116 FERC ¶ 61,292
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Midwest Independent Transmission System Operator, Inc. — Docket No. ER06-1112-000

ORDER ACCEPTING FILING

(Issued September 26, 2006)

1. In this order, the Commission accepts the June 6, 2006 filing (June 6 Filing) of the Midwest Independent Transmission System Operator Inc. (Midwest ISO) describing the status of its efforts to develop a replacement for the interim resource adequacy plan currently approved as Module E of the Midwest ISO's Open Access Transmission and Energy Markets Tariff (TEMT). As discussed below, the Midwest ISO is directed to file a timetable for development and implementation of its phased approach, and with regard to a potential energy only market (EOM) identifying and describing any pre-conditions for such an EOM such as demand-side management programs and longer term energy contracts.

Background

2. On August 6, 2004, the Commission approved Module E of the TEMT "as a short-term transition mechanism to ensure that the day-to-day reliability needs" of the Midwest ISO are met.[1] The Commission directed the Midwest ISO to work within its stakeholder process to develop a more permanent resource adequacy plan.[2] On October 5, 2004, the

[1] *Midwest Independent Transmission System Operator, Inc.*, 108 FERC ¶ 61,163, at P 421, *order on reh'g*, 109 FERC ¶ 61,157 (2004), *order on reh'g*, 111 FERC ¶ 61,043, *reh'g denied*, 112 FERC ¶ 61,086 (2005).

[2] *Id.* P 397.

Midwest ISO made a compliance filing in which it committed to have a permanent resource adequacy plan by early June 2006.[3] This timeframe was accepted by the Commission.[4]

3. The Midwest ISO states that one of the key goals of an energy market is to send efficient, accurate and transparent price signals to market participants regarding the true value of energy. Such price signals can improve the quality of generation decisions and reduce the costs associated with those decisions. These price signals can also lead to better investment decisions with respect to transmission network upgrades, changes to distribution facilities, and demand side management initiatives. The Midwest ISO expects that these improvements to energy pricing will lead to improved reliability in the region.

4. In the June 6 Filing, the Midwest ISO describes the status of its efforts to develop a replacement for the interim resource adequacy plan. The Midwest ISO states that, during the past 18 months, it has undertaken significant work with stakeholders to establish a resource adequacy plan. Efforts described by the Midwest ISO include: (1) conducting meetings with the Midwest ISO Supply Adequacy Working Group; (2) working independently and in coordination with the Organization of MISO States' (OMS) Resource Adequacy Working Group; (3) drafting and disseminating to stakeholders technical papers on a number of informational topics; (4) discussing the interrelation of resource adequacy issues with the provision of ancillary services through the Ancillary Services Task Force; (5) discussing the impact of resource adequacy on control area issues through the Control Area Working Group; and (6) participating in Commission technical conferences and informal discussions with industry stakeholders on resource adequacy topics.[5] The Midwest ISO further states that these stakeholder discussions have focused on the development of a resource adequacy program that addresses: "(1) the unique characteristics of the Midwest ISO's Market Participants; (2) the Midwest ISO Region's needs; and (3) the views of applicable state regulators, including those of the [OMS]."[6]

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[3] Midwest Independent Transmission System Operator, Inc. Compliance Filing, Docket Nos. ER04-691-007 and EL04-104-006, at 31 (filed Oct. 5, 2004).

[4] *See Midwest Independent Transmission System Operator, Inc.*, 109 FERC ¶ 61,285, at P 335 (2004), *order on reh'g*, 111 FERC ¶ 61,043, at P 99 (2005).

[5] June 6 Filing at 3.

[6] *Id.* at 4.

5. The June 6 Filing does not make a concrete resource adequacy proposal; it does, however, outline a general two-phase approach for subsequent filings to implement a permanent resource adequacy plan.[7] The Midwest ISO states that the phased approach is "more efficient and productive" and "reasonable" given that there is no need to "act rashly to address resource adequacy, in part, because of the historic adequate reserves in the Midwest ISO Region."[8]

6. In Phase I, the Midwest ISO proposes an ancillary services market for short-term contingency reserves. It adds that operating reserve markets need to recognize locational differences of generation resources and load. The Midwest ISO also adds that capacity markets may still be required, at least on an interim basis, to maintain reliability in constrained load pockets. The Midwest ISO states that Phase I began with the April 3, 2006 informational filing in Docket No. ER04-691 on consolidation of control area/balancing authority operations; it commits to working with the balancing authorities on any required amendments to the Balancing Authority Agreement. The Midwest ISO anticipates filing detailed Phase I plans with Commission in the fall of 2006.

7. In Phase II, the Midwest ISO proposes to undertake a long-term integration of shortage pricing with the energy markets. The Midwest ISO says Phase II will include the following initiatives: (1) the implementation of more or different demand-side management (DSM) programs; (2) the development of longer term financial transmission rights (FTRs); (3) the facilitation of longer term energy contracts by market participants; (4) the coordination and resolution of seams issues with neighboring regional transmission organizations (RTOs) and non-market regions; and (5) the coordination of resource adequacy requirements with national and regional resource adequacy standards. Midwest ISO says that DSM programs will help to mitigate price spikes and will reduce the potential for the exercise of market power. It states that longer term FTRs (beyond the current one-year term) will effectively allow market participants to establish congestion hedges associated with the delivery of energy from generation resources. Longer term FTRs will allow longer term hedges, more risk management options, and thus reduce the risks market participants face. The Midwest ISO states that its proposal to facilitate longer term energy contracts (those for energy delivery more than one year in advance) is designed to provide an effective tool for market participants to manage risks and costs, as well as to provide financial institutions with more confidence regarding the economic viability of generation resources which could facilitate increased investment in

[7] In its answer the Midwest ISO establishes that it is not asking to implement an EOM market at this time. Midwest ISO Answer at 12.

