119 FERC ¶ 61,339
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Montana Generation, LLC Docket No. ER07-827-000

ORDER GRANTING AUTHORIZATION TO MAKE AFFILIATE SALES

(Issued June 29, 2007)

1. In this order, we grant Montana Generation, LLC's (Montana Generation) application under section 205 of the Federal Power Act (FPA)[1] that requests Commission authorization to make power sales to its affiliate, NorthWestern Corporation (NorthWestern). Montana Generation explains that the proposed power purchase agreements (PPAs), are the product of a negotiated settlement among NorthWestern, the Montana Consumer Counsel (Montana Counsel) and the Montana Public Service Commission (Montana Commission) arising from NorthWestern's bankruptcy and a request for proposal (RFP) process implemented by NorthWestern. The RFP sought, among other products, long-term electricity supply for NorthWestern's default supply customers in Montana, with service commencing on July 1, 2007, consistent with the Default Supply Resource Procurement Plan filed with the Montana Commission in January 2004. By this order, we find that the competitive solicitation, as described below and conducted consistent with the process described herein, satisfies the Commission's concerns regarding affiliate abuse. Accordingly, we will authorize this affiliate sale and condition our approval on the seller providing the service under the rates, terms and conditions as submitted in the instant submittal. This authorization will be effective as of the date of issuance of this order.

Background

2. On May 1, 2007, Montana Generation submitted a request for authorization to make power sales to its affiliated franchised public utility NorthWestern. Montana Generation states that the requested authorization will permit it to make unit firm energy sales to NorthWestern pursuant to a pair of mirror image PPAs. Montana Generation states that NorthWestern's Colstrip Unit No. 4 operations submitted the winning bid of

[1] 16 U.S.C. § 824d (2000).

the RFP through a neutral proxy, however because NorthWestern cannot contract with itself, Montana Generation and NorthWestern entered into the mirror image PPAs. Montana Generation asserts that the RFP was conducted consistent with the Commission's standards for approving affiliate sales that result from the participation in a competitive procurement process and that the resulting rates will be just and reasonable.

3. According to Montana Generation, it is an indirect wholly-owned subsidiary of NorthWestern with authorization to make sales at market-based rates.[2] Montana Generation states that NorthWestern is a franchised public utility company serving retail customers primarily in Montana and South Dakota, where NorthWestern is subject to regulation by the state commissions. Montana Generation states that NorthWestern provides electric transmission service in Montana but owns no rate-based generation. Its predecessor, the Montana Power Company (Montana Power), divested such generation in 1999. However, Montana Generation states that NorthWestern holds a non-rate based 30 percent leasehold interest in Unit No. 4 at the Colstrip electric generating complex in eastern Montana. In addition, Montana Generation states that NorthWestern has market-based rate authorization.[3]

4. Montana Generation states that NorthWestern's default supply customers have an average load of approximately 708 MW and a peak load of approximately 1,122 MW. Montana Generation states that PPL Montana, LLC acquired Montana Power's rate-based generation facilities and currently supplies the majority of the default supply customers' load under two firm agreements that will terminate on June 30, 2007 (one for 300 MW and the other for 150 MW).

5. According to Montana Generation, NorthWestern conducted the competitive solicitation process in 2004, administered and supervised by an independent energy consultant, Lands Energy Consulting, Inc. (Lands Energy).[4] The competitive solicitation

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[2] *NorthWestern Corporation*, 112 FERC ¶ 61,019 (2005) (*NorthWestern*). Montana Generation notes that it was previously known as NorthWestern Energy Marketing, LLC. *Montana Generation, LLC,* Docket No. ER07-597-000 (June 1, 2007) (unpublished letter order).

[3] Application at 3 (*citing NorthWestern*).

