule 1 or under Schedule 24 (because all recovery would be regional); under the latter option, all Balancing Authority costs would be recovered on a zonal basis.

30. WPS Resources and Basin each contend that the Midwest ISO TOs' proposed Schedule 24-A incorporates rate design errors that, according to WPS Resources, will make it impossible to administer correctly. It notes that the Annual Zone Rate (AZR) is expressed in dollars per megawatt-hour, but the formula rate also states that zonal rates will be calculated by dividing the AZR by 12 (for monthly service), 52 (for weekly service), 365 (for daily service) or 8760 (for hourly service). Basin makes the same observation with respect to the zonal and average rates for generators located outside the Midwest ISO. Both entities argue that the division does not make sense, and WPS Resources adds that the only rate that should be developed in this manner is a rate expressed in dollars per megawatt-hour year. Accordingly, WPS Resources and Basin urge the Commission to direct the Midwest ISO TOs to correct their rate design by eliminating the references to monthly, weekly, daily and hourly rates. In their answer, the Midwest ISO TOs state that they will rectify any problem that the Commission finds with the units used in the formulas.

31. The Midwest ISO TOs state that negotiating the proposal framed in the June 6 filing required three and a half months of discussions. They argue that it is "virtually inconceivable" that Commission-sponsored settlement proceedings would yield greater consensus than what the parties have already achieved. The Midwest ISO TOs also believe that Commission-sponsored settlement discussions likely would involve reopening issues that are already settled. They state that the circumstances here do not warrant this action.

32. The Midwest ISO TOs also indicate that their proposal incorporates a choice between cost recovery under Schedule 1 and under Schedule 24 because some Balancing Authorities preferred to continue recovering costs as they have in the past, *i.e.*, under Schedule 1. The Midwest ISO TOs argue that, because the revised Schedule 1 states that amounts recovered under Schedule 1 must not include amounts recovered under Schedule 24, load in zones where Balancing Authority costs are recovered under Schedule 24 will not pay a disproportionate share of Balancing Authority costs. The Midwest ISO TOs state that the difference between what the customer would pay if the relevant Balancing Authority recovers its Balancing Authority costs through Schedule 24 should not differ appreciably from the amount the customer would pay if the Balancing Authority continues to recover its costs through Schedule 1. The same, they add, is true for generators outside the Midwest ISO paying the average annual rate.

33. Next, the Midwest ISO TOs state that their proposal does not violate the TEMT II Order or the Balancing Authority Agreement. They argue that the TEMT II Order recognizes that the Midwest ISO and the Midwest ISO TOs must address cost issues resulting from the new allocation of functional responsibilities, but that it does not state that Balancing Authority costs cannot be collected under Schedule 1. The Midwest ISO TOs further argue that the proposal is not inconsistent with the Balancing Authority Agreement because it is a modification to that agreement that the Balancing Authorities passed by a three-fourths vote. Finally, the Midwest ISO TOs argue that their proposal does not violate the Balancing Authority Settlement Order's requirement that the proposal be transparent and auditable because any Balancing Authority costs recovered under Schedule 24 must be placed in specific sub-accounts.

34. In its answer, WPS Resources argues that customers in zones where Balancing Authorities recover their costs under Schedule 24 will pay two and a half times more than customers in zones where Balancing Authorities recover their costs under Schedule 1. Regardless of how many control areas are included in a region, WPS Resources says, if even one control area in a zone recovers its costs on a zonal basis, customers in that control area will pay increased costs. WPS Resources attaches an appendix to its answer that contains formulas for allocating recovered costs, and a numerical example of what customers would pay if three utilities in a zone recovered their Balancing Authority costs under Schedule 1, Schedule 24, or a combination of the two.

35. WPS Resources argues that the Midwest ISO stakeholder process is, increasingly, one in which the Midwest ISO TOs present proposals to the other stakeholders, who have little ability to influence the Midwest ISO TOs to modify their positions. WPS Resources states that it participated actively in the negotiations concerning cost recovery options, but that it abstained from the final vote because the negotiations did not achieve what WPS Resources would consider a just and reasonable result.

