

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Devon Power LLC,

Docket No. EL06-47-000

v.

ISO New England, Inc.

ORDER DENYING COMPLAINT

(Issued March 13, 2006)

1. In a complaint filed by Devon Power LLC (Devon) against ISO New England, Inc. (ISO-NE), Devon argues that ISO-NE erroneously interpreted section 3.5 (Non-Performance Penalty) of a Reliability Must Run agreement (RMR Agreement) and penalized Devon for 72 hours in response to the Devon units being unavailable for less than two hours. Devon further asserts that ISO-NE failed to pro rate the amount of the hourly penalty for the portion of each hour in which the units were in fact unavailable. The Commission finds that ISO-NE properly interpreted the RMR Agreement and denies the complaint.

Background

2. On June 8, 2005, at 12:45¹ Devon Units 11-14 were issued a dispatch instruction by ISO-NE, with an expected on-line time of 13:20. At 13:11 Devon informed the ISO-NE control room that the Units would be unable to operate due to an inability to obtain natural gas from the Iroquois Gas Transmission System, LP (Iroquois) in time to meet the dispatch instruction. Devon states that it experienced a delay in receiving confirmation of its intra-day gas nominations as a result of new operating restrictions imposed by the pipeline. Devon states that confirmations were subsequently received, allowing the Units to return to service, and at 14:27 Devon states that it notified ISO-NE that the Units were available for dispatch. Devon states that on the next day (June 9, 2005) the Devon Units responded to dispatch instructions, and no further dispatch instructions were received through June 11, 2005.

¹ The 24 operating hour convention is used herein for each hour.

3. Devon states that on August 11, 2005, ISO-NE settled the June payments made to Devon under the RMR Agreement, and reduced Devon's net monthly availability payment by a non-performance penalty of \$192,093.12. Devon states that ISO-NE imposed the Non-Performance Penalty for each of the 72 hours beginning with Hour Ending 14 on June 8, 2005. Pursuant to section 6.3.6 of ISO-NE's Tariff Billing Dispute procedures,² the Requested Billing Adjustment (RBA) Decision would be final and binding if not appealed by Devon within 20 business days, including appeal of the RBA Decision to the Commission. On November 9, 2005, Devon timely filed its RBA pursuant to the ISO-NE Billing Dispute Procedures, disputing the application of the non-performance penalty for 72 hours, and ISO-NE's failure to pro rate the calculation of the hourly penalty for the portions of each of the two hours that the Devon units were not available.

4. On December 13, 2005, ISO-NE issued its RBA Decision denying both grounds of error raised by Devon in the RBA.

Complaint

5. On January 12, 2006, as revised on January 13, 2006, Devon filed with the Commission a complaint against ISO-NE, contending that ISO-NE's interpretation of section 3.5 of the RMR Agreement "is plainly inconsistent with the scope of section 3.5, as set forth in the initial language of that section". Devon claims that this misinterpretation resulted in a non-performance penalty levied against Devon in the amount of \$192,093.12. Devon claims the appropriate amount should be \$3,112.62. Section 3.5 states as follows:

3.5 Non-Performance Penalty. If a Unit of a Resource fails to comply fully with a dispatch by ISO issued in accordance with the unit characteristics provided on Schedule 3 and such failure is not due to a *Force Majeure* Event, the Unit shall be subject to a Non-Performance Penalty computed in accordance with this section 3.5

3.5.1 The monthly Non-Performance Penalty shall be the sum of the amounts applied for each Hour in the Month by multiplying (i) the Availability Deficiency Factor for the Hour by (ii) the Hourly Penalty Rate for Unit as set forth on Schedule 4 (the Unit's Hourly Availability Rate); provided that the Non-Performance Penalty for any month shall not

² ISO-NE, FERC Electric Tariff No. 3, General Terms and Conditions, section 1, Exhibit ID, § 6.3.6.

exceed the Fixed Cost Payment for the Month. For purposes of this calculation:

- (a) an Availability Deficiency Factor shall be applied for each Hour of the Penalty Period as one minus the number determined by dividing (a) the MWh delivered to the NEPOOL Control Area (the “Delivered MWhs”) for the hour in question by (b) the product of the MWs requested in the Dispatch Instruction (the “Requested MW”) and the percentage of the hour (up to 100%) that the Resource was subject to a Dispatch Instruction.
- (b) The Penalty Period shall be the 72 hour period beginning at the time Owner fails to comply fully with a dispatch by ISO, provided that if Owner in accordance with section 5.2 had scheduled an outage to begin during the 72-hour period, the Penalty Period will terminate at the time the outage was scheduled to begin. The Requested MWs shall be reduced to eliminate the effect of any Force Majeure affecting deliveries.