[8] June 6 Filing at 5.

generation resources by reducing risks and costs. The other parts of Phase II involve coordination to address seams issues and to meet national and regional resource adequacy standards. The Midwest ISO anticipates making its Phase II filing with the Commission in 2007.

Notice of Filing

8. Notice of the Midwest ISO's June 6 Filing was published in the *Federal Register*, 71 Fed. Reg. 34,916 (2006), with interventions and protests due on or before June 27, 2006. At the request of the OMS, on June 20, 2006, as corrected on June 21, 2006, the Commission granted an extension of time to and including July 14, 2006.

9. Timely motions to intervene were filed by: American Municipal Power-Ohio, Inc.; BP Energy Company; the Coalition of Midwest Transmission Customers (CMTC); Exelon Corporation (Exelon); the Indiana Office of Utility Consumer Counselor; the Midwest Industrial Customers;[9] and the Midwest Stand-Alone Transmission Companies.[10] Timely motions to intervene and comments were filed by: Ameren Services Company, on behalf of the Ameren Companies (Ameren);[11] Constellation Energy Group Companies (Constellation);[12] Detroit Edison Company (Detroit Edison); Dominion Retail, Inc., Dominion Energy Kewaunee, Inc., Dominion Energy Marketing,

[9] For purposes of their filing, the Midwest Industrial Customers include: the American Forestry and Paper Association, Wisconsin Industrial Energy Group, Inc., Wisconsin Manufacturers Commerce, and Wisconsin Paper Council.

[10] For purposes of their filing, the Midwest Stand-Alone Transmission Companies include: American Transmission Company LLC, International Transmission Company d/b/a ITC*Transmission*, and Michigan Electric Transmission Company, LLC.

[11] For purposes of their filing, the Ameren Companies include: Central Illinois Light Company d/b/a AmerenCILCO, Central Illinois Public Service Company d/b/a AmerenCIPS, Illinois Power Company d/b/a AmerenIP, Union Electric Company d/b/a AmerenUE, Ameren Energy, Inc., and Ameren Energy Marketing Company.

[12] For purposes of their filing, the Constellation Energy Group Companies include: Constellation Energy Commodities Group, Inc., Constellation Generation Group, LLC, and Constellation NewEnergy, Inc.

Inc., and Troy Energy LLC (collectively, Dominion); Duke Energy;[13] Dynegy Power Marketing, Inc. (Dynegy); the Electricity Consumers Resource Council (ELCON); the Midwest TDUs;[14] Reliant Energy, Inc. (Reliant); Strategic Energy, L.L.C. (Strategic); Williams Power Company, Inc. (Williams); Wisconsin Electric Power Company (Wisconsin Electric); and Wisconsin Public Service Corporation, Upper Peninsula Power Company, WPS Energy Services Inc., and WPS Power Development, LLC (collectively, WPS).[15] The OMS filed a notice of intervention and comments. Untimely motions to intervene were filed by: Consumers Energy Company (Consumers); and PSEG Energy Resources & Trade LLC (PSEG). Untimely motions to intervene and comments were filed by: Alcoa Inc. and Alcoa Power Generating Inc. (collectively, Alcoa); and PPL EnergyPlus, LLC (PPL EnergyPlus).

10. On July 31, 2006, the Midwest ISO filed an answer to the comments. On August 14, 2006, Detroit Edison filed a reply to the Midwest ISO's answer.

Discussion

A. Procedural Matters

11. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2006), the notice of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding. We will grant the motions for late intervention of Consumers, PSEG, Alcoa, and PPL EnergyPlus, given their interests in this proceeding, the early stage of this proceeding, and the absence of any undue prejudice or delay.

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[13] For purposes of its filing, Duke Energy includes: Cincinnati Gas & Electric Company d/b/a Duke Energy Ohio, Inc., PSI Energy, Inc. d/b/a Duke Energy Indiana, Inc., Union Light, Heat and Power Company d/b/a Duke Energy Kentucky, Inc., and Duke Energy Americas, LLC.

[14] For purposes of their filing, the Midwest TDUs include: Great Lakes Utilities, Indiana Municipal Power Agency, Lincoln Electric System, Madison Gas & Electric Company, Midwest Municipal Transmission Group, Missouri Joint Municipal Electric Utility Commission, Missouri River Energy Services, Southern Minnesota Municipal Power Agency, and Wisconsin Public Power Inc.

[15] Although styled as out-of-time motions to intervene, the interventions of CMTC, Exelon, Strategic, and Williams are, in fact, timely.

12. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2006), prohibits an answer to a protest or an answer unless otherwise ordered by the decisional authority. We will accept the answers of the Midwest ISO and Detroit Edison because they have provided information that assisted us in our decision-making process.

