

138 FERC ¶ 61,121
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Philip D. Moeller, John R. Norris,
and Cheryl A. LaFleur.

Puget Sound Energy, Inc.

Docket No. EL10-71-000

ORDER ON PETITION FOR DECLARATORY ORDER

(Issued February 16, 2012)

1. On June 4, 2010, Puget Sound Energy, Inc. (Puget) filed a petition for declaratory order requesting that the Commission find that locational exchanges of electric power are permissible wholesale power transactions and not transmission transactions subject to an open access transmission tariff (OATT) (Puget Petition). On February 17, 2011, the Commission issued an order¹ deferring consideration of Puget's Petition pending the outcome of the Notice of Inquiry (NOI) related to locational exchanges in Docket No. RM11-9-000.² As discussed below, the Commission finds that when the simultaneous exchange transaction (as defined below) involves the marketing function of a public utility transmission provider, the public utility must seek prior approval from the Commission if the transaction involves its affiliated transmission provider's system.³ The Commission therefore denies Puget's petition, in part, with regard to proposed transactions involving the marketing function of a public utility transmission provider and its affiliated transmission provider's system. The Commission grants Puget's Petition, in part, with regard to all other simultaneous exchange transactions, which the

¹ *Puget Sound Energy, Inc.*, 134 FERC ¶ 61,122, at P 4 (2011) (February 2011 Order).

² *Locational Exchanges of Wholesale Electric Power*, 76 FR 10353 (Feb. 24, 2011), FERC Stats. and Regs. ¶ 35,570 (2011) (NOI). As discussed below, the Commission is terminating the proceedings in Docket No. RM11-9-000.

³ Involvement of the transmission provider's system means that one point of the simultaneous exchange is either within or on the border of the transmission provider's system.

Commission concludes do not require prior Commission approval beyond the necessary authorization under section 205 of the Federal Power Act for the sale for resale of electric energy.⁴

I. Background

A. Puget's Petition

2. Puget requests that the Commission issue a declaratory order finding that locational exchanges of power are wholesale power transactions, and are not transmission transactions that must be undertaken in accordance with an OATT. In the petition, Puget defines a locational exchange as:

...a pair of simultaneously arranged wholesale power transactions between the same counterparties in which party A sells electricity to party B at one location, and party B sells the same volume of electricity to party A at a different location with the same delivery period, but not necessarily at the same price.⁵

If the Commission does not adopt Puget's preferred declaration, Puget proposes that the Commission adopt an alternative declaration that:

Locational exchanges performed (a) to bypass a constraint on a transmission system or to reduce risks of transmission curtailment, or (b) to trade around locational power market price spreads, do not constitute transmission transactions that must be conducted under authority of an OATT, but rather are wholesale power sales transactions.⁶

3. Puget's requests include as wholesale power sales those locational exchanges in which the marketing function of a transmission provider engages in an exchange

⁴ As explained below, the Commission will continue to consider ways to enhance the transparency of these arrangements, including modification to the EQR reporting requirements, to ensure that they are not being utilized to circumvent Commission regulations.

⁵ Puget, Petition for Declaratory Order, Docket No. EL10-71-000, at p. 1 (filed June 4, 2010) (Puget's Petition).

⁶ *Id.* at 4.

involving the transmission provider's system. Puget claims that locational exchanges are common in the electric industry, particularly in the Pacific Northwest. However, Puget states that Puget has ceased to engage in new locational exchange arrangements following an audit of Puget's operations conducted by the Commission's Office of Enforcement in Docket No. PA07-1-000. Puget asserts that, based on the audit report issued in that docket, it is unable to determine whether the Commission would view all locational exchanges as transmission transactions undertaken in violation of the OATT.