6. Devon contends that the initial language plainly states that the non-performance penalty is to be applied only for the hours for which Devon failed to comply with a dispatch instruction. The Devon Units were unable to respond due to unavailability of gas for less than two hours on June 8, 2005, and actually responded fully to dispatch instructions received on June 9, 2005. However, ISO-NE penalized Devon even in hours in which it complied with dispatch instructions and in hours in which it was available to comply.

7. Devon states that the fact that the penalty period is of a limited duration of 72 hours, beginning at the time a unit fails to comply fully with a dispatch, does not mean that the non-performance penalty is to be applied in each of those 72 hours, but is plainly a limitation on the duration of the period in which the penalty may be applied. Devon states that its units experienced a direct reduction in their monthly availability payment as a result of being unavailable during hours 14 and 15 on June 8, 2005, and the non-performance penalty was applied on top of that. Devon states that ISO-NE’s misconstruction of the non-performance penalty disproportionately penalizes the Devon Units because they have short minimum run times (2 hours). Devon states that its units would have expected to run for only two hours upon ISO dispatch and yet, under ISO-NE’s interpretation, the units are penalized for 72 hours, 36 times their expected hourly

availability payments. Devon states that section 3.5 of the RMR Agreement should not be construed to effect such a disproportionate penalty compared to compensation allowed for providing reliability services.

8. Devon contends that ISO-NE's interpretation of section 3.5 of the RMR Agreement in conflict with the express termination of the penalty period if the owner had previously scheduled an outage to begin during the 72-hour period. Devon asserts that this provision only makes sense if the penalty period is a limitation. Devon states that ISO-NE acknowledges that under its interpretation, a unit that returns to available status and responds to subsequent dispatch instructions continues to be penalized. Devon states that since a scheduled outage presumptively predates and is unrelated to the initial failure to respond to the dispatch instruction, ISO-NE's construction of the penalty period bestows an unwarranted end to the penalty as a result of a coincidence, but punishes units that return quickly to service and respond fully to all subsequent dispatch instructions. Devon states that this approach would be a disincentive to quick resumption of availability.

9. Devon asserts that the formula set forth in section 3.5.1 of the RMR Agreement is to be applied on an hourly basis, which is consistent with construing the 72 hour penalty period as a limitation. Devon notes that the formula is calculated "for each hour in the month" based on an availability deficiency factor "for the hour." Devon states that on its face, the formula calls for a calculation "for the hour," taking into account the availability deficiency factor in such hour. Devon states that there is no basis in the language of the provision to assume that calculations of penalty amounts are to be made in any hours in which the availability deficiency factor is zero (such as the hours in which the unit resumed availability for dispatch). Devon asserts that if the penalty were intended to be assessed for a 72 hour period, the contract language would have been written more simply as the product of 72 times the amount of the hourly rate calculation.

10. Devon states that ISO-NE's reliance on the provision in section 3.5.1(a) of the RMR Agreement that an availability deficiency factor "shall be applied for each Hour of the Penalty Period" does not support ISO-NE's interpretation that the availability deficiency factor in the initial hour is to be applied to every hour thereafter.

11. Devon states that the RBA Decision is inconsistent with ISO-NE's previous acknowledgment of the purpose and the source of the non-performance penalty. Devon includes in its filing a memorandum³ to the New England Power Pool Markets Committee (NEPOOL) in which ISO-NE states "The [non-performance] penalty provision...is intended to provide appropriate, but not overly burdensome, incentives to keep the Resource in good working condition." Devon notes that, under ISO-NE's current position a unit will be burdened with the same penalty if it were unavailable for

³ See Exhibit 3 of the filing.

part of one hour, or if it remains unavailable for 72 hours, continuing to impose the penalty without regard to its availability and full responses to subsequent dispatch instructions.

12. Finally, Devon states that section 3.5 of the RMR Agreement expressly provides that the penalty is properly applied on a *pro rata* basis for the portions of each hour in which the units failed to comply with the dispatch instruction. Devon cites section 3.5.1(a) of the RMR Agreement which states that the availability deficiency factor is to be pro rated “for the percentage of the hour (up to 100%) that the resource was subject to a Dispatch instruction.” Devon states that its failure to comply with the dispatch instructions received June 8, 2005 at 12:45 did not begin until 13:20, accordingly the availability deficiency factor should be pro rated for that hour. Similarly, Devon states that the units became available at 14:30 when Devon informed ISO-NE that the units were again fully available to comply, thus that hour’s availability deficiency factor should be pro rated as well.

13. Devon requests the Commission to require ISO-NE to make a billing adjustment to credit the monthly availability payments due Devon for the month of June 2005, by the amount of \$188,980.50, plus interest.