B. Analysis

13. We will accept the Midwest ISO's June 6 Filing and its proposed phased approach to a permanent resource adequacy plan. However, given the importance of the Midwest ISO proceeding expeditiously and in light of the lack of substantive details in the June 6 Filing, the Commission directs the Midwest ISO to file a more detailed timetable for implementing milestones for each phase of its plan. The Midwest ISO should provide planned implementation dates for both Phases I and II when it makes its Phase I filing. We accept the Midwest ISO's commitment to file Phase I in Fall of 2006 and to file Phase II in 2007.

1. Midwest ISO's Plans for Resource Adequacy

a. Comments

14. Almost all commenters maintain that the Midwest ISO's proposal is far from fully developed and will require continuing efforts of stakeholders and the Midwest ISO to generate a sufficiently detailed plan to induce resource adequacy. Comments on the June 6 Filing focus on four general issues: (1) the adequacy of the June 6 Filing; (2) the stakeholder process; (3) the Midwest ISO's proposed phased approach; and (4) the concept of an EOM for the Midwest ISO region.

15. First, while almost all commenters note the lack of detail in the June 6 Filing, several protestors[16] assert that the June 6 Filing is so insufficient that it fails to satisfy the Midwest ISO's obligation to make such a filing. For example, WPS argues that the June 6 Filing provides insufficient detail regarding the implementation of the Midwest ISO's long-term resource adequacy requirements, has not been proven to be compatible with PJM's long-term resource adequacy model, and does not comply with the Commission's orders because it does not itself constitute a permanent long-term resource adequacy plan.

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[16] Such commenters include: Ameren, Detroit Edison, Dominion, Duke Energy, Dynegy, Reliant, and WPS.

16. Commenters' recommendations as to how the Commission should respond to the June 6 Filing vary. The Midwest TDUs ask the Commission to await the Midwest ISO's Phase I filing before passing judgment on the proposal. Others[17] argue that, because the June 6 Filing lacks any substantive details, the Commission should explicitly reject the filing and require the Midwest ISO to file a more complete filing. For example, Williams asks the Commission to "direct the [Midwest] ISO to file revised tariff sheets, appropriate draft Business Practice Manuals along with sufficient support for its market design proposal, and establish specific implementation dates."[18]

17. Some commenters[19] seek specific deadlines by which the Commission should require the Midwest ISO to file a resource adequacy plan, ranging from August 2006 to May 2007. For example, Duke Energy argues that the Commission should direct the Midwest ISO to develop and file a capacity market proposal within 120 days (or whatever period is deemed reasonable) or to convene a trial-type evidentiary hearing or, at a minimum, a technical conference, to determine whether an EOM or a capacity market can provide the needed resource adequacy. Reliant requests the Commission require, within 90 days, a report and order a subsequent technical conference on, among other things: a formal review and report on Module E; an analysis of the real-time prices needed to support resource adequacy in an EOM for a given reliability reserve level; a model describing how price caps and mitigation will change to allow those prices to occur; and the comments and opinion of the Independent Market Monitor (IMM) on each of these issues.

18. Second, while commenters such as Strategic applaud the Midwest ISO's stakeholder process thus far, several commenters[20] raise concerns about the stakeholder process. These commenters argue that the Midwest ISO has failed to provide timely information to stakeholders throughout the process and has failed to respond to the questions raised by stakeholders and to proposals that reflect stakeholder views. These commenters also argue that the June 6 Filing overstates the involvement in and contribution of stakeholders.

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[17] Such commenters include: Dynegy, Duke Energy, and Williams.

[18] Williams Comments at 4.

[19] Such commenters include: Ameren, Constellation, Dominion, Detroit Edison, Duke Energy, Reliant, and WPS.

[20] Such commenters include: Ameren, Williams, and WPS.

19. Third, while commenters debate the role of a phased approach in meeting long-run regional reliability requirements and want more details concerning the proposed phases, many commenters[21] support the proposed phased approach.

20. For example, the OMS filed comments generally supporting the Midwest ISO's two-phase approach. The OMS believes that the Midwest ISO should move forward with its Phase I proposal as to the functional consolidation of balancing authority functions, the transfer of other functions to the Midwest ISO, and creation of the related ancillary services market.[22] It encourages a cost-benefit study, prior to implementing the ancillary services market, "so that a 'look-back' evaluation can accurately compare the costs of historical ancillary services to the costs of the future [ancillary services market] proposal."[23] As to implementation of Phase I, the OMS "suggests that the Midwest ISO provide the pros and cons of various design alternatives under consideration" and seeks more information about DSM market operations under scarcity pricing conditions and about self-supply of ancillary services.[24]

21. The OMS also supports Phase II, but advises the Midwest ISO to research increasing demand response resources and study the impact of demand response on energy prices to ensure a healthy EOM. The OMS maintains that the Midwest ISO must coordinate demand response with the state regulatory commissions. The OMS states that "[t]he Midwest ISO should explain exactly how it envisions [Load Serving Entities (LSEs)] managing their load in the aggregate to respond to wholesale prices, or the extent and conditions under which retail demand response behind an LSE should or could participate directly in the wholesale market as market participants." The OMS also states that it "is unaware of any determination of how the relevant parties should and would

[21] Such commenters include: Alcoa, ELCON, the OMS, Strategic, and Wisconsin Electric.

[22] Dominion urges the Commission to require the Midwest ISO to take steps to reduce the number of control areas within its footprint. Dominion urges the Commission to require a compliance filing "demonstrating substantive progress towards the consolidation of balancing authorities/control areas no later than September 1, 2006." Dominion Comments at 14.

[23] OMS Comments at 7.