3. Discussion

36. In the Balancing Authority Settlement Order, we accepted the concept of a cost recovery mechanism for Balancing Authorities to recover costs incurred under the Balancing Authority Agreement.²² The Balancing Authority Settlement filing stated that those costs would be collected “in the same manner as costs recovered under Schedule 17”²³ – *i.e.*, on a regional basis, using postage-stamp pricing. The Commission reviewed the proposal under the “just and reasonable” standard of FPA section 205 because the proposal was presented in the form of a contested settlement.²⁴ The Commission conditionally approved the settlement, ordered a compliance filing to implement the proposal, and required the Midwest ISO TOs to submit accounting details. Instead of implementing the Commission’s requirements through a compliance filing, the Midwest ISO TOs made a new section 205 filing to govern recovery of these costs. Because they chose to submit a new proposal, the Midwest ISO TOs bear the burden to establish that it is just and reasonable.²⁵ As we discuss below, we find that they have not met that burden. The fact that a three-quarters majority of Balancing Authorities have agreed to change the Balancing Authority Agreement and to propose these amendments to the TEMT, although desirable (and, in the case of the Balancing Authority Agreement, necessary), does not, in and of itself, ensure the justness and reasonableness of the proposal. Ultimately, that responsibility rests with the Commission.²⁶

37. In the section 205 filing, the Midwest ISO TOs propose to change the cost recovery methodology of Schedule 24 from a regional basis to a zonal basis. In addition, under proposed Schedule 24-A, the Midwest ISO TOs propose to permit Balancing Authorities a choice between booking labor-related costs to Account No. 561 or Account No. 556. The result, as protestors indicate, would allow Balancing Authorities to choose whether to recover costs on a regional basis (under Schedule 1) or on a zonal basis (under

²² Balancing Authority Settlement Order at P 59.

²³ Explanatory Statement at 7, Docket Nos. ER04-691-002 and EL04-104-002 (Oct. 5, 2004).

²⁴ *See Mobil Oil Corp. v. FPC*, 417 U.S. 283, 314 (1974).

²⁵ 16 U.S.C. § 824d (2000).

²⁶ *See* 16 U.S.C. § 824d(b) (2000); *Pennsylvania Electric Co. v. FERC*, 11 F.3d 207, 210 (D.C. Cir. 1993).

proposed Schedule 24), and to alternate between the two schedules at their discretion.²⁷ We find a number of problems with the proposal.

38. The Midwest ISO TOs have not clearly explained their rationale for moving from a regional cost recovery methodology under Schedule 17 to a zonal cost recovery methodology. They merely state that the regional cost recovery methodology of Schedule 17 created “too many issues.”²⁸ The Midwest ISO TOs do not explain, however, why the regional rate design reflected in Schedule 17 creates “issues,” or even identify what the alleged issues are. Merely stating that there are problems with the current cost recovery methodology does not establish that the proposed substitute is just and reasonable. Nor have the Midwest ISO TOs explained why providing a choice to permit recovery under Schedule 1, which also employs a regional rate design, does not lead to the same problems allegedly created by Schedule 17.

39. The Midwest ISO TOs’ second justification for the proposal – which is that it is important to allow the Balancing Authorities the option to choose accounts and cost recovery methodologies in order to avoid under-recovery of costs²⁹ – is also insufficient to establish that the proposal is just and reasonable. We agree with WPS Resources and Basin that the result of permitting this choice would be that customers whose Balancing Authority chose to recover costs under Schedule 24/24-A would pay a zonal charge plus a share of regional charges, while customers whose Balancing Authority chose to recover costs under Schedule 1 would pay only a share of regional charges. This choice would also permit the Balancing Authorities to choose the entities from which they recover costs: Schedule 1 provides for cost recovery from transmission customers only, and revised Schedule 24 and proposed Schedule 24-A would permit recovery of costs from generators and transmission customers, but on a zonal basis. As a result, customers in some zones of the Midwest ISO region would unjustifiably subsidize customers in other zones, and some categories of customers would unjustifiably subsidize others.

²⁷ The filing does not explain how the costs booked to Account Nos. 556 and 561 would interact between Schedule 1 and Schedules 24/24-A; however, it remains unrebutted that this would provide a basis for the Balancing Authorities to shift costs between Schedules 1 and 24/24-A at their discretion.