4. Puget asserts that locational exchanges provide certain benefits. According to Puget, locational exchanges allow it to avoid transmission constraints existing in the Cascade Mountains for power moving from east to west. Puget asserts that these constraints occur because the majority of its generation assets are located east of the Cascades, while the majority of its load is located west of the Cascade Mountains. By using locational exchanges, Puget explains that it can buy power from a generator west of the Cascade Mountains and make a matching sale of power to that same generator east of the Cascade Mountains. Puget also states that locational exchanges facilitate the trading around price spreads at different hubs to optimize the value of power or transmission asset positions, avoid unnecessary transmission usage, eliminate scheduling burdens, and enhance deliverability of wind power resources to market from remote locations. Further, Puget claims that locational exchanges have been widespread for many years and asserts that there is no evidence of market problems caused by locational exchange transactions.

5. Puget states that only one prior Commission decision, *UAMPS*,⁷ has held that a transaction similar to a locational exchange constituted transmission service that must be provided pursuant to an OATT. However, Puget explains that in *El Paso*,⁸ the Commission accepted a "swap and purchase" agreement similar to a locational exchange. Puget contends that the *El Paso* order demonstrates that, except under the specific facts of *UAMPS*, locational exchanges are not treated as transmission transactions by the Commission.

6. Puget further adds that locational exchanges are distinguishable from buy-sell transactions discussed in Order No. 888.⁹ Puget emphasizes that locational exchanges

⁷ Puget's Petition at p. 9-11 (citing *United Associated Municipal Power Systems v. PacifiCorp*, 83 FERC ¶ 61,337 (1998) (*UAMPS*), *reh'g*, 87 FERC ¶ 61,044 (1999) (*UAMPS Rehearing*) (collectively, *UAMPS Orders*)).

⁸ *El Paso Electric Co.*, 115 FERC ¶ 61,312 (2006).

⁹ Puget's Petition at p. 13 (citing *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of*

are not traditional “buy-sell” transactions in which: (1) Party A sells power to Party B at Point X; (2) Party B delivers that power to Point Y using its own transmission rights; and (3) Party B sells the power back to Party A at Point Y. Puget stipulates that such buy-sell transactions, where one party is simply substituted for the other party as shipper, are prohibited by the Commission pursuant to Order No. 888. Puget states that locational exchanges differ from buy-sells because, in a locational exchange, each party owns or controls rights to power at the respective sides of the transaction. Puget also seeks to distinguish Order No. 888, stating that in Order No. 888 the Commission merely reaffirmed its jurisdiction over the transmission component of certain retail buy-sell transactions. Puget also distinguishes buy-sell transactions that raise concern in the gas industry from locational exchanges, because buy-sell transactions are undertaken to avoid regulatory jurisdiction and oversight. By contrast, Puget explains, in the electric industry the Commission maintains jurisdiction over locational exchanges regardless of whether the transactions are characterized as transmission or wholesale power sales.

7. Puget claims that the Commission considered locational exchanges as part of its rulemaking for the establishment of the Commission’s Market Behavior Rules and determined that such exchanges were not “wash trades,” as defined by the Commission.¹⁰ Puget further contends that the Commission had deferred its determination regarding the regulatory treatment of locational exchanges in Order No. 717 concerning Standards of Conduct for Transmission Providers, when the Commission stated that it is “not always obvious whether such exchanges should be classified as transmission or as the purchase and sale of generation” for Standards of Conduct purposes.¹¹

Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, FERC Stats. & Regs. ¶ 31,036, at 31,785 (1996), *order on reh’g*, Order No. 888-A, FERC Stats. & Regs. ¶ 31,048, *order on reh’g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh’g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff’d in relevant part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *aff’d sub nom. New York v. FERC*, 535 U.S. 1 (2002)).

¹⁰ Puget’s Petition at p. 15 (citing *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 105 FERC ¶ 61,218, at P 46-58 (2003) (2003 MBR Investigation Order) (defining wash trades as “prearranged offsetting trades of the same product among the same parties, which involve no economic risk and no net change in beneficial ownership[.]”)).

¹¹ Puget’s Petition at p. 16 (citing *Standards of Conduct for Transmission Providers*, Order No. 717, FERC Stats. & Regs. ¶ 31,280 at P 82 (2008)).