[24] *Id.* at 9.

treat current or new demand response resources in the determination of planning reserve margins."[25]

22. The OMS states that "[f]undamental to establishing an effective RTO environment for long-term firm transmission rights at the Midwest ISO will be the coordination of: 1) the allocation of existing financial transmission rights; 2) transmission expansion required for deliverability; and 3) the allocation of the costs resulting [from] transmission upgrades necessary to grant such rights."[26] The OMS states that enhanced transmission planning should be added as a sixth element to the Midwest ISO's Phase II long-term resource adequacy plan.

23. Strategic argues "[t]his plan is an appropriate solution for a regional [sic] that maintains a substantial supply surplus."[27] It supports the Midwest ISO's effort to integrate ancillary services with energy markets and would like to see the Midwest ISO specifically address scarcity pricing in Phase I. Strategic supports the Midwest ISO's Phase II proposal, but would like further detail. Strategic cautions the Midwest ISO that products be offered in a non-discriminatory fashion and not to bias the market to favor forward contracting against shorter-term deals.

24. Alcoa also supports the Midwest ISO's two-phase approach. Alcoa notes that three of the issues relegated to Phase II – DSM programs, development of longer term FTRs and the facilitation of longer term energy contracts by market participants – are of great importance, and requests that these three issues be broken out of Phase II and given special priority for implementation.

25. In contrast, Duke Energy argues that, while the market reforms proposed in Phase I and Phase II are "potentially good ideas to improve the markets,"[28] they do not address resource adequacy.

26. WPS argues that Phase I should be accomplished in parallel and outside of the Midwest ISO's proposed resource adequacy plan because it does nothing to promote long-term resource adequacy. Moreover, WPS argues that it may be premature to adopt an approach to co-optimize the operating reserves market into the energy market without

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[25] *Id.* at 16-17.

[26] *Id.* at 20.

[27] Strategic Comments at 3.

[28] Duke Energy Comments at 9.

having first established locational operating reserve requirements. WPS also notes that the development of longer term FTRs, identified as part of Phase II, is subject to the Commission's rulemaking in Docket Nos. RM06-8-000 and AD05-7-000. Further, WPS asserts that the Midwest ISO's Phase II emphasizes reliance on longer term energy contracts but the Midwest ISO fails to explain how it will provide incentives for market participants to engage in longer term energy contracts, other than the threat of high scarcity pricing, nor any specific terms and conditions of such contracts. WPS also asserts that the Midwest ISO already has an obligation to comply with Electric Reliability Organization and Regional Reliability Organization (RRO) requirements, regardless of its inclusion as a Phase II initiative.

27. Similarly, Reliant argues that, although the Phase I development of an ancillary services market may be important, and remains a top priority, it is not designed to meet resource adequacy requirements. Reliant also maintains that the June 6 Filing fails to provide any specificity of how the Phase II elements constitute a resource adequacy plan, and fails to address critical real-time pricing changes needed in the Midwest ISO Region to support certain of these elements.

28. Fourth, commenters are split as to whether an EOM is the appropriate approach for a permanent resource adequacy plan in the Midwest ISO Region. Several commenters[29] argue that the EOM model is fundamentally flawed.

29. For example, Duke Energy argues, *inter alia*, that: (1) EOM markets are highly volatile, making severe price volatility the norm and boom-bust cycles much more likely; (2) EOM markets lack a resource adequacy requirement *per se*, relying on the market to decide how much capacity is necessary to ensure that reliability standards are met; (3) the EOM model encourages competitive LSEs to opportunistically exit the energy market when scarcity arises, shifting reliability costs to other parties such as providers of last resort (POLRs); (4) the EOM model directly conflicts with the PJM market design and will create several seams, including pricing at the time of scarcity and dependence on PJM for reliability purposes; (5) the EOM model will not resolve load pocket issues and will fail to send locational signals to build where most needed in the Midwest ISO region; and (6) EOMs have failed in the past, citing the failure of the California EOM in 2000 and 2001. Duke Energy also argues that investors may expect high real time electricity prices in the EOM to be refunded after the fact, and will thus be unwilling to invest in new generation. In his affidavit for Duke Energy, Robert Stoddard states that the Midwest ISO's planning studies indicate that, in order to maintain reserve margins consistent with traditional reliability standards, additional capacity (beyond that currently

[29] Such commenters include: Ameren, Detroit Edison, Duke Energy, and Reliant.

under construction) will be needed within the next three years. Given the typical development timeframes, Mr. Stoddard believes there is little time for the Midwest ISO to develop a robust energy and reserve market design. Thus, Mr. Stoddard believes the Midwest ISO should implement a well-designed capacity market as a backstop.

30. Similarly, Ameren states that "while, from an academic viewpoint, the EOM approach could potentially serve as a basis for [a resource adequacy] plan, the EOM approach is unlikely to work in reality."[30] Ameren also raises concerns that an EOM is unlikely to be operational any time in the next few years. Ameren argues that, in contrast, "historical capacity mechanisms are well known and proven methods that can be utilized today to create a capacity market without introducing risks that reduce reliability and heighten the likelihood of involuntary economic-based interruptions" in addition to "more likely to be politically and socially acceptable."[31]

31. Detroit Edison argues that EOMs are untested and "imprudent" given the "volatility and uncertainty inherent in energy markets."[32] Detroit Edison also states that the Commission should require the Midwest ISO's resource adequacy plan to include long-term planning reserve criteria for all LSEs within the Midwest ISO region, consistent with the long-term resource adequacy plans advanced in PJM and the New York Independent System Operator, Inc. regions.