Notice

14. Notice of the complaint was published in the *Federal Register*, 71 Fed. Reg. 3,285 (January 20, 2006), with comments, interventions, and protests due on or before February 1, 2006. The New England Power Pool Participants Committee filed an intervention. Consolidated Edison Energy, Inc. (ConEd) and PSEG Energy Resources & Trade LLC (PSEG) filed comments in support of Devon’s complaint. ISO-NE filed an answer to the complaint. The Connecticut Department of Public Utility Control (Connecticut DPUC) filed comments in support of ISO-NE. The Connecticut Office of Consumer Counsel (COCC) filed a motion to intervene out-of-time, in support of ISO-NE. Devon filed an answer to ISO-NE’s answer.

Comments of PSEG and ConEd supporting Devon’s complaint

15. PSEG states that ISO-NE’s interpretation of the language renders meaningless the formula for calculating the applicable penalty in section 3.5.1(a) of the RMR Agreement, and instead, a generator would incur a 72 hour penalty for each hour in which it did not comply with a dispatch instruction, conflicting with ISO-NE’s stated intent of allowing reasonable penalties that encourage generators to make their facilities speedily available following a forced outage.

16. ConEd states that ISO-NE’s interpretation disregards the plain language of the agreements, which expressly state that the availability deficiency factor shall be

separately determined “for each hour of the penalty period” pursuant to a calculation conducted “for the hour in question.” ConEd asserts that the only way the pertinent contract language can be interpreted and applied, paying heed to all of its terms, is when the availability deficiency factor is in fact calculated separately for each hour of the penalty period. ConEd states that a precept of contractual construction should apply, namely that any ambiguity in a contract is to be construed against the drafter.

Comments of Connecticut DPUC and COCC opposing Devon’s complaint

17. Connecticut DPUC supports ISO-NE’s RBA Decision, stating that the plain language of section 3.5 of the RMR Agreement provides that the penalty for undisputed failure to perform shall be calculated based on 72 hours as the penalty period. Connecticut DPUC states that Devon’s interpretation would result in a de minimis penalty, allowing Devon to not perform whenever it believes that the cost of the penalty and loss of RMR payments for not operating when called upon will be lower than the costs associated with performance, such as obtaining fuel, or repairing broken equipment. Connecticut DPUC advises the Commission that this ruling will act as precedent, as the non-performance penalty provision is contained in all current RMR contracts in New England, and urges the Commission not to adopt Devon’s interpretation.

18. COCC states that ISO-NE’s interpretation is correct, because when a unit fails to respond to a dispatch instruction, the system needs to arrange for more expensive power, and once arranged, may not send another dispatch instruction to the RMR unit because the unit’s output must be replaced. COCC states that the minuscule penalty Devon claims is appropriate would do nothing to ensure that the ratepayers receive a reliability benefit in exchange for the substantial RMR availability payments.

ISO-NE’s answer

19. ISO-NE requests that the Commission dismiss Devon’s complaint. ISO-NE states that Devon’s arguments in support of its interpretation of section 3.5 of the RMR Agreement do not comport with the plain language of section 3.5, are misplaced because of policy reasons, and do not sufficiently refute ISO-NE’s RBA Decision.

20. ISO-NE states that the purpose of the RMR Agreement is to ensure local reliability of the system. Therefore, the system operator pays the RMR generator a portion of its fixed costs to stand ready to deliver an hourly minimum energy requirement. ISO-NE notes that a generator can only incur a non-performance penalty in hours in which it has represented itself as available to operate because if it tells ISO-NE it is not available, then it will not receive a dispatch instruction. Thus, in every hour, the generator may tell the ISO that it is not available to operate and thus have the potential for losing one hour of the annual fixed revenue requirement (AFRR) payment it receives for being available. ISO-NE states that, if not for the operation of the non-performance

penalty, it is possible for a baseload generator to earn 100 percent of its AFRR by meeting its target available hours for the annual period even though it failed to start or fully comply with dispatch instructions in some hours.

21. ISO-NE states that given the stakes at risk for ratepayers and for the reliability of the system, it is irrational to think that an inconsequential monetary penalty would be sufficient to send a clear signal about the expected conduct under the RMR Agreement, let alone change offending behavior. ISO-NE notes that the NEPOOL memorandum cited by Devon goes on to state that “it is typical for customers paying for ‘unit’ power to require the seller to provide performance guarantees.” ISO-NE states that the reference to “performance guarantees” was intended to signal that such a mechanism must be substantial in nature (although not overly burdensome) to adequately protect the interests of the customers paying for the power.