B. Comments on Puget's Petition

8. Xcel Energy Services Inc. (Xcel),¹² Financial Institutions Energy Group (Financial Institutions),¹³ and Portland General Electric Company (PGE) filed comments supporting Puget's petition. PGE agrees with Puget that locational exchanges are common arrangements, particularly in western power markets, and that locational exchanges alleviate capacity constraints and enhance the deliverability of variable resources.¹⁴ Similarly, Xcel states that locational exchanges allow parties to take advantage of price spreads, to optimize the value of power or transmission positions, and to utilize resources in their portfolios that may be distant from native loads.¹⁵ Financial Institutions contends that the simultaneous nature of the locational transactions should not have any bearing on whether such transactions are deemed transmission service or power trades.¹⁶

9. Financial Institutions also asserts that the Commission has been aware that the industry has been using locational exchanges, claiming that Puget reported locational exchanges in its financial reports to the Commission and its electric quarterly transaction reports (EQR). Moreover, Financial Institutions contends that an administrative law judge's initial decision has acknowledged the use of locational exchanges and characterized the transactions as wholesale power trades.¹⁷ Financial Institutions asserts that the Commission did not correct the administrative law judge's characterization of

¹² Xcel filed its comments on behalf of itself and the Xcel Energy Operating Companies. Xcel is the service company for the Xcel Energy Inc. holding company system and, *inter alia*, represents the Xcel Energy Operating Companies in matters before the Commission. The Xcel Energy Operating Companies are Northern State Power Company, a Minnesota corporation; Northern States Power Company, a Wisconsin corporation; Public Service Company of Colorado; and Southwestern Public Service Company.

¹³ Financial Institutions include investment and commercial banks that provide a broad range of financial services to all segments of the U.S. and global economy.

¹⁴ Financial Institutions Comments at 8-9; PGE Comments at 2; Xcel Comments at 3-4.

¹⁵ Xcel Comments at 3.

¹⁶ Financial Institutions Comments at 7.

¹⁷ Financial Institutions Comments at 3 (citing *Nevada Power*, 101 FERC ¶ 63,031, at 65,323 (2002)).

locational exchanges as power trades; therefore, Financial Institutions asserts that the Commission has not treated locational exchanges as transmission service.¹⁸

C. February 2011 Order

10. On February 17, 2011,¹⁹ the Commission deferred action regarding Puget's petition pending the outcome of the NOI issued in Docket No. RM11-9-000.²⁰ In the February 2011 Order, the Commission determined that the record in the Puget proceeding was insufficient to support a Commission determination regarding Puget's petition and that Puget's filing raised significant policy issues that would be examined in the NOI.²¹

II. Discussion

11. The Commission finds that when a simultaneous exchange transaction, as defined below, involves the marketing function of a public utility transmission provider, the public utility must seek prior approval from the Commission if the transaction involves its affiliated transmission provider's system.²² The Commission therefore denies Puget's petition, in part, with regard to simultaneous exchange transactions involving the marketing function of a public utility transmission provider and its affiliated transmission provider's system. The Commission grants Puget's Petition, in part, with regard to all other simultaneous exchange transactions, which the Commission concludes do not require prior Commission approval.

12. Puget seeks guidance regarding a category of transactions that it refers to as locational exchanges, characterized by Puget as "a pair of simultaneously arranged wholesale power transactions between the same counterparties in which party A sells to party B at one location, and party B sells the same volume of electricity to party A at a different location with the same delivery period, but not necessarily at the same price." The Commission is concerned that Puget's focus on transactions with the *same* delivery

¹⁸ Financial Institutions Comments at 6-7.

¹⁹ February 2011 Order, 134 FERC ¶ 61,122 at P 4.

²⁰ NOI, 76 Fed. Reg. 10,353 (2011), FERC Stats. and Regs. ¶ 35,570.

²¹ In an order issued contemporaneously with this order, the Commission has terminated the NOI. 138 FERC ¶ 61,122 (2012).

