

114 FERC ¶ 61,200
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Mystic Development, LLC

Docket No. ER06-427-000

ORDER ACCEPTING AND SUSPENDING AGREEMENT AND ESTABLISHING
HEARING AND SETTLEMENT JUDGE PROCEDURES

(Issued February 24, 2006)

1. On December 29, 2005, Mystic Development, LLC (Mystic) filed an unexecuted Reliability Must Run Agreement (RMR Agreement) for the supply of electric energy at cost-based rates from its two combined-cycle, gas-fired generation facilities, known as the Mystic 8 and Mystic 9 Units, or Units, as requested by ISO-New England, Inc. (ISO-NE) to ensure reliability. Mystic requests that the Commission accept its proposed RMR Agreement and waive the Commission's 60-day prior notice requirement¹ to permit an effective date of January 1, 2006. In this order, we find that the Units qualify for RMR treatment, accept and suspend, for a nominal period, this RMR Agreement, and make it effective on January 1, 2006, subject to refund. We will also establish hearing and settlement judge procedures with respect to the establishment of a just, reasonable, and not unduly discriminatory or preferential cost-of-service rate. In addition, we will direct Mystic to make a compliance filing with respect to the future possible resale of gas it purchases for the Units and to correct a formulary error.

I. Background

2. ISO-NE has authority, under Market Rule 1,² to negotiate agreements for the purchase of electric energy at cost-based rates from generation facilities that ISO-NE

¹ See 16 U.S.C. § 824d (2000); 18 C.F.R. § 35.3 (2005).

² Market Rule 1 permits ISO-NE to negotiate contracts for the supply of power at cost-based rates to keep a generating facility in operation when the facility is needed for reliability in New England. Market Rule 1, section III, Appendix A, at III.A.6.2 and section III, Appendix A, Exhibit 2, at 3.3.

identifies as being necessary to ensure reliability, but that are unable to recover their operating costs under current market conditions.³

II. Mystic's Filing

A. The Need for an RMR Agreement

3. Mystic Units 8 and 9 are located in Everett, Massachusetts, and have a combined winter capacity of 1,658 MW. Mystic 8 began commercial operation in April 2003, and Mystic 9 began commercial operation in June 2003. Both Units are in the Northeast Massachusetts/Boston load pocket. Mystic sells the output of each Unit to Boston Generating, LLC (Boston Generating), which, in turn, sells the output to Sempra Energy Trading Corp. (Sempra) under a marketing agreement. Sempra markets the Units' output through bilateral trades and into the ISO-NE spot electricity markets.⁴

4. Mystic submits that it meets the criteria for RMR treatment and thus is entitled to cost-of-service rates. It states that ISO-NE has determined that Mystic 8 and Mystic 9 are needed to maintain reliability in the Boston Import Area,⁵ and that the Commission should accept ISO-NE's reliability determination, given the limited availability of firm gas supply to electric generating facilities in the Northeast. It states that it has long-term firm gas supplies that are delivered at a liquefied natural gas (LNG) terminal located next to its facility, and, thus, is uniquely situated to meet ISO-NE's reliability needs.⁶

5. Mystic further states that neither Mystic 8 nor Mystic 9 has been able to adequately recover its costs since a group of lenders acquired the Units in 2004,⁷ and that

³ See, e.g., *Milford Power Company, LLC* 110 FERC ¶ 61,299 (*Milford I*), order on reh'g, 112 FERC ¶ 61,154 (2005) (*Milford II*).

⁴ Mystic Transmittal Letter at 5.

⁵ *Id.* at 7-8 and Exhibits D & E.

⁶ Mystic Transmittal Letter at 8.

⁷ *Id.* In 2004, a group of lenders acquired Boston Generating, the parent company of Mystic and its affiliated generation project companies, from a subsidiary of Exelon Corp. as part of a settlement in lieu of foreclosure due to Boston Generating's default under a credit agreement with the lenders. *Id.* at n.22.

a detailed forecast indicates that these Units will continue to under-recover their costs in the future.⁸ Mystic states that Mystic Units 8 and 9 experienced a net loss of \$17.3 million in the fiscal year ending December 31, 2004, which was the first full year of their operation and is the test year for purposes of cost-of-service calculations.⁹ Mystic states that its Units often do not operate in merit,¹⁰ and that even with extensive self-scheduling¹¹ and out-of-merit commitments for reliability, the Units' capacity factors over the 12-month period from October 2004 to September 2005 were 51.9 percent for Mystic Unit 8 and 51.8 percent for Mystic Unit 9. It further states that, even under the most optimistic projections, the Units will continue to earn insufficient revenues in 2006.¹²

B. The Components of the Proposed RMR Agreement

1. Liquidated Damages and Self-Scheduling

6. Mystic states that the proposed RMR Agreement is substantially similar to ISO-NE's *pro forma* Cost-of-Service Agreement, with one exception, which relates to fuel costs. Mystic notes that it has a long-term gas supply contract with Distrigas of Massachusetts (Distrigas), and that, to guarantee firm transportation of gas to the Mystic Units, Mystic sited its generation next to Distrigas' LNG facility. According to Mystic, this arrangement reduces the risk of interruption to Mystic's supply of natural gas, while at the same time providing an anchor tenant for the expansion of the Distrigas facility.¹³

7. Mystic states that, under its contract with Distrigas, it has a Firm Weekly Quantity of 1,400,000 MMBtu per week that it must take to avoid paying liquidated damages, which are 25 percent of the contract price for the difference between 1,400,000 MMBtu

⁸ *Id.* at 8-10.