[4] Montana Generation states that Lands Energy, a Washington state corporation, is an independent energy consulting company providing informational and advisory consulting services to utilities, large industrial users, trading companies, power plant developers and other wholesale producers and consumers of energy. Established in 1998, it specializes in combining financial trading expertise with a detailed knowledge of the Western North American natural gas and power grid to develop practical energy optimization techniques that reduce risk and create value.

process was designed to address NorthWestern's need for new power supplies to replace the PPL Montana agreements. Montana Generation states that the Montana Commission regulates the method through which NorthWestern is required to acquire power to meet the needs of its default supply customers. Montana Generation asserts that this method is consistent with the principals outlined by the Commission in *Allegheny*.[5]

6. Montana Generation also explains that NorthWestern initiated the solicitation process for long-term electricity supply needs for its Montana default supply customers for service commencing on July 1, 2007, consistent with the Default Supply Resource Procurement Plan filed with the Montana Commission in January 2004. The RFP requested bids for long-term supply but did not specify a term length. NorthWestern sought proposals for various types of resources, including base-load, dispatchable/shaped and wind energy. The RFP stated that all proposals, including from affiliates, would be subject to the same deadlines, screening procedures and screening criteria. The RFP stated that NorthWestern may bid its resources into the RFP.[6]

7. Montana Generation also states that although NorthWestern identified specific resources and quantities, the RFP stated that those resources and volumes were illustrative and that all resources would be considered. Montana Generation states that NorthWestern sent a copy of the RFP to 130 individuals and industry news organizations, issued a press release and posted the RFP on the Lands Energy website. Bidders were required to submit bids on a $/MWh basis. The winning bid for base-load service was selected on the basis of price and non-price terms. Finally, Montana Generation reiterates that Lands Energy supervised and monitored the solicitation process that led to the mirror image PPAs.

8. Montana Generation states that Lands Energy received 51 "intent to respond" forms, and 44 proposals (9 for intermediate term products and 35 for long-term products). The names of the bidders were masked. Several proposals included multiple products which were evaluated as separate proposals. Accordingly, the 35 long-term submittals were broken down into over 60 proposals for modeling purposes. Lands Energy evaluated the proposals and recommended 21 proposals to NorthWestern. NorthWestern selected eight of Lands Energy's recommended proposals by conducting a qualitative and

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[5] Application at 5 (*citing Allegheny Energy Supply Co.*, 108 FERC ¶ 61,082 at P 33 (2004) (*Allegheny)*).

[6] On September 14, 2003, NorthWestern filed a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code. A bankruptcy settlement among NorthWestern, Montana Counsel and the Montana Commission required NorthWestern to bid a 90 MW Offer utilizing power generated at Colstrip Unit 4 (90 MW Offer) into the 2004 solicitation process.

quantitative review of the proposals and stochastic modeling using the PCI model (a portfolio model that considers, among other things, risk). The names of the bidders were not revealed to NorthWestern until after it selected a short-list of bidders with which it might pursue further negotiation.

9. The RFP contemplated and put bidders on notice that there would be negotiations after short-list selections. Testimony submitted with the application states that NorthWestern made counteroffers to three of the short-listed bidders as part of the negotiations. One of the counteroffers regarded the 90 MW Offer from NorthWestern's Colstrip Unit No. 4, resulting in an extension of the term from 2010 to 2018.

10. NorthWestern sought advance approval from the Montana Commission for a new power supply and a term sheet for the 90 MW Offer from the Colstrip plant. The term sheet outlined the price, term, and quantity for the 90 MW Offer which was selected by Lands Energy as a winning bid in the RFP process.[7] NorthWestern subsequently entered into a Stipulation Agreement with the Montana Counsel in order to resolve NorthWestern's Electric Default Supply Filings for 2002-2004 (Tracker Settlement), which was approved by the Montana Commission.[8] NorthWestern was informed by the Montana Commission staff that the price, quantity and term of the 90 MW Offer were implicitly approved by the Tracker Settlement and the best course of action would be to effectuate the 90 MW Offer by entering into an enforceable agreement with a subsidiary.

11. In light of the above, NorthWestern has entered into a mirror image pair of firm PPAs for a 90 MW per hour unit contingent sale of power commencing on July 1, 2007 at a price of $35.25 per MWh and ending on December 31, 2018 at a price of $36.25 per MWh. In the first PPA, NorthWestern sells 90 MW per hour to Montana Generation, while in the second PPA, Montana Generation sells 90 MW per hour to NorthWestern on behalf of the Default Supply customers.