32. Several commenters[33] also argue that the EOM may be unworkable for the Midwest ISO region in particular. For example, WPS maintains that the Midwest ISO has failed to demonstrate that the EOM will be compatible with PJM's RPM for resource adequacy and the EOM design could result in seams issues. WPS states that the Midwest ISO's failure to establish a region-wide LSE-specific mandatory capacity requirement may lead to improper cross-subsidization and the erosion of reserves.

33. Dominion expresses concern with the Midwest ISO's proposal to forego the development of a locational installed capacity market. Dominion argues that, to the extent the Midwest ISO anticipates abandoning an installed capacity market, it must make significant changes to its existing market platform to ensure that energy and ancillary service prices reach the levels necessary to support investment in new and

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[30] Ameren Comments at 8.

[31] *Id.* at 9.

[32] Detroit Edison Comments at 7.

[33] Such commenters include: Dominion, Duke Energy, Reliant, and WPS.

existing generation resources, particularly generators on the margin. Dominion urges the Commission to direct the Midwest ISO to implement true scarcity prices through Phase II no later than September 2006.

34. Reliant argues that the Midwest ISO should answer various questions about the feasibility of EOM markets in the Midwest ISO region, including: (1) is reliability a public good; (2) is the potential for demand response in real-time adequate; (3) will politicians, legislators and regulators allow the real-time electricity prices needed to support an EOM; and (4) will LSEs believe regulators will allow prices high enough to support an EOM.

35. By comparison, several commenters[34] filed comments explicitly supporting an EOM approach to resource adequacy for the Midwest region. For example, the OMS states that, based on its review of capacity constructs elsewhere, it would not advise commitment of the Midwest ISO's resources towards developing capacity market plans for the Midwest. The OMS notes that it is seeking additional information from Midwest ISO staff regarding "'subregional geographic' reserve margins based on load and resource data," and "how the Midwest ISO is assisting Reliability First [LSEs] to determine planning reserve requirements for the new [Planned Reserve Sharing Groups]."[35] The OMS also notes that the Midwest ISO expects an overall reserve level of 15 percent through the summer of 2009 and as such, reliability is not a concern in the Midwest ISO region at this time.

36. PPL EnergyPlus argues that an EOM will provide incentive for LSEs to act responsibly to protect themselves and their end-use customers from price volatility. It maintains that installed capacity markets create secondary market design problems including the disincentive to short-run operational reliability. It argues that additional concerns could arise because of an improperly constructed demand curve or excessive market mitigation. PPL EnergyPlus further argues that the EOM is not inconsistent with the long-term reliability plans in PJM. PPL EnergyPlus asserts that, notwithstanding the reliability pricing model currently subject to settlement discussions in the PJM region, the "end state" for both PJM and the Midwest ISO is "one in which energy markets are used to address resource adequacy issues."[36]

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[34] Such commenters include: Alcoa, ELCON, the OMS, PPL EnergyPlus, Strategic, and Wisconsin Electric.

[35] OMS Comments at 14.

[36] PPL EnergyPlus Comments at 8.

37. Wisconsin Electric claims that the best way to ensure that sufficient capacity is built is to rely on the resource adequacy and reliability standards developed by the NERC RROs, obviating the need for a Midwest ISO-wide resource adequacy requirement.

38. ELCON conditionally supports the EOM approach, arguing that EOMs appropriately rely on market signals rather than excessive regulation.[37] ELCON claims that locational installed capacity markets "distort price signals and require further regulatory intervention … to ensure short-term reliability and long-term investment."[38] ELCON argues that the Midwest ISO must meet certain preconditions, to ensure the successful implementation of the EOM and prevent the risk of price spikes to end-users. These include a showing that: (1) suppliers are sufficiently risk averse to exposure to spot energy prices that they will negotiate bilateral contracts without the level of risk premiums typically required in contracts offered in the Northeast ISO/RTO markets; (2) prices are set by supply and demand, constrained by competition among generators, price responsive load, and price caps sets at the average "value of lost load"; (3) the wholesale market is predominantly a forward market with only limited purchases in the spot market; (4) the OMS supports the EOM design with conforming actions in the retail markets (*e.g.*, enable demand response, encourage LSEs to forward contract where and when forward markets are sufficiently liquid and robust, and establish reserve levels); and (5) there is transmission adequacy such that local market power of generators is eliminated or mitigated by the IMM.[39]

b. <u>Answer</u>

39. The Midwest ISO states that the June 6 Filing should not be rejected for lacking in detail, arguing that "the generality of the … filing simply reflects the complexity of the subject matter, the need for careful development of a more market-based approach, and the ongoing consultations with stakeholders that have a wide spectrum of positions on the relevant issues."[40] The Midwest ISO states that, given its concern about "prejudging" the eventual shape of the resource adequacy plan, "the restraint in detail is not a mark of deficiency, but rather a demonstration of efficiency in developing a program that requires

[37] Alcoa generally supports ELCON's comments.

[38] ELCON Comments at 3.

[39] *Id.* at 5-6.