⁹ *Id.* at 9.

¹⁰ A generator operates in merit when it is scheduled under normal conditions.

¹¹ Self-scheduling is scheduling to operate other than at ISO-NE's direction.

¹² Mystic Transmittal Letter at 9-10.

¹³ *Id.* at 12.

and the amount of gas Mystic took during the relevant week.¹⁴ In return for agreeing to this must-take provision, Mystic receives a guaranteed supply of gas and firm delivery, and pays \$0.20/MMBtu less than the Algonquin Citygate price.¹⁵

8. Mystic proposes to absorb the risk of liquidated damages in return for the ability to self-schedule its Units.¹⁶ Mystic submits that this approach would result in lower costs for load in comparison to a true-up approach. It would also allow the Mystic Units to burn additional gas and thereby reduce, if not eliminate, liquidated damages.¹⁷

9. Section 3.2 of the *pro forma* Cost-of-Service Agreement prohibits the self-scheduling of facilities under RMR Agreements.¹⁸ Mystic has not adopted this section of the *pro forma* Cost-of-Service Agreement; rather, Section 3.2.4 of the proposed RMR Agreement provides that the Mystic Units shall self-schedule. Mystic states that ISO-NE supports the modification to the *pro forma* Cost-of-Service Agreement allowing the Mystic Units to self-schedule.¹⁹

10. Mystic asserts that allowing its Units to self-schedule increases efficiency and benefits load, since load will not be exposed to liquidated damages and will always pay the lesser of the Locational Marginal Price (LMP) or the Stipulated Bid Cost²⁰ for electric energy that the Units generate when self-scheduling.

¹⁴ *Id.* According to Mystic, Distrigas relies on the must-take provision of the contract to schedule LNG tanker deliveries weeks or months in advance. *Id.* at n.31.

¹⁵ *Id.* at 12.

¹⁶ *Id.* at 14.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ The Stipulated Bid Costs are self-adjusting rates that include formulae and costs for fuel, variable operating and maintenance (O&M), and environmental allowances that Mystic and ISO-NE have agreed upon.

2. Components of the Monthly Fixed-Cost Charge

11. Under the proposed RMR Agreement, Mystic would provide reliability service for ISO-NE in exchange for a Monthly Fixed-Cost Charge determined under Schedule 4 of the Agreement. The Monthly Fixed-Cost Charge is a cost-of-service charge based on a 12-month test year ending December 31, 2004. Mystic states that test year O&M expenses and end-of-period balance sheet items are actual amounts for 2004.²¹

12. The Revenue Requirement for each of the Mystic Units (8 and 9) is the sum of Return on Rate Base, Income Tax, Fixed O&M, Depreciation, and Taxes Other Than Income Taxes.²²

13. Mystic states that it does not issue publicly traded stock and is not subject to traditional rate regulation.²³ It has adopted a capital structure of 50 percent debt and 50 percent equity and a return on equity (ROE) of 10.88 percent. Mystic states that the Commission has approved this capital structure and ROE for similar entities providing reliability services in the ISO-NE service area.²⁴

14. Under section 3.2 of the proposed RMR Agreement, Mystic will submit bids based on the Stipulated Bid Cost for energy and ancillary services that Mystic Units 8 and 9 generate. The proposed RMR Agreement incorporates directly into the Monthly Fixed-Cost Charge certain extraordinary variable costs that are not reflected in the Stipulated

²¹ Mystic Transmittal Letter at 16.

²² Return is the product of Rate of Return times Rate Base, where Rate Base is Net Plant (Gross Plant net of Accumulated Depreciation), less Accumulated Deferred Income Taxes, plus additions to Rate Base.

²³ Mystic Transmittal Letter at 16.

²⁴ *Id.* at 16 & n.36. Mystic cites *Devon Power Company*, 104 FERC ¶ 61,123 at P 48-49 (2003); *Devon Power LLC*, 106 FERC ¶ 61,264 at P 23 (2004) ; *ISO New England, Inc.*, 108 FERC ¶ 61,272 at P 14 (2004); *PSEG Power Connecticut, LLC*, 110 FERC ¶ 61,020 at P 45 (*PSEG I*); *order on reh'g*, 110 FERC ¶ 61,441 (*PSEG II*); *order denying reh'g*, 113 FERC ¶ 61,210 (2005); *Bridgeport Energy, LLC*, 112 FERC ¶ 61,077 at P 48 (*Bridgeport I*), *reh'g denied*, 113 FERC ¶ 61,311 (2005) (*Bridgeport II*).

Bid Costs.²⁵ Mystic will credit market revenues in excess of the Stipulated Bid Costs (inframarginal revenues) and any other revenues related to the Mystic Units against the Monthly Fixed-Cost Charge, thus reducing the charge for a particular month.

C. Term of the Proposed RMR Agreement

15. Mystic asks that the Commission allow the proposed RMR Agreement to become effective on January 1, 2006 and expire on the day before a Locational Installed Capacity (LICAP) mechanism encompassing the two Units becomes effective. If ISO-NE finds that one or both of the Units is no longer needed for reliability, the Agreement states that ISO-NE may terminate the proposed RMR Agreement with respect to either or both Units after a 120-day notice period.²⁶

III. Notice of Filing, Interventions, Comments, and Protests

16. Notice of Mystic's filing was published in the *Federal Register*, 71 Fed. Reg. 2212 (2006), with interventions and protests due on or before January 19, 2006. ISO-NE filed a timely motion to intervene with no substantive comments. NSTAR Electric and Gas Corporation (NSTAR); New England Power Pool Participants Committee (NEPOOL);²⁷ Massachusetts Municipal Wholesale Electric Company, Reading Municipal Light Department, Wellesley Municipal Light Plant, and Concord Municipal Light Plant (collectively, Municipals); and the Massachusetts Attorney General (Mass AG) filed

²⁵ Mystic Transmittal Letter at 17 & n.37. These costs include penalties that Mystic is assessed under a Long-Term Service Agreement with its turbine/generator vendor associated with trips after a turbine has experienced 100 starts in a maintenance cycle; these penalties are paid in addition to the Monthly Fixed-Cost Charge.