²⁸ Midwest ISO TOs Transmittal Letter at 7 (Jun. 6, 2005).

²⁹ *See id.* at n.6.

40. While the Midwest ISO TOs argue that the “issue is one of shifting dollars from one schedule to another” and that the change from a regional to a zonal cost recovery methodology “should not have a significant impact on rates or costs,”³⁰ they provide no support for these assertions. In fact, WPS Resources has presented an appendix to its Answer that suggests that there may be significant cost shifts associated with the tariff change. We therefore conclude that, merely as a result of their geographical location (and based on the choice of a Balancing Authority), similarly situated customers will pay different rates under the Midwest ISO TOs’ proposal. Additionally, we are concerned that the proposed rate design for the zonal charges under Schedules 24 and 24-A may provide improper price incentives for generators if generators are required to pay different rates based on the megawatts they inject into each zone. This concern does not currently exist under Schedule 17.³¹ As the Midwest ISO TOs have made no attempt to explain why the difference between categories of customers, and between customers located within different zones, is justifiable,³² we find that the result is unduly discriminatory.³³

41. Protestors next contend that the proposed revisions to Schedule 24 are unjust and unreasonable because, among other things, they violate the TEMT II Order and the Balancing Authority Agreement. In light of our finding that the proposed revisions to Schedule 24 (and proposed Schedule 24-A) are unduly discriminatory, and therefore unacceptable, we need not decide now whether those revisions are also unjust and unreasonable.

42. Schedule 24-A includes divisors that divide the rates into monthly, weekly, daily and hourly components. The Midwest ISO and Midwest TOs were, as the Midwest ISO TOs concede, in error to include such divisors, as the rate is already expressed in megawatt-hours. However, as we are rejecting the proposed Schedule 24-A, the protestors’ arguments about the rate design in Schedule 24-A are moot.

³⁰ Midwest ISO TOs Answer at 5.

³¹ Under Schedule 17, all market participants, including generators, pay the same regional postage-stamp rate.

³² *See Alabama Elec. Coop. v. FERC*, 684 F.2d 20, 29 (D.C. Cir. 1982) (“In the typical case, where a rate design call[s] for different rates to customer classes which are similarly situated, the utility has the burden of satisfying FERC that such differences exist between the classes as to justify the separate rates.”).

³³ *See id.* at 27-30.

43. We agree with WPS Resources that the Midwest ISO TOs' compliance filing does not fulfill the requirements of the Balancing Authority Settlement Order because it does not make the cost recovery process more transparent and easier to audit. As described above, by allowing the Balancing Authorities to choose – and freely alternate – between recovering costs under Schedules 1 and 24, the Midwest ISO TOs' proposal would make it possible for some zones to over-recover costs. Moreover, because there are no requirements that the Midwest ISO TOs notify market participants as to which schedule they would use to recover their costs at what time, market participants would not be able to reliably anticipate their share of Balancing Authority costs. Further, the proposal would decrease, rather than increase, clarity as to how the recovered costs are accounted for. The Midwest ISO TOs propose an accounting mechanism for labor costs only, under the proposed Schedule 24-A. They do not explain how they would account for any other costs under Schedule 24, as the Balancing Authority Settlement Order required. It would be difficult or impossible to ensure that the Balancing Authorities had recovered the appropriate costs under the proposed schedules, contrary to the direction in the Commission's order. That the Midwest ISO TOs would create new sub-accounts of Account Nos. 556 and 561 for Balancing Authority costs does not overcome the proposal's problems, especially given that such sub-accounts are not identified in the tariff proposal.

44. Accordingly, we will reject the compliance filing and require the Midwest ISO TOs to file a new compliance filing within 60 days of the date of this order. This decision, however, is without prejudice to the Midwest ISO TOs' making future filings under section 205 of the FPA to propose a new cost recovery mechanism.

The Commission orders:

(A) The Midwest ISO TOs' compliance filing is hereby rejected. The Midwest ISO TOs are hereby directed to make a new compliance filing, within 30 days of the date of this order, to satisfy the requirements of the Balancing Authority Settlement Order.

(B) The Midwest ISO TOs' section 205 filing is hereby rejected.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.