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[7] As a result of the RFP, NorthWestern also entered into a 20 year contract with a non-affiliate Invenergy Wind, LLC. Pursuant to the contract NorthWestern can purchase up to 150 MW from the Judith Gap wind generation project.

[8] *See In the Matter of the Applications by NorthWestern Energy Regarding its Electric Default Supply Filings for the Tracking Periods 2002 through 2004; Stipulation Agreement Between NorthWestern Energy, the Montana Consumer Counsel*, Docket No. D2003.6.77 and D2004.6.90; Final Order 6574(E) (Dec. 16, 2005).

Notice of Filing and Responsive Pleadings

12. Notice of Montana Generation's filing was published in the *Federal Register*,[9] with motions to intervene and protests due on or before May 22, 2007. The Montana Counsel filed a timely motion to intervene and protest to Montana Generation's application. Montana Generation filed an answer to the Montana Counsel's protest.

Discussion

A. Procedural Issues

13. Pursuant to Rule 214 of the Commission's Rule of Practice and Procedure,[10] the Montana Counsel's timely filed, unopposed motion to intervene serves to make it a party to this proceeding.

14. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure,[11] prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept the above-identified answer submitted by Montana Generation because it has provided information that assisted us in our decision-making process.

B. Affiliate Abuse Analysis

15. The primary issue in reviewing the Montana Generation filing is whether the Commission's concerns regarding affiliate abuse have been satisfied. In *Edgar*, the Commission stated that, in cases where affiliates are entering into market-based rate sales agreements, it is essential that ratepayers be protected and that transactions be above suspicion in order to ensure that the market is not distorted. The Commission has approved affiliate sales resulting from competitive bidding processes after the Commission has determined that, based on the evidence, the proposed sale was a result of direct head-to-head competition between affiliated and competing unaffiliated suppliers.[12]

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[9] 72 Fed. Reg. 27,113 (2007).

[10] 18 C.F.R. § 385.214 (2006).

[11] 18 C.F.R. § 385.213(a)(2) (2006).

[12] *See Boston Edison Co. Re: Edgar Electric Energy Co.*, 55 FERC ¶ 61,382 at 62,167-69 (1991) (*Edgar*). *See also Connecticut Light & Power Co. and Western Massachusetts Electric Co.*, 90 FERC ¶ 61,195 at 61,633-34 (2000); *Aquila Energy Marketing Corp.*, 87 FERC ¶ 61,217 at 61,857-58 (1999); *MEP Pleasant Hill, LLC*, 88 FERC ¶ 61,027 at 61,059-60 (1999).

16. When an entity presents this type of evidence, the Commission has required assurance that: (1) a competitive solicitation process was designed and implemented without undue preference for an affiliate; (2) the analysis of bids did not favor affiliates, particularly with respect to non-price factors; and (3) the affiliate was selected based on some reasonable combination of price and non-price factors.[13]

17. In *Allegheny*, the Commission provided guidance as to how it will evaluate whether a competitive solicitation process such as the one in the instant proceeding satisfies the *Edgar* criteria. As the Commission stated therein, the underlying principle when evaluating a competitive solicitation process under the *Edgar* criteria is that no affiliate should receive undue preference during any stage of the process. The Commission stated that the following four guidelines will help the Commission determine if a competitive solicitation process satisfies that underlying principle: (1) Transparency: the competitive solicitation process should be open and fair; (2) Definition: the product or products sought through the competitive solicitation should be precisely defined; (3) Evaluation: evaluation criteria should be standardized and applied equally to all bids and bidders; and (4) Oversight: an independent third-party should design the solicitation, administer bidding, and evaluate bids prior to the company's selection. The Montana Counsel does not challenge NorthWestern's compliance with the principles explained in *Edgar* and *Allegheny*. As discussed below, the Commission finds that the RFP satisfies the *Allegheny* guidelines.