Additionally, Schedule 5 provides that any such excess startup costs that occur when Mystic starts in a 1x1 configuration will be subtracted from the Monthly Fixed-Cost Charge.

²⁶ Mystic Transmittal Letter at 18.

²⁷ NEPOOL states that it neither supports nor opposes the proposed RMR Agreement, and has not reviewed variations between it and the *pro forma* Cost-of-Service Agreement and the proposed cost-based rates. NEPOOL urges the Commission to consider carefully the proposed rates and changes to the *pro forma* Cost-of-Service Agreement.

timely interventions and protests or comments. On January 25, 2006, NSTAR filed an erratum to its January 19, 2006 filing. On January 30, 2006, NRG Power Marketing, Inc., Connecticut Jet Power LLC, Devon Power LLC, Middletown Power LLC, Montville Power LLC, Norwalk Power LLC, and Somerset Power LLC (collectively, the “NRG Companies”) filed a motion to intervene out-of-time. On February 2, 2006, ISO-NE filed an answer to protests on the question of reliability. On February 3, 2006, Mystic filed an answer to protests. On February 10, 2006, ISO-NE filed a Motion to Lodge an answer that it filed in *Bridgeport Energy, LLC*, Docket No. ER05-611-002 and ER05-611-003. On February 17, 2006, Municipals filed an answer to Mystic’s answer and ISO-NE’s Motion to Lodge answer and NSTAR filed an answer to Mystic’s answer.

IV. Discussion

A. Procedural Matters

17. 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. Given the early stage of the proceeding, the lack of undue prejudice or delay and the NRG Companies’ interest, we find good cause to grant, under Rule 214, their unopposed, untimely motion to intervene in this proceeding.

18. Rule 213(a)(2) of the Commission’s Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2005), prohibits answers to protests unless otherwise ordered by the decisional authority. We will accept ISO-NE’s, Mystic’s, Municipals and NSTAR’s answers because they have provided information that assisted us in our decision-making process.

B. Reliability Determination

Comments

19. Municipals state that the Commission has held that, in order to be eligible for an RMR Agreement, a generator must demonstrate that its units are needed for reliability. Municipals state that Mystic’s showing on this point, the “Summary of System Planning Reports” that ISO-NE prepared, is out of date. Municipals argue that this supporting document fails to take into account significant system improvements that are either currently in place or soon to be completed. They also say that it assumes facility retirements that have neither occurred nor will occur during the proposed term of the RMR Agreement. Municipals ask the Commission to direct Mystic to seek an accurate reliability determination from ISO-NE.

ISO-NE Answer

20. ISO-NE answers that intervenors are relying on not yet completed projects to argue that ISO-NE's previous reliability determination for the Mystic units is inaccurate. Further, ISO-NE notes that these types of additions do not change the bulk power system in the New England area as it existed in December 2004, when ISO-NE prepared its system summary, which showed that the Mystic Units are needed for reliability.²⁸

Mystic Answer

21. Mystic argues that its Units are in fact needed for reliability. It notes that ISO-NE has found that ISO-NE needs the Mystic Units both for operating reserves and for voltage control.²⁹ Mystic notes that in 2006, predicted load levels will be nearly 200 MW higher than they were in 2004, and there have been no capacity additions since that time.³⁰

Commission Determination

22. Under Market Rule 1, ISO-NE has the authority to determine whether a generator is needed for reliability purposes, which is a prerequisite for negotiating an RMR Agreement.³¹ In several prior orders, the Commission, based on a review of the supporting documentation, has agreed with ISO-NE's reliability determination.³² Here, we agree that ISO-NE has properly found that the Units are needed for reliability. We reject as unpersuasive intervenors' claims that a new and updated supporting study is necessary. We agree with ISO-NE that the system changes that Municipals claim need to

²⁸ ISO-NE Answer at 5-7. ISO-NE adds that "there have been no major transmission or generation projects that would have changed the need for Mystic's considerable generating output in the Boston area." *Id.* at 7.

²⁹ Mystic Answer at 5 (*citing* Summary of System Planning Reports Supporting the Need for Mystic Units 7, 8 and 9 for System Reliability at 1-2).

³⁰ Mystic Answer at 6.

³¹ Market Rule 1, section III, Appendix A, at III.A.6.2 and section III, Appendix A, Exhibit 2, at 3.3.

³² *E.g.*, *PSEG I* at P 19; *Milford I*, at P 42; *Milford II*, at P 14, 18; *Bridgeport II* at P 8.

be reflected in a new supporting study would not change ISO-NE's reliability determination. Therefore, we reject the Municipals' request that Mystic seek a new reliability determination from ISO-NE.