[40] Midwest ISO Answer at 10.

the further consideration and incorporation of various stakeholders and regulatory inputs."[41]

40. The Midwest ISO further argues that the June 6 Filing is not deficient due to the lack of specific deadlines. The Midwest ISO states that "establishing … artificial deadlines is not conducive to productive resolution of differences of opinion regarding complex resource adequacy issues."[42] The Midwest ISO restates its commitment to make supplemental filings as set forth in the June 6 Filing. The Midwest ISO also notes that "[u]nder these circumstances, it would be counterproductive to hold any trial-type hearings or technical conferences, as such proceedings could merely divert the valuable time and resources of the parties, thereby causing further delay."[43]

41. The Midwest ISO also explicitly endorses the comments filed by the OMS, and states its intention to "follow [the OMS's] recommendation that reliability objectives be pursued in a linear fashion: begin with shorter-term reliability measures (co-optimization of operating reserves and development of effective ancillary services markets) and then proceed, if necessary, to develop longer-term reliability tools, such as capacity markets."[44] The Midwest ISO notes that state commissions "continue to be responsible for reviewing the prudence of utility decisions in their individual states, including investment in generation facilities to meet any mandated long-term planning reserve requirement" and therefore, "the views of the OMS should be carefully considered in determining *if* it is necessary to implement longer-term planning reserve requirements and also *when* such longer-term requirements should be mandated."[45]

42. The Midwest ISO acknowledges that more work needs to be done to address perceived weaknesses in the EOM approach and states that it is not proposing to implement an EOM at this time for this reason. The Midwest ISO states that an EOM proposal is still being studied by the Midwest ISO and "there is neither prudent nor pressing reason to reject EOM from the very outset."[46]

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[41] *Id.* at 11.

[42] *Id.* at 13.

[43] *Id.* at 14.

[44] *Id.* at 6 (citing OMS Comments at 3).

[45] *Id.* at 5-6 (emphasis in the original).

[46] *Id.* at 12.

43. The Midwest ISO asserts, however, that, "it is premature to preclude adoption of EOM ideas, particularly because the short-term, phased-in approach of co-optimization of Operating Reserves has not yet been implemented and evaluated."[47] The Midwest ISO also submits that it is not reasonable to require it to simultaneously implement the EOM and installed capacity approaches.

c. Commission Determination

i. Adequacy of the June 6 Filing

44. We recognize that several of the commenters view the June 6 Filing as so lacking in detail that they believe the Commission should find the filing deficient. Nevertheless, we believe that with the guidance provided here, and with the identification of milestones and deadlines which we require here, the June 6 Filing is a basis to build upon. It is our expectation that these milestones and deadlines, once established in the Phase I filing later this fall, will be met and that each will be met in sufficient detail and with sufficient input from the stakeholder process to adequately address many of the concerns raised in this proceeding.

45. Merely finding the June 6 Filing deficient would do little service to what has been a multi-year stakeholder effort. Therefore, just as we did during the early development of the TEMT, we will provide guidance to the Midwest ISO and the stakeholders so that they may more fully develop the proposal.[48] However, unlike that proceeding, we will require that the milestones, deadlines and an implementation plan be filed as part of the Phase I filing.

ii. Stakeholder Process

46. We believe that a stakeholder process is important and we are encouraged that the Midwest ISO is working with its stakeholders to develop a permanent resource adequacy plan. We are pleased with the progress to date and expect it will continue and gain even

[47] *Id.*

[48] *See Midwest Independent Transmission System Operator, Inc.*, 105 FERC ¶ 61,145, at P 22-23, *order on reh'g*, 105 FERC ¶ 61,272 (2003).

greater momentum going forward.[49] We are especially pleased with the leadership role the OMS has undertaken in this stakeholder process and recognize that resource adequacy issues are of critical importance to the states.

47. We understand that because of the wide variety of stakeholder positions regarding resource adequacy issues, and the complexity of the issues, it has been difficult for the Midwest ISO to make substantial progress. We are also mindful that, given the diverse groups of stakeholders in the region, unanimity on all issues surrounding resource adequacy is likely not achievable. Therefore, we recognize that Midwest ISO as an independent organization will need to use its discretion in those areas lacking a consensus.

48. At the same time, we believe that developing and implementing a workable plan to promote resource adequacy in the Midwest ISO region is important. While resource adequacy does not appear to be an immediate problem in the Midwest ISO region, it is important to adopt plans that result in resource adequacy over the intermediate term and long term.

iii. Phased Approach

49. We will accept Midwest ISO's phased approach to developing a workable permanent resource adequacy plan for the region. We are not persuaded by the commenters favoring rejection of a phased approach, but rather, like the OMS and others, believe that given the current reserve levels in the region for the next few years, a phased approach represents a reasonable means of achieving long-term resource adequacy in the region.

50. While we are accepting this approach, our acceptance is conditioned upon specific milestones, deadlines and an implementation plan being developed to further refine the Midwest ISO's Phase II filing and to address the numerous concerns and issues from commenters as discussed more fully below. This plan along with identified milestones and deadlines shall be filed as part of Midwest ISO's Phase I filing later this fall. We add that we expect to remain informed and parties to remain engaged throughout the process.

[49] We note that some commenters have raised concern over the timeliness and responsiveness of the Midwest ISO during portion of the stakeholder process. While we are generally satisfied with the process, we remind the Midwest ISO that timely and responsive actions should enable a more fully developed proposal.