1. <u>Transparency Principle</u>

18. Montana Generation states that the process was transparent, open to all interested parties and widely advertised. Montana Generation states that in addition to press releases and public notices, NorthWestern's RFP was sent to 130 individuals and industry news organizations and each potential bidder was supplied with the same bidding package. Further, Montana Generation states that Lands Energy was retained to supervise and monitor the solicitation process. Montana Generation notes that the RFP was posted on the Lands Energy website and Lands Energy conducted two conference calls open to all potential bidders. Montana Generation asserts that all bidders had equal access to the data relevant to NorthWestern's RFP. Montana Generation states that the names of the bidders were masked and were not revealed to NorthWestern until after it selected a short-list of bidders with which it might pursue further negotiation.

19. Based on Montana Generation's representations, the Commission finds that the RFP is consistent with the Commission's transparency guidelines.

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[13] *Edgar*, 55 FERC ¶ 61,382 at 62,168.

2. Definition Principle

20. Montana Generation states that the products sought through the solicitation were well defined. NorthWestern sought bids for intermediate and long-term electric energy and capacity resources in the following categories: base-load, dispatchable/shaped, wind and full and partial requirements. According to Montana Generation, NorthWestern also set forth the specific requirements to be included in each type of proposal. Montana Generation notes that interested parties were aware that bids for base-load power were being solicited.

21. Based on these representations, the Commission finds that the RFP was consistent with the Commission's definition guidelines.

3. Evaluation Principle

22. Montana Generation states that the evaluation criteria was standardized and applied equally to all base-load bidders and that the bidders were masked until after Montana Generation had selected its short list of bidders with which to pursue further negotiations. Montana Generation states that Lands Energy actively monitored and interacted with NorthWestern personnel with regard to the bid component of the solicitation process to ensure that all prospective bidders were treated equally. Montana Generation states that the bids were evaluated for both price and non-price terms. In its testimony, Lands Energy described in detail the qualitative and quantitative review applied to the proposals submitted.[14] According to Lands Energy, the quantitative price review captured the price-related elements of each proposal, such as the cost relative to proposed capacity and energy, the costs and benefits of the dispatchability, the firmness of the product, the ability to remarket the energy, and the value associated with the point or points of delivery. In the preliminary short-listing process, the spreadsheet model that was used did not compute the value of ancillary services or lack thereof, nor the costs and risks associated with integrating the resource into NorthWestern's portfolio. Lands Energy also describes the stochastic modeling it performed on NorthWestern's behalf, using the PCI GenTrader Model as part of the final selection process in order to capture those values and assess the relative impact they would have on different resource portfolios.

23. Further, Lands Energy states that it developed the preliminary shortlist of 21 offers by comparing resource proposals of similar resource types or categories. This was done to identify whether proposals that did not score at the top of their resource type warranted continued review. Lands Energy also stated that a resource with specific qualitative

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[14] Exhibit C at 20-30. Montana Generation attached the testimony as Exhibit C to its request for authorization.

strengths, but not at the top of its category in a pure price/value analysis, might have been included in the preliminary short list for additional consideration in order to ensure that NorthWestern had a good sample of resource alternatives. Lands Energy then submitted the price scores and qualitative summaries to NorthWestern and the Technical Advisory Committee for review and comment prior to the completion of the preliminary shortlist selections. Lands Energy states that assessment of the qualitative areas of each proposal involved consideration of: (1) development risk; (2) project team experience; (3) site control; (4) environmental review; (5) permit status; (6) counterparty risk; (7) unit complexity and technology risk; and (8) NorthWestern supplier diversity and counterparty concerns.

24. Based on these representations, the Commission finds that the RFP was consistent with the Commission's evaluation principle guidelines.

4. Oversight Principle

25. Montana Generation states that the competitive solicitation process was administered and supervised by Lands Energy, an independent energy consultant. The competitive solicitation process followed the RFP process outlined in the bid package supplied to all potential bidders, affiliated and unaffiliated. According to Montana Generation, that the independent consultant Lands Energy identified the NorthWestern Colstrip Unit No. 4 bid as the lowest base-load bid. Montana Generation represents that the winning bidders were not disclosed to NorthWestern until after NorthWestern had selected a short-list of bidders from the list of bidders recommended by the independent consultant.

26. Based on these representations, the Commission finds that the RFP was consistent with the Commission's oversight principle guidelines.