C. Whether Units Will Recover Their Costs (Facility Costs Test)

Comments

23. Municipals state that Mystic is asking the Commission to approve an enormous shift of risk from Mystic to Northeast Massachusetts consumers and that the market distortions resulting from approval of Mystic's requested RMR Agreement would be substantial. Municipals state that Mystic Units 8 and 9 are new, reasonably efficient merchant generation plants that were built precisely because sophisticated investors expected that the Units would be profitable. They add that Mystic's investors understood that there was no guarantee that Mystic would be able to earn a profit.

24. Municipals surmise that the difficulty that Mystic Units 8 and 9 are having in competing in the market has nothing to do with the Units' operational efficiency or a market design flaw. Instead, investors simply made poor decisions. Municipals state that the data contained in Mystic's filing show that for 2004, Mystic Units 8 and 9 produced revenues well in excess of their "facility costs,"³³ and that the Mystic Units' revenues for the first nine months of 2005 are on pace to substantially exceed 2004 revenues.

25. Municipals also state that Mystic witness Robert Stoddard's Fundamentals Forecast and Forward Price Forecast analyses, which were used to forecast Mystic's net operating margin for 2006, are flawed. The Fundamentals Forecast understates the substantial revenues Mystic earns through uplift charges, and the Forward Price Forecast uses incorrect assumptions. According to Municipals, the Forward Price Forecast does not support Mystic's claim that it needs an RMR agreement in order to recover its facilities' costs. Also, Mass AG states that Mystic's historical capacity factor is significantly higher than the 35 percent capacity factor used to predict future revenues.

26. NSTAR states that Mystic has failed to show that the Units are eligible for RMR treatment, since there is no showing of likely shutdown or credible evidence of financial distress. NSTAR argues that over the long term, the Units will realize the financial

³³ Facility costs are costs ordinarily necessary to keep a facility available. *Bridgeport I* at P 35.

benefits contemplated by Mystic's owners when they purchased the Mystic Units in 2003.

27. NSTAR states that Mystic's facility cost analysis fails to support its claim for RMR relief because it includes items that the Commission has determined are not properly part of a facility cost analysis. NSTAR also states that Mystic has either inadequately explained or supported, or not explained at all many of the items that it has included in the study. It says that Mystic will earn sufficient revenues using market-based rates to meet its going-forward facility costs.

28. Mass AG states that applicants have not demonstrated that Mystic Units 8 and 9 are eligible for RMR treatment. Mass AG submits that Mystic has improperly included certain debt-service obligations in its facility cost analysis.

Mystic's Answer

29. Mystic responds that, by its calculations, the facility costs of the Units exceed Mystic's total revenues in 2004 by \$17.3 million and in 2005 by \$56.6 million. Mystic forecasts that the facility costs will exceed its total revenues in 2006 by up to \$80 million. It says that the Commission has recognized that existing market rules in New England do not adequately compensate generators, particularly those in the Boston area, and that location-specific payments are necessary to keep generators running.³⁴

30. Mystic argues that if a generating unit fails to recover its facility costs from the market and is needed for reliability, RMR treatment is appropriate. Mystic states that the Commission has consistently ruled that "under the current market rules, submitting a request to deactivate pursuant to section 18.4 of the Restated NEPOOL Agreement is not a prerequisite for receiving RMR treatment."³⁵ Mystic acknowledges that it used a 35 percent capacity factor for 2006 (although it experienced a 52 percent capacity factor for the 12 months ending September 2005),³⁶ and that it did not factor in uplift charges.³⁷ It

³⁴ Mystic Answer at 8 (*citing Devon Power LLC*, 103 FERC ¶ 61,082 at P 31, 37 (2003), *order on reh'g*, 104 FERC ¶ 61,123 (2003)).

³⁵ Mystic Answer at 9 (*citing PSEG I* at P 19, *Devon Power LLC*, 109 FERC ¶ 61,154 at P 27 (2004)).

³⁶ *Compare* Mystic Transmittal Letter at 9-10 *with* Mystic Answer at 9.

³⁷ Mystic Answer at 10.

also claims that it inverted the summer and winter ratings for the Units in its forecasts,³⁸ but argues that, even correcting for these factors, the Mystic Units will not even come close to recovering their facility costs in 2006.³⁹

31. Mystic further states that it properly included debt-service in its facilities' cost study⁴⁰ and that it properly excluded potential profits from the sale of gas, since Distrigas is preventing Mystic from reselling gas.⁴¹

Commission Determination

32. We will address first whether Mystic has shown that it will not recover its facility costs for the Units. As in *Bridgeport*⁴² and *Berkshire I*,⁴³ the Commission will compare facility costs such as fixed O&M, Administrative and General (A&G), and taxes to revenues earned in the energy and capacity markets in determining whether a proposed RMR Agreement is necessary for a generating facility to remain operational. The Commission will also include Mystic's debt-service payments in the cost-of-service comparison. To avoid compromising the reliability of a unit, the Commission must consider debt-service costs, just as we consider any other fixed costs.⁴⁴ The Commission finds that, although Mystic makes its debt-service payments to its parent company (reducing the likelihood of foreclosure), they are still obligations that are unique to these Units and must be serviced regardless of whether the Units operate. As such, there is no basis for excluding these costs. Based on Mystic's application, we find that Mystic has adequately demonstrated that the Units are not able to recover their facility costs and qualify for an RMR Agreement.

³⁸ *Id.* at 11.

³⁹ *Id.* at 9-17.

⁴⁰ *Id.* at 17-18 (citing *Berkshire Power Company, LLC*, 112 FERC ¶ 61,253 at P 25 (2005) (*Berkshire I*), order on reh'g, 114 FERC ¶ 61,099 at P 7 (2006) (*Berkshire II*)).

