ORAL ARGUMENT IS SCHEDULED FOR OCTOBER 7, 2004

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IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 03-1238, *et al.*
(consolidated)

MIDWEST INDEPENDENT TRANSMISSION SYSTEM OPERATOR, INC., *et al.*,
PETITIONERS,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.

ON PETITION FOR REVIEW OF ORDERS OF THE FEDERAL ENERGY REGULATORY COMMISSION

BRIEF OF RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

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JUNE 7, 2004

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CIRCUIT RULE 28(a)(1) CERTIFICATE

A. Parties and Amici

The parties before this Court are identified in the brief of Petitioners.

B. Rulings Under Review

1. *Midwest Independent Transmission System Operator, Inc.*, 103 FERC ¶ 61,048 (2003); and

2. *Midwest Independent Transmission System Operator, Inc.*, 104 FERC ¶ 61,060 (2003).

C. Related Cases

This case has not previously been before this Court or any other court. Counsel is not aware of any other related cases pending before this or any other court.

_____
Lona T. Perry
Attorney

June 7, 2004

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GLOSSARY

Annual Charges Rehearing	*Revision of Annual Charges to Public Utilities (California Independent System Operator, et al.)*, 101 FERC ¶ 61,043, *reh'g dismissed*, 101 FERC ¶ 61,326 (2002)
Conference Report	H.R. Conf. Rep. No. 