51. As part of this phased approach, the Midwest ISO shall coordinate with the OMS and other stakeholders to consider provisions for participation of demand resources in ancillary services markets in its Phase I filing. Based on the stakeholder process, Midwest ISO is directed to include in its section 205 filing for Phase I either: (a) provisions, for implementation in summer 2007, for the commitment and dispatch of interruptible demand, behind the meter generation and other demand resources that are capable of providing operating reserves and short-term contingency reserves; or (b) an explanation and rationale for not including such provisions in its tariff and identifying specific barriers, causes or issues that prevented the filing. At that time, the Commission will consider whether it would be useful to convene a technical conference to consider the filing.

iv. EOM

52. Various commenters support the EOM construct while reserving final judgment until the specifics of the EOM are filed. Others request rejection of the EOM as fundamentally flawed, unworkable or conflicting with neighboring RTO resource adequacy plans. We agree with the Midwest ISO's assertion that "it is premature to preclude adoption of EOM ideas." Indeed, we believe that an EOM could be a just and reasonable approach to addressing resource adequacy needs for the region in the future. Most of the details of an EOM have yet to be developed, and once a detailed proposal is filed with us parties will, of course, be free to raise specific concerns.

53. We reject calls from commenters that we require the Midwest ISO to file a capacity market proposal in lieu of an EOM approach to resource adequacy. We have consistently allowed for regional differences in the RTO context and have never mandated a one-size-fits-all approach for dealing with resource adequacy.[50]

54. While we support the concept of an EOM approach, we agree with virtually all the commenters that concerns of the market participants about an EOM must be addressed by the Midwest ISO and many more details must be determined before an EOM proposal can be approved. While below we provide guidance as to areas we believe need to be

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[50] *See generally Long-Term Firm Transmission Rights in Organized Electricity Markets*, 71 Fed. Reg. 43,564 (2006), FERC Stats. & Regs. ¶ 31,226, at P 100 (2006) (noting the appropriateness of recognizing regional differences in market design); *Southwest Power Pool, Inc.*, 110 FERC ¶ 61,031, at P 22-23 (2005) (finding that differences between RTO regions may be warranted given the different circumstances of the markets); *Midwest Independent Transmission System Operator, Inc.*, 102 FERC ¶ 61,196, at P 43 (2003) (same).

more fully addressed, we do not mean this list to be all-inclusive and we expect that the Midwest ISO will continue to have a robust stakeholder process to fully vet issues surrounding an EOM approach prior to filing Phase II in 2007.

55. For instance, we agree with many of the commenters that for a workable EOM, robust DSM programs are of vital importance. We would expect that before deployment of any DSM program there would be an analysis of whether the infrastructure is adequate to support demand response in real-time. Likewise we agree with the OMS that DSM programs need to be coordinated with demand response programs at the state level. We also agree that Midwest ISO should fully explain how LSEs managing their load in the aggregate could respond to wholesale prices, or the extent and conditions under which retail demand response behind an LSE should or could participate directly in the wholesale market. Earlier in this order, we directed the Midwest ISO to work with the OMS and other stakeholders on participation of demand resources in the markets and market design modifications. Such provisions would provide a platform to integrate into Midwest ISO market design the resource adequacy standards and programs required by the states and other reliability authorities. In particular, the Midwest ISO shall consider with the OMS and other stakeholders procedures for commitment and dispatch of interruptible demand (consistent with state/local resource adequacy requirements and programs), behind the meter generation and other demand resources that are capable of participating in the proposed EOM.

56. Additionally, commenters raise significant issues associated with the development of longer term FTRs, the facilitation of longer term energy contracts by market participants, and the resolution of seams issues with neighboring RTOs; these must be addressed by the Midwest ISO in Phase II. For instance, OMS believes that necessary steps in developing longer term FTRs are the coordination of the allocation of existing rights, effective transmission expansion and the resulting cost allocation from the expansion. ELCON stresses the need to focus on various steps to promote longer term energy contracts so as to mitigate short term price volatility to customers. Duke Energy's concerns that competitive LSEs will opportunistically exit the energy market when scarcity arises, shifting reliability costs to other parties, must also be addressed.

v. **Conclusion**

57. In sum, it is reasonable for the Midwest ISO to proceed with a phased approach. However, as discussed above, we will require the Midwest ISO to file as part of the Phase I filing this fall a more detailed timetable for implementing Phase II. We expect that this filing will include milestones and deadlines for both phases as well as detailed implementation plans, including timelines to fully respond to EOM concerns in Phase II. Moreover, we expect the Midwest ISO to meet these milestones and deadlines once

established. This is critical for the successful and timely development of a permanent resource adequacy plan for the region.

2. Proposed Changes to the Existing Module E

a. Comments

58. Until a permanent resource adequacy proposal is proposed by the Midwest ISO and approved by the Commission, the interim procedures currently set forth in Module E remain in place. Interim resource adequacy requirements are based on the current reliability mechanisms of the states and the RROs within the Midwest ISO; market participants must comply with the appropriate state or regional reliability requirements where their load is served. If load is located in multiple regions within the Midwest ISO, it is pro-rated according to each region's reliability requirements. There is no compliance obligation for the *pro rata* share of load that is outside the Midwest ISO. The Midwest ISO determines what standards are in place in each state or region and then notifies market participants of their applicable obligation where the load is served. In the event of a conflict between state and RRO reliability requirements, market participants must comply with the state's requirements and then that portion of the RRO requirements that is feasible. If the Midwest ISO does not find any reliability standards in place where load is being served within its region, it applies a default annual reserve margin of 12 percent.[51]

59. Given the delay in the development of a permanent resource adequacy plan, some commenters call for immediate changes to the Midwest ISO's pre-existing Module E mechanism. For one, Duke Energy calls for a system-wide minimum planning reserve requirement of 12 percent. It argues that while states, state commissions, or legislatures could continue to mandate a higher reserve margin requirement, a minimum would help ensure a level playing field for planning purposes and help minimize the "free rider" problem. Similarly, Detroit Edison argues that the interim resource adequacy plan set forth as Module E discriminates among LSEs in the Midwest ISO region, and urges the Commission to impose on all LSEs not currently subject to a planning reserve requirement a minimum planning reserve requirement of 12 percent pending finalization and approval of a permanent resource adequacy plan.