Discussion

Procedural Matters

22. Pursuant to Rule 214 of the Commission’s Rules of Practice and Procedure, 18 C.F.R. §385.214 (2004), the notices of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding. Given COCC’s interest, and the lack of undue prejudice in this early stage of the proceeding, we find good cause to grant, pursuant to Rule 214(d), 18 C.F.R. § 214(d), its untimely, unopposed motion to intervene.

23. Rule 213(a)(2) of the Commission’s Rules of Practice and Procedure, 18 C.F.R. §385.213(a)(2) (2003), prohibits an answer to an answer, unless otherwise ordered by the decisional authority. We will accept Devon’s answer because it has provided information that assisted us in our decision-making process.

Commission Determination

24. In determining the meaning of an agreement, the Commission applies the traditional rules of contract construction.⁴ Pursuant to these rules, the Commission must ascertain the intent of the parties by considering the language of the document itself, its purpose, and the circumstances of its execution and performance.⁵ Thus, the

⁴ *E.g., Mid Louisiana Gas Co. v. FERC*, 780 F.2d 1238 at 1243 (5th Cir. 1986).

⁵ *Penzoil Co. v. FERC*, 645 F. 2d 360,388 (5th Cir. 1981), *cert. denied*, 454 U.S. 1142 (1981).

Commission looks to the language of the agreement and its regulatory context.⁶ In the absence of an ambiguity, the Commission determines the meaning of the argument from the language of that agreement without resort to extrinsic or parole evidence.⁷

25. We will deny Devon's complaint. We agree with ISO-NE that section 3.5 of the RMR Agreement authorizes a 72 hour penalty. Although section 3.5.1 of the RMR Agreement indicates that the formula will be calculated on an hourly basis, section 3.5.1(b) of the RMR Agreement states that "The Penalty Period shall be the 72 hour period beginning at the time Owner fails to comply fully with a dispatch..." This language thus indicates that the RMR Agreement specifies that 72 hours is the length of time for which the Non-Performance Penalty applies. Devon admits that its units were completely unavailable for over one hour; therefore, zero MWs are to be used for the hourly calculation, which results in a full hourly penalty amount. If Devon had provided 50 percent of the MWs required by the dispatch it would have had its penalty reduced by 50 percent for the entire 72 hour period.

26. Section 3.5.1(b) of the RMR Agreement clearly designates only one way for the penalty period to be shortened. A scheduled outage is not just an unrelated coincidence, as alleged by Devon, but rather a period in which the generator is pre-scheduling its unavailability, and a time when the system already knows it cannot rely on that generator, and is not paying the generator for its availability. Additionally, as ISO-NE notes, a generator is only penalized when it reports its availability (thus collecting its fixed cost payment) and then does not perform.

27. Devon complains that ISO-NE's interpretation unfairly penalizes it for its short run time. However, section 3.5.1 of the RMR Agreement clearly states "the Non-Performance Penalty for any month shall not exceed the Fixed Cost Payment for the Month." Thus, Devon never actually owed ISO-NE for non-performance; it merely had monies removed from its fixed monthly payment.

28. In short, the Commission finds that generators self report their availability and, thus, collect their RMR availability payments from ISO-NE and its rate payers. Devon self-reported that it was available. ISO-NE contacted Devon after reading the critical notices issued by Iroquois to confirm that the Devon units were available and received no

⁶ *Amerada Hess Pipeline Corp.*, 74 FERC ¶ 61,318 (1996), *aff'd*, *Amerada Hess Pipeline Corp. v. FERC*, 117 F.3d 596 (D.C. Cir. 1997); *Columbia Gas Transmission Corp.*, 64 FERC ¶ 61.365 at 63,582 (1993) (*citing Penzoil Co. v. FERC*, 645 F. 2d 360,368 (5th Cir. 1981), *cert. denied*, 454 U.S. 1142 (1981)).

⁷ *Seattle v. FERC*, 923 F. 2d 713,716 (9th Cir. 1991); *Alabama Power Co. v. FERC*, 993 F. 2d 1557, 1565 (D.C. Cir. 1993).

indication from Devon that its units would not be available. When system reliability is at issue, the Commission believes that unless the generator is absolutely sure that it can run, it should not report itself as available and, thereby, collect the RMR availability payment from rate payers while possibly jeopardizing the integrity of the system in the event it cannot perform and the system must secure a new generation source. The 72 hour penalty does not provide a disincentive for a generator to quickly become available again because, once the generator reports itself as available, it resumes collection of the RMR availability payments. The 72 hours of penalty, which cannot exceed the monthly fixed cost payment, is not excessive, but rather necessary to the reliability of the system.

The Commission orders:

Devon's complaint is hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.