²² Involvement of the transmission provider's system means that one point of the simultaneous exchange is either within or on the border of the transmission provider's system.

period may unduly restrict the category of transactions relevant to the analysis of issues raised in Puget's Petition. The Commission therefore refers herein to “simultaneous exchanges” that involve *overlapping* delivery periods, and defines such transactions as follows:

Simultaneous exchanges occur when a pair of simultaneously arranged (i.e., part of the same negotiations) wholesale power transactions between the same counterparties in which party A sells an electricity product to party B at one location and party B sells a similar electricity product to party A at a different location have an overlapping delivery period. The simultaneous exchange is the overlapping portion (both in volume and delivery period) of these wholesale power transactions.

This definition encompasses the types of transactions identified in Puget's Petition as locational exchanges as well as additional transactions in which the delivery periods overlap but are not identical.

13. The Commission's concern regarding simultaneous exchanges is that certain of these transactions may resemble transmission service because they involve a party placing power onto the power grid at one delivery point and then simultaneously receiving power at another delivery point. In addition, when such transactions involve the marketing function of a transmission provider, they may appear to enable the marketing function to effectively provide service on its transmission provider's system without the reservation of service on that system. A transmission provider's marketing function has a unique relationship with the transmission provider that is governed by the Commission's Standards of Conduct, which prohibit marketing function employees from conducting transmission functions²³ and prohibit many types of communication between the transmission function employees and marketing function employees.²⁴

14. The Commission is concerned that the marketing function of a transmission provider could utilize the complexity of simultaneous exchanges to effectively perform transmission functions where the transactions involve the transmission provider's system, circumventing Commission regulations involving open access transmission service. In certain circumstances, the transmission provider would continue to recover its full cost-of-service through its transmission rates, while the merchant affiliate could benefit from the additional revenues provided by the simultaneous exchange. Therefore, as a result of these concerns, we will not permit the marketing function of a transmission provider to

²³ 18 C.F.R. 358.5(b) (2011).

²⁴ *Id.* See also 18 C.F.R. 358.2(b) (2011).

engage in simultaneous exchanges involving that transmission provider's system absent prior Commission authorization as evaluated on a case-by-case basis.

15. The Commission's prior decisions involving simultaneous exchanges reflect the particular concern that certain types of simultaneous exchanges may enable the marketing function of a transmission provider to effectively provide transmission service. In *UAMPS*, the Commission prohibited an arrangement in which a transmission customer sold electricity to a transmission provider's merchant affiliate at one location, and the transmission provider's merchant affiliate sold the same volume of electricity to the transmission customer at a different location.²⁵ The Commission determined that the transaction effectuated transmission service and violated the separation of functions between the merchant affiliate and the transmission provider. The Commission explained:

The redispatch transaction offered by PacifiCorp's Merchant Function is, unquestionably, a transmission service; the sole result of the transaction is to deliver a [UAMPS] resource from a receipt point on PacifiCorp's system to a delivery point on PacifiCorp's system.²⁶

The Commission rejects Puget's contention that the *UAMPS Orders* are inapplicable to the Commission's evaluation of other simultaneous exchanges. These orders did not hold that all simultaneous exchange-like transactions outside the particular facts of the *UAMPS Orders* were permissible.²⁷ Rather, the *UAMPS Orders* suggest broader concerns related to simultaneous exchange-like transactions and separation of functions between the marketing function and the transmission function of the transmission provider.

16. While the Commission is concerned with simultaneous exchanges by a marketing function of a transmission provider involving the transmission provider's system, the

²⁵ *UAMPS*, 83 FERC at 62,367, *reh'g*, *UAMPS Rehearing*, 87 FERC at 61,187-88. *UAMPS* was operating on PacifiCorp's transmission system under a grandfathered agreement that pre-dated Order No. 888 and did not give *UAMPS* the right to demand redispatch. After PacifiCorp's transmission operator denied *UAMP*'s request for redispatch, *UAMPS* entered into the simultaneous exchange-like arrangement with PacifiCorp's merchant function.

²⁶ *UAMPS*, 83 FERC at 62,367, *reh'g*, *UAMPS Rehearing*, 87 FERC at 61,188.