C. Montana Counsel Protest

27. The Montana Counsel states that it does not object to NorthWestern's compliance with the Commission's standards for authorization to make power sales to its affiliate, NorthWestern. However, the Montana Counsel questions both the necessity and appropriateness of inserting a special purpose subsidiary (Montana Generation) into the transaction in order to execute a competitively vetted power sale. The Montana Counsel argues that NorthWestern's almost two-year delay implementing the stipulated settlement and the inexplicable complication of the manner by which it chose to implement the settlement, raise concerns about the corporate structure NorthWestern chose. The Montana Counsel asserts that the transaction should be a simple and straight forward intracorporate transaction. The Montana Counsel points out that NorthWestern's Colstrip Unit No. 4 entitlement is not a new resource; it is involved in other commitments that simply must be taken into consideration in future restructurings. The Montana Counsel states that NorthWestern continues to hold the unregulated assets of Colstrip Unit No. 4,

just as it did before. Consequently there is no need to procure the power through a contract.[15]

28. The Montana Counsel also states that Montana Generation's documentation of its contract with NorthWestern is incomplete; the record contains no indication that the power sale is at a fixed price. The Montana Counsel argues that the Commission should at a minimum require that Montana Generation modify its proposed agreement with NorthWestern to preclude modification of the contract prices and other terms established by the settlement in order to ensure that NorthWestern's default supply customers realize the benefit of the bargain that was struck on their behalf in the May 31, 2005 settlement stipulation between the Montana Counsel and NorthWestern. The Montana Counsel therefore requests that to the extent that the Commission accepts Montana Generation's proposed contracts for filing that the contracts be modified to preclude changes in price and other terms.

29. In response to the Montana Counsel's comments, Montana Generation explains that the mirror image PPAs are necessary to fully describe the delivery arrangements required to provide the energy outlined in the initial term sheet. For example, Montana Generation states that the term sheet is incomplete because it does not contain the requisite additional terms such as scheduling, point of delivery, unit contingency, *force majeure* and maintenance. Montana Generation explains that the mirror image Edison Electric Institute (EEI) Master Agreement is appropriate to use to memorialize the transaction because the affiliated transaction necessarily requires an agreement and NorthWestern cannot contract with itself.

30. Montana Generation disagrees that the record is incomplete. Montana Generation states that the filing includes as Attachment No. 1 the standard transaction confirmation letter containing the important terms of the proposed sale such as price, term, point of delivery, and unit commitment. Montana Generation explains that it did not include a copy of the Master Power Purchase Agreement since it is an industry-recognized standard form agreement for long-term power purchases.[16]

[15] Montana Generation explains that in 1985, its predecessor Montana Power entered into a sale-leaseback of its 30 percent interest in the Colstrip Unit 4 electric generation facility. The Commission disclaimed jurisdiction over the sale/leaseback transaction because the transaction involved only generating facilities and equipment associated with the generating facilities. *See Montana Power Co.*, 35 FERC ¶ 61,084 (1986). Montana Power's leasehold interest was never placed into rate base.

[16] The standard form agreement is accessible at www.eei.org.

D. Commission Determination

31. The *Edgar* criteria and *Allegheny* guidelines are designed to ensure that the transactions between affiliates do not unduly favor affiliates and thereby protect captive customers from affiliate abuse. The Montana Counsel states that "there is no issue in this case as to the transparency and competitiveness of the process through which NorthWestern's Colstrip 4 entitlement was chosen as a resource for Montana default supply."[17] As discussed herein, we agree and conclude that the RFP satisfies our affiliate abuse concerns.

32. Specifically, one of the key issues before this Commission is whether the RFP satisfies the Commission's concerns regarding affiliate abuse and otherwise would result in just and reasonable wholesale rates. In that regard, the Commission finds that the competitive solicitation process satisfies our concerns regarding affiliate abuse because the RFP is consistent with the *Edgar* criteria and the *Allegheny* guidelines. Moreover, Montana Counsel does not argue that the process is inconsistent with our precedent.