⁴¹ Mystic Answer at 16.

⁴² *Bridgeport I* at P 36.

⁴³ *Berkshire I* at P 25.

⁴⁴ *Berkshire II* at P 7.

33. Additionally, we disagree with NSTAR that the Mystic Units may not receive RMR treatment because their shutdown is not imminent. We have previously held that submitting a request to deactivate under section 18.4 of the NEPOOL Agreement is not a prerequisite to consideration for RMR treatment,⁴⁵ and we will not revisit this issue at this time.

D. Specific Cost-of-Service Elements

1. General Issues

Comments

34. Municipals state that Mystic witness Theodore Horton's testimony neither supports nor explains significant increases in expense components between 2004 and 2005, or a decline in credits received in 2004. Municipals argue that the Commission should obtain more evidence before approving charges of the magnitude that Mystic is requesting.

35. NSTAR also states that Mystic has failed to support its cost-of-service analysis, that the rates are excessive, are based upon a non-representative, hypothetical capital structure, and contain unsupported costs and cost-of-capital claims. NSTAR contends that required revisions to Mystic's cost-of-service data would significantly reduce the proposed RMR rates.

36. NSTAR also asserts that the Commission should condition any RMR relief that it allows to Mystic. NSTAR, Municipals, and Mass AG ask the Commission to limit RMR treatment to a "going-forward cost" alternative, under which Mystic would be able to recover only its actual and reasonable out-of-pocket costs incurred during the term of the agreement. For these purposes, "going-forward costs" are fixed O&M, A&G, and Tax Expenses.⁴⁶ According to these intervenors, Mystic should recover Capital Costs (*i.e.*, return of and return on investment) from market-related revenues. Additionally, the intervenors assert that the Commission should require Mystic to incorporate a levelized Rate Base into Mystic's cost-of-service.

⁴⁵ *PSEG I* at P 19; *Devon Power LLC*, 109 FERC ¶ 61,154 at P 27 (2004).

⁴⁶ Municipals Protest at 50. *See also* NSTAR Protest at 28.

37. Mass AG states that Mystic fails to support its cost-of-service analysis. Mass AG points out that Mystic has submitted audited financial statements only for the years 2002 and 2003, not for the proposed test year of 2004. Mass AG also alleges that it is impossible to determine from the audited financial statements the revenue, costs or other relevant financial information specific to the Mystic 8 or 9 Units.⁴⁷ Mass AG states that the Commission should require Mystic to update its filed test year costs for calendar year 2005. It also states that Mystic's facility cost analysis is inconsistent with its prior filing in Docket No. ER05-1304-000.

38. Mass AG also maintains that Mystic should use its actual capital structure (which, as of October 31, 2005, was approximately 76 percent long-term debt and 24 percent equity), not a hypothetical 50/50 capital structure. It claims that, based on Mystic's actual capital structure, Mystic's pre-tax cost-of-capital should be 11.47 percent, rather than the 12.57 percent that Mystic is proposing to use, based on a capital structure that it does not possess.

Mystic's Answer

39. Mystic answers that the Commission has found that a 10.88 percent ROE is appropriate for facilities providing reliability services to ISO-NE under RMR Agreements during the period before LICAP implementation. It asks the Commission to either summarily affirm the use of a 10.88 percent ROE based on a hypothetical 50/50 percent capital structure, or set the issue of an appropriate ROE for hearing.⁴⁸

2. Affiliate Abuse and Cost-of-Debt

40. Several intervenors raise the issue of affiliate abuse. According to NSTAR, Mystic provides no evidence of the financial arrangements and obligations involving its parent and its parent's subsidiaries, which own the Mystic 7 and Fore River Units. NSTAR maintains that the Commission should direct Mystic to prove the absence of affiliate abuse and require Mystic, its parent company, and its parent's subsidiaries to adopt a code of conduct to ensure that Mystic's parent and its affiliates provide non-power services to Mystic at the lower of cost or market value. NSTAR also asks the Commission to condition RMR status to prevent the exercise of market power. Mass AG

⁴⁷ See also NSTAR Protest at 9.

⁴⁸ Mystic Answer at 25.

says that Mystic fails to provide sufficient information related to the long-term debt shared between Mystic and Fore River.

Mystic's Answer

41. Mystic responds that its debt costs are an allocation of the total debt-service obligations of the Boston Generating projects (which include Fore River), based on Mystic's relative share of net property, plant and equipment. Mystic adds that Boston Generating and its lenders negotiated the underlying lending arrangements at arms-length.⁴⁹ It concludes that if NSTAR believes that Mystic may over-recover its debt costs through RMR rates, NSTAR can pursue that concern during settlement procedures or at hearing.⁵⁰

3. Fuel Index Formula and Long-Term Service Agreement Penalties

42. Municipals state that under the proposed RMR Agreement, Mystic would be paid a fuel cost component that is greater than Mystic's actual fuel costs under the Distringas contract.⁵¹ The Schedule 1, Fuel Price Index is set at:

$$\text{Fuel Index} = 100\% \times (\text{Algonquin, city-gates})$$

43. Municipals assert that Mystic actually pays \$0.20/MMBtu less than this price and, therefore, would be receiving a payment that is greater than its actual fuel costs for each unit of gas burned when Mystic's Stipulated Bids are accepted by ISO-NE.