²⁷ The Commission did not limit its determination in *UAMPS* to its facts but only clarified that *UAMPS* did not categorically prohibit a merchant affiliate from purchasing and reselling power. *UAMPS Rehearing*, 87 FERC at 61,188.

Commission has not prohibited all simultaneous exchange-like transactions involving marketing function affiliates. In *El Paso*, the Commission distinguished the transaction from the facts presented in the *UAMPS Orders* to permit the transaction between El Paso and Phelps Dodge.²⁸ For instance, the Commission identified facts indicating the presence of competitive alternatives to the marketing function affiliate in that particular simultaneous exchange transaction.²⁹ Given the specific facts in *El Paso*, the Commission's concern that its transmission service regulations were potentially being circumvented was alleviated, and the Commission allowed the transaction.

17. In consideration of this precedent, the Commission grants in part Puget's Petition with regard to simultaneous exchanges that do not involve the marketing function of a public utility transmission provider. That is, entities are permitted to engage in simultaneous exchanges without prior Commission approval (beyond the necessary authorization under section 205 of the Federal Power Act for the sale for resale of electric energy) if such transactions do not include the marketing function of a transmission provider conducting simultaneous exchange transactions involving that transmission provider's system. Because of our general concerns regarding the potential for simultaneous exchanges to effectively provide transmission service, the Commission will consider ways to enhance the transparency of these arrangements, including potential modifications to the EQR reporting requirements.

18. The Commission recognizes that, although both the *UAMPS Orders* and *El Paso* evinced concerns with simultaneous exchange-like arrangements involving marketing affiliates, the obligation of the marketing function of the transmission provider to seek pre-approval to engage in these transactions may have not been sufficiently clear. Accordingly, the Commission will not impose this obligation upon simultaneous exchanges that are or have been effective prior to the date of this order's issuance.

19. In light of our determinations above, the Commission declines to adopt Puget's proposed generic rule that all transactions defined by Puget as locational exchanges are permissible wholesale power transactions. In the alternative, Puget asks the Commission to define as wholesale power transactions, locational exchanges that (a) bypass a

²⁸ *El Paso*, 115 FERC ¶ 61,312 at P 18-22.

²⁹ The Commission observed that the generation substations at which the sales occurred and the lines interconnecting the substations were owned jointly by multiple parties, not just El Paso, and thus El Paso's counterparty could have obtained service from another source. *El Paso*, 115 FERC ¶ 61,312 at P 18. The Commission also observed that the swap could have been entered into with another power marketer instead of El Paso's marketing affiliate. *El Paso*, 115 FERC ¶ 61,312 at P 21.

constraint on a transmission system or to reduce risks of transmission curtailment or (b) trade around locational power market price spreads. The Commission rejects this alternative because, as discussed above, either of these broad categories of transactions could implicate our concerns about the marketing function's role in the transaction. Puget has not provided the type of specific information that would allow the Commission to evaluate any specific transaction involving the marketing function of a public utility transmission provider.³⁰ The denial of Puget's petition is without prejudice to Puget making a subsequent request providing greater detail regarding specific transactions involving the marketing function of the public utility transmission provider and its affiliated transmission provider's system. For example, in such a filing, Puget could (1) identify all the parties to the transaction, (2) specify the delivery and receipt points involved, (3) describe the terms and conditions, including any charges or compensation, (4) provide details of ultimate power sources and sinks, (5) identify available competitive alternatives (accounting for physical constraints or whether transmission service for a related transaction has previously been denied), (6) describe the operational implications, including any potential reliability and curtailment issues, (7) provide the power levels of the exchange, and (8) specify the desired dates and times for the exchange. The Commission may, of course, request additional information if needed to understand a proposed transaction.

The Commission orders:

The petition for declaratory order filed by Puget is hereby granted in part and denied in part as discussed in the body of this order.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.

³⁰ For instance, in its petition, Puget described a power transaction to address a constraint across the Cascades; however Puget did not provide the level of detail that was provided to the Commission in *El Paso* or that would otherwise allow the Commission to fully evaluate the transaction.