33. Rather, a concern of Montana Counsel's is with the necessity and appropriateness of using a special purpose subsidiary (Montana Generation) to effectuate the transaction. However, beyond suggesting a "concern," the Montana Counsel does not explain what problems it sees with the use of a special purpose subsidiary or what harm may result from use of a special purpose subsidiary.[18] Such concerns, in any event, are not relevant to this proceeding, and also are more appropriately raised at the state level.

34. With regard to Montana Counsel's concern that Montana Generation may in the future seek to modify the price and other terms, we expressly condition our authorization herein on the seller providing service under the rates, terms and conditions as submitted in the instant submittal. In this regard, we find that Montana Generation, in its May 1 Filing, submitted as Attachment 1 the standard transaction confirmation letter, which is part of the EEI Master Agreement. This standard confirmation letter contains the important terms of the proposed sale of power between Montana Generation and NorthWestern, such as price, term, point of delivery, and unit commitment. Further, the Master Agreement is an industry-recognized standard form agreement for long-term power purchases, and if NorthWestern and/or its affiliates seek to charge different rates for these affiliate sales, they must obtain prior authorization from the Commission.

35. In addition, we find that Montana Generation need not file all of the documentation for the parties' agreement. Order No. 2001,[19] which implemented Section

[17] Montana Counsel comments at 6.

[18] *Id.* at 6-7.

[19] *Revised Public Utility Filing Requirements*, Order No. 2001, FERC Stats. &

35.1(g)[20] of the Commission's regulations, obviates the need to file with the Commission service agreements under market-based power sales tariffs.

36. Accordingly, the Commission concludes that the competitive solicitation process described by Montana Generation satisfies the Commission's concerns regarding affiliate abuse and results in just and reasonable rates. Therefore, the Commission grants Montana Generation's request for authorization to make affiliate sales to NorthWestern pursuant to NorthWestern's 2004 RFP, as discussed herein. Montana Generation and NorthWestern must receive prior approval from the Commission under section 205 of the FPA for any other sales to affiliates with a franchised electric service territory and captive customers pursuant to subsequent RFPs.

37. This order satisfies the requirement that Montana Generation and NorthWestern first receive Commission authorization, pursuant to section 205 of the FPA, before engaging in power sales at market-based rates with an affiliate. Consistent with the procedures the Commission adopted in Order No. 2001, Montana Generation must file electronically with the Commission an Electronic Quarterly Report containing: (1) a summary of the contractual terms and conditions in every effective service agreement for market-based power sales; and (2) transaction information for effective short-term (less than one year) and long-term (one year or greater) market-based power sales during the most recent calendar quarter.[21] Electric Quarterly Reports must be filed quarterly no later than 30 days after the end of the reporting quarter.[22]

Regs. ¶ 31,127 , *reh'g denied*, Order No. 2001-A, 100 FERC ¶ 61,074, *reh'g denied*, Order No. 2001-B, 100 FERC ¶ 61,342, *order directing filing*, Order No. 2001-C, 101 FERC ¶ 61,314 (2002), *order directing filing,* Order No.2001-D, 102 FERC ¶ 61,334 (2003).

[20] *See* 18 C.F.R. § 35.1(g) (2006) ("[A]ny market-based rate agreement pursuant to a tariff shall not be filed with the Commission.").

[21] Required data sets for contractual and transactional information to be reported in Electric Quarterly Reports are described in Attachments B and C of Order No. 2001. The Electric Quarterly Report must be submitted to the Commission using the EQR Submission System Software, which may be downloaded from the Commission's website at http://www.ferc.gov/docs-filing/eqr.asp.

[22] The exact dates for these reports are prescribed in 18 C.F.R. § 35.10b (2006). Failure to file an Electric Quarterly Report (without an appropriate request for extension), or failure to report an agreement in an Electric Quarterly Report, may result in forfeiture of market-based rate authority, requiring filing of a new application for market-based rate authority if the applicant wishes to resume making sales at market-based rates.

The Commission orders:

The application for authorization for Montana Generation to make power sales to its affiliate, NorthWestern, pursuant to NorthWestern's 2004 RFP is granted as conditioned herein, effective as of the date of issuance of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.