44. Municipals also argue that the proposed RMR Agreement requires ratepayers to subsidize Mystic's mitigation of its liquidated damages by allowing Mystic to externalize the Long-Term Service Agreement penalty costs associated with additional unit starts incurred in connection with self-scheduling to mitigate liquidated damages. Municipals recommend that ratepayers only bear Long-Term Service Agreement penalty costs to the

⁴⁹ *Id.* at 20.

⁵⁰ *Id.* at n.42.

⁵¹ Municipals' Protest at 69.

extent that the number of *ISO-called* starts exceeds the Long-Term Service Agreement penalty threshold of 100 starts per maintenance cycle.⁵²

Commission Determination

45. As we discuss below in more detail, Mystic's proposed RMR Agreement raises issues of material fact that cannot be resolved based on the record before us, and are more appropriately addressed in the hearing and settlement judge procedures ordered below.

46. Our preliminary analysis indicates that the rates in Mystic's proposed RMR Agreement have not been shown to be just and reasonable and may be unjust, unreasonable, unduly discriminatory or preferential, or otherwise unlawful. Therefore, we will accept Mystic's proposed RMR Agreement for filing, suspend it for a nominal period, make it effective January 1, 2006, as requested, subject to refund, and set it for hearing and settlement judge procedures.⁵³

47. We will reject the request for a five-month suspension period. Where an entity does not have a firm, cost-based rate on file with the Commission and, instead, charges market-based rates, which can vary, we cannot determine whether a proposed cost-based rate would be a rate increase at any given time.⁵⁴ Because we cannot determine whether Mystic's proposed RMR rates are substantially excessive, we will decline to impose a five-month suspension period.⁵⁵ However, we will suspend the rates for a nominal period. While the hearing and settlement judge procedures established in this order should consider the entire cost-of-service, the Commission will rule summarily on certain other aspects of the RMR Agreement, and provide additional guidance for the ordered hearing, as discussed below.

48. To provide the parties an opportunity to resolve these matters among themselves, we will hold the hearing in abeyance and direct settlement judge procedures, pursuant to Rule 603 of the Commission's Rules of Practice and Procedure.⁵⁶ If the parties desire,

⁵² *Id.* at 70.

⁵³ Our suspension and waiver analysis are discussed below.

⁵⁴ *PSEG II* at P 40.

⁵⁵ *Id.*; *Milford I* at P 23; *Bridgeport I* at P 73-75.

⁵⁶ 18 C.F.R. § 385.603 (2005).

they may, by mutual agreement, request a specific judge as the settlement judge in this proceeding; otherwise, the Chief Judge will select a judge for this purpose.⁵⁷ 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 commencement of a hearing by assigning the case to a presiding judge.

49. Consistent with our determinations in other RMR proceedings,⁵⁸ the Commission will reject the intervenors' request to limit cost recovery to going-forward costs or to a form of levelized costs. This issue has been fully litigated in prior proceedings and we will not revisit it here. As we have previously found, full cost-of-service recovery is consistent with the cost-of-service provisions of Market Rule 1⁵⁹ and thus appropriate for RMR Agreements. Providing only minimum, marginal, and variable cost recovery to the Units may not allow Mystic to maintain the Units so that they can continue to operate reliably. It would defeat the purpose of the RMR agreement, which is to ensure that the Units are available for reliability purposes. We note that the RMR Agreement requires that any inframarginal or "other" revenues that the Units earn in the market will be credited against the Monthly Fixed-Cost Charge.

50. While we have found that a 10.88 percent ROE is a conservative proxy for merchant generating facilities,⁶⁰ we have also stated that we would prefer to use an actual debt/equity ratio rather than a hypothetical one.⁶¹ We will, therefore, as we have in the

⁵⁷ If the parties decide to request a specific judge, they must make their joint request to the Chief Judge by telephone at (202) 502-8500 within five days of the date of this order. The Commission's web site contains a list of Commission judges and a summary of their backgrounds and experience (www.ferc.gov – click on Office of Administrative Law Judges).

⁵⁸ *Consolidated Edison Energy Massachusetts, Inc.*, 112 FERC ¶ 61,263 at P 40 (2005) (*Consolidated Edison*); *PSEG I* at P 30; *Milford I* at P 70; *Milford II* at P 28; *Bridgeport I* at P 46; *Berkshire I* at P 29.

⁵⁹ Market Rule 1, Appendix A, Exhibit 2, section 3.3.1.

⁶⁰ *Milford I* at P 72; *Milford II* at P 34; *PSEG II* at P 35; *Devon Power Company*, 104 FERC ¶ 61,123 at P 48-49 (2003).

⁶¹ *Milford I* at P 73.

past,⁶² include in the hearing and settlement judge instructions that Mystic's actual debt/equity ratio be determined.⁶³ The Commission further sets for the hearing and settlement judge a determination of Mystic's 2004 financial information necessary for a proper cost-of-service analysis.

51. The Commission agrees that Mystic has incorrectly stated the Fuel Index definition in Schedule 1. Mystic states in its transmittal letter that "[I]n return for this take-or-pay provision in its contract with DISTRIGAS, Mystic receives a guaranteed supply of gas (including firm transportation) and pays \$.20/MMBtu less than the Algonquin Citygate price."⁶⁴ Therefore, the Commission will require Mystic to make a compliance filing within 30 days of the date of this order to change the Fuel Price Index to state:

$$\text{Fuel Index} = 100\% \times (\$0.20/\text{MMBtu less than Algonquin, city-gates})$$

52. The proposed RMR Agreement allows Mystic to self-schedule its Units in order to mitigate its fuel costs. Self-scheduling allows Mystic the opportunity to operate when its Stipulated Bid Cost is greater than the LMP (a period when ISO-NE would not schedule the Mystic Units unless for reliability purposes) in order to mitigate or avoid the penalty for not meeting its gas Firm Weekly Quantity. We find that there are material issues of fact with respect to the Long-Term Service Agreement penalty charges that cannot be resolved on the record before us. Mystic must demonstrate that it takes into account the possibility of Long-Term Service Agreement penalty charges when it self-schedules to mitigate its gas liquidated damages.