60. Reliant argues that the Midwest ISO should explain how Module E is currently being implemented. Reliant maintains that "[i]ssues worthy of discussion remain"

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[51] *See Midwest Independent Transmission System Operator, Inc., supra* note 1, at P 388-89.

including, for example, that Module E allows some entities to satisfy their reliability requirements with liquidated damages contracts and other financial arrangements, rather than physical capacity.[52]

b. Answers

61. In response to Detroit Edison and Duke Energy, the Midwest ISO argues that there is no need to impose a 12 percent planning reserve minimum requirement pending the establishment of a permanent resource adequacy plan. The Midwest ISO argues that, to the extent Detroit Edison proposes a default margin different from Module E's current default provision, the request is a collateral attack on the Module E requirements already approved by the Commission. In response to Duke Energy's concerns, the Midwest ISO argues that operating reserve obligations are more effective at ensuring reliability than planning reserve obligations. The Midwest ISO also states that Duke Energy's request for a minimum 12 percent planning reserve requirement for all market participants is a collateral attack on existing default provisions. The Midwest ISO maintains that, without adequate prior consultation with stakeholders, the imposition of a 12 percent requirement "would unfairly disrupt the energy marketplace, detrimentally impact commercial activity and would unreasonably cause confusion among Market Participants."[53] The Midwest ISO also states that this is largely a moot point because the RROs in the Midwest ISO region will require compliance with region-wide reliability standards. The Midwest ISO further maintains that protestors have failed to provide any additional evidence that the Midwest ISO's existing standards are insufficient.

62. In response to the Midwest ISO, Detroit Edison argues that the Midwest ISO misunderstands its protest on this issue. Detroit Edison argues that its proposed 12 percent planning reserve requirement is not "duplicative" to the 12 percent "default" reserve margin set forth in Module E because the 12 percent "default" reserve margin is applied only to those entities not otherwise subject to any reserve requirement (planning or operating). Detroit Edison argues that, accordingly, entities located within certain Midwest ISO regions are permitted to rely on *operating* reserve standards to meet Module E reserve requirements while franchised utilities in the same region must abide by a higher *planning* reserve requirement. Detroit Edison maintains that "[i]t is axiomatic that operating reserves and planning reserves cannot be used interchangeably, as each serves a distinct purpose from a resource adequacy perspective."[54] Detroit

[52] Reliant Comments at 7.

[53] Midwest ISO Answer at 9.

[54] Detroit Edison Answer at 4, n.4.

Edison also argues that the Midwest ISO's characterization of Detroit Edison's protest as a collateral attack is wrong because Module E was only a interim solution that should have been replaced by June 1, 2006. Further, Detroit Edison argues that the Midwest ISO has the responsibility for ensuring long-term reliability across its footprint, and cannot shift that responsibility to RROs.

c. Commission Determination

63. The Commission agrees with the Midwest ISO that commenters' requested changes to the pre-existing Module E amount to a collateral attack on prior Commission orders accepting Module E.[55] We have previously declined to adopt Detroit Edison's request to modify Module E to require an annual reserve margin of 12 percent to apply to all LSEs.[56] The Commission continues to believe that "for the interim period when Module E is in effect, a 12 percent reserve margin only applicable where no pre-existing standard is in effect is a reasonable requirement, because present reserve margins are effective and will be preserved."[57] As also indicated in that previous Commission order, however, "we are not prejudging the merits of a minimum reserve requirement as part of the permanent resource adequacy plan and we encourage Detroit Edison [and other parties] to raise their views through the resource adequacy stakeholder process underway to develop the permanent plan."[58]

64. Although the interim procedures set forth in Module E have remained in place longer than the Midwest ISO, stakeholders, and certainly the Commission contemplated, we agree with the Midwest ISO that changing Module E at this time, particularly absent prior stakeholder input, may cause confusion, and possibly commercial disruption, in the Midwest ISO market. Accordingly, we decline to require additional changes to Module E at this juncture.

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[55] In addition, we have long required that a complaint not be included as part of another pleading such as a protest. *See, e.g., Louisiana Power & Light Company*, 50 FERC ¶ 61,040, at 61,062-63 (1990); *Entergy Services, Inc.*, 52 FERC ¶ 61,317, at 62,270 (1990); *Yankee Atomic Electric Company*, 60 FERC ¶ 61,316, at 62,096-97 (1992).

[56] *Midwest Independent Transmission System Operator, Inc., supra* note 4, at P 317.

[57] *Id.*

[58] *Id.*

The Commission orders:

The Midwest ISO's June 6 Filing is hereby accepted, as described in the body of this order.

By the Commission. Commissioner Moeller not participating.

(S E A L)

Magalie R. Salas,
Secretary.