E. Re-sale of Gas Provision

53. Mass AG states that Mystic fails to provide any information about its rights under its contract with DISTRIGAS to resell the gas that it purchases from DISTRIGAS. Mass AG

⁶² *Id.*

⁶³ In arriving at the 10.88 percent ROE as a suitable proxy ROE for RMR units, the Commission relied on a proxy group of five large, integrated, publicly traded utilities, rather than on a group of proxy merchant generators. *Id.* at P 72. Mystic indicates that an appropriate ROE for merchant generators like Mystic would probably be higher. Mystic Answer at 25.

⁶⁴ Mystic Transmittal Letter at 12.

states that the Commission should offset RMR rates with any revenues Mystic receives from the resale of gas.⁶⁵

54. Similarly, Municipals claim that Mystic proposes to depart from the *pro forma* RMR Agreement in section 3.1.2 to provide that “Revenues and charges associated with the Units’ gas supply agreements shall not be considered ‘related to the Resource’ for purposes of this paragraph.”⁶⁶ Municipals argue that the Commission should reject Mystic’s proposed deviation from the *pro forma* Cost-of-Service Agreement and require Mystic to credit to the Monthly Fixed-Cost Charge any revenues associated with gas it purchases from Distrigas and resells.

55. Mystic answers that no is offset possible, since Distrigas has prevented Mystic from selling any of the gas that Mystic buys under its contract with Distrigas.⁶⁷

Commission Determination

56. The Commission will require that Mystic modify its proposed departure from the *pro forma* Cost-of-Service Agreement in section 3.1.2. The Commission agrees that, to the extent that Mystic’s contract with Distrigas prevents it from reselling any gas, Mystic should exclude all charges and costs associated with liquidated damages under its gas supply agreements in its Stipulated Bids or in the calculation of the Monthly Fixed-Cost Charge, because Mystic is allowed to self-schedule its Units in return for assuming the responsibility of its gas related liquidated damages. However, the issue of whether Mystic has the right to sell any of the gas that it purchases under its contract with Distrigas is in litigation.⁶⁸ Therefore, to account for the possibility that Mystic in the future may have the right to resell gas, or have either Distrigas or an affiliated party sell the gas for Mystic, we will require Mystic to revise section 3.1.2 to propose an appropriate treatment of costs and revenues to reflect possible future sales of gas. We will direct Mystic, in its compliance filing, to modify section 3.1.2 as discussed above.

⁶⁵ Mass AG Protest at 6-7.

⁶⁶ *Id.* at 71 (*citing* section 3.1.2 of the proposed RMR Agreement).

⁶⁷ Mystic Answer at 16.

⁶⁸ Mystic Transmittal Letter at 12 n.31.

F. Waiver of Commission Requirements

57. Mystic requests waiver of any of the Commission's cost-of-service data requirements and any of the Commission's other regulations under part 35 as necessary for the proposed RMR Agreement to become effective as requested.

Comments

58. NSTAR contends that Mystic should be subject to the same reporting requirements as are traditional utilities who sell power at cost-based rates so that the Commission, NSTAR, and other affected parties will be able to monitor the costs on which Mystic's rates are based. It argues that Mystic's filing is patently deficient under section 35.13 of the Commission's regulations.⁶⁹ In addition, NSTAR asks the Commission to revoke the waivers previously granted to Mystic (when it received authority to charge market-based rates) of the accounting and other requirements of parts 41, 101 and 141 of the Commission's regulations.⁷⁰

59. Municipals state that there has been no regulatory scrutiny of the costs here. Municipals urge the Commission to deny the requested waiver of the Commission's cost-of-service data filing requirements.

Mystic's Answer

60. Mystic answers that the Commission has rejected requests to impose the accounting and reporting requirements and should do so again here, since the Mystic Units will continue to operate under market-based rate authority, on which the waivers are based.⁷¹

⁶⁹ 18 C.F.R. § 35.13 (2005).

⁷⁰ See *Sithe Fore River Development LLC & Sithe Mystic Development LLC*, unpublished Letter Order issued in Docket Nos. ER01-41-000 and ER01-42-000 (November 29, 2000); *Mystic I, LLC*, unpublished letter order issued in Docket Nos. ER04-657-000, *et al.* (June 4, 2004).

⁷¹ Mystic Answer at 28.

Commission Determination

61. Consistent with our precedent,⁷² we will deny the request to revoke waivers of parts 35, 41, 101, and 141 of the Commission's regulations. Although they may operate under the RMR Agreement, the Units will continue to operate generally under market-based rate authority. Under the RMR Agreement, Mystic will offset any market revenues against the Monthly Fixed-Cost Charge in the RMR Agreement.

G. Term of the RMR Agreement

62. NSTAR states that the requested term of the RMR Agreement (until the implementation of LICAP) is inconsistent with Market Rule 1. NSTAR asserts that, if LICAP is not implemented in the near future, Mystic could continue to collect RMR payments based on a cost-of-service period that may not reflect true operating costs. NSTAR and Mass AG argue that the Commission should set a specific end for the RMR Agreements at the earlier of LICAP implementation or one year from the effective date of the RMR Agreement.

63. Mystic answers that the Commission has addressed this issue repeatedly, finding that RMR Agreements should extend through the implementation of a LICAP mechanism (subject to ISO-NE's right to terminate earlier under appropriate circumstances).⁷³

Commission Determination

64. We will reject NSTAR's request as a collateral attack on prior Commission orders. In the LICAP proceeding, the Commission stated that it will consider RMR Agreements that are limited to a single term, expiring when the LICAP mechanism is implemented.⁷⁴ The proposed termination provisions of this agreement are consistent with prior

⁷² *E.g., Milford II* at P 39-41; *Consolidated Edison* at P 48.

⁷³ Mystic Answer at 26.

⁷⁴ *Devon Power LLC*, 107 FERC ¶ 61,240 at P 72, *order on reh'g*, 109 FERC ¶ 61,154 at P 25, 29 (2004).

Commission orders, including recently approved RMR Agreements in *Milford*,⁷⁵ *PSEG I*,⁷⁶ and *Bridgeport I*.⁷⁷

H. Effective Date and Suspension Period

65. Mystic requests waiver of the Commission's prior notice requirement⁷⁸ to allow the RMR Agreement to become effective on January 1, 2006. Mystic states that it was unable to file the RMR Agreement 60 days before that date because it did not complete RMR Agreement negotiations with ISO-NE until December 29, 2005. Mystic filed the proposed RMR Agreement that same day.

Comments

66. Municipals request that the Commission suspend the proposed RMR Agreement and make it effective subject to refund, and the outcome of an evidentiary hearing to determine whether the rates that Mystic proposes are just and reasonable. Municipals ask the Commission to deny the requested 60-day waiver of the Commission's prior notice requirement.

67. NSTAR similarly asks the Commission to suspend the proposed rates for the full five-month period permitted under the Federal Power Act (FPA)⁷⁹ and make them subject to refund.

68. Mass AG states that the Commission should reject Mystic's proposed RMR Agreement or suspend the rates for a reasonable time and set the issues for hearing, with discovery rights, to ensure that the rates ultimately approved by the Commission are just and reasonable.

⁷⁵ *Milford I* at P 81; *Milford II* at P 32.

⁷⁶ *PSEG I* at P 56.

⁷⁷ *Bridgeport II* at P 39.

⁷⁸ 16 U.S.C. § 824d (2000); 18 C.F.R. § 35.3 (2005).

⁷⁹ 18 U.S.C. § 824d (2000).

69. Municipals and NSTAR ask the Commission to reject Mystic's request for waiver of the prior notice requirement and to suspend the RMR Agreement for five months.⁸⁰

Mystic's Answer

70. Mystic answers that Units 8 and 9 satisfy the RMR criteria as discussed above. Mystic argues that the Commission should rule summarily that the Units qualify for RMR treatment. It says that the Commission should set the issue of the level of cost-of-service rates for hearing.⁸¹

Commission Determination

71. As we have explained in more detail above, a hearing and settlement judge procedures are warranted in this proceeding because there are issues of material fact regarding the determination of the cost of service that cannot be resolved on the record before us.

72. The Commission has granted waiver of the prior notice requirement where: (a) agreements are intended to permit operation by a generator that is needed to assure system reliability; (b) the applicant may only learn upon very short notice which units will be RMR units; and (c) the applicant might not be able to file 60 days before the commencement of service due to the short notice.⁸² Mystic and ISO-NE did not complete their negotiations regarding the proposed RMR Agreement until December 29, 2005. We note that under Market Rule 1, Mystic could not file the RMR Agreement until it had received the approval of ISO-NE and completed negotiations of the RMR Agreement. Mystic filed the proposed RMR Agreement promptly upon the completion of negotiations. Consistent with prior RMR proceedings, we will grant waiver of the prior notice requirement, and make the RMR Agreement effective on January 1, 2006, as requested.⁸³

⁸⁰ Municipals Protest at 74-76; NSTAR Protest at 36.

⁸¹ Mystic Answer at 3.

⁸² See *Mirant Americas Energy Marketing, L.P.*, 105 FERC ¶ 61,359 at P 14-16 (2003); *Milford I* at P 25; *Berkshire I* at P 27.

⁸³ *Milford I* at P 25; *Berkshire I* at P 27.

The Commission orders:

(A) The proposed RMR Agreement is hereby accepted for filing, and suspended for a nominal period, to become effective January 1, 2006, as requested, subject to refund, and subject to the compliance filing that we order in paragraph (F) below, as discussed in the body of this order.

(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 regulations under the Federal Power Act (18 C.F.R. Chapter I), a public hearing shall be held concerning the proposed RMR Agreement. However, the hearing shall be held in abeyance to provide time for settlement judge procedures, as discussed in Paragraphs (C) and (D).

(C) Pursuant to Rule 603 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.603 (2005), 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 within five (5) days of the date of this order.

(D) Within sixty days of the date of this order, the settlement judge shall file a report with the Commission and the Chief Judge 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 sixty (60) days thereafter, informing the Commission and the Chief Judge of the parties' progress toward settlement.

(E) If the settlement judge procedures fail and a trial-type evidentiary hearing is to be held, a presiding judge, to be designated by the Chief Judge, shall, within fifteen (15) days of the date of the presiding judge's designation, convene a prehearing conference in this proceeding in a hearing room of the 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 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.

(F) Mystic is hereby directed to submit a compliance filing within 30 days of the date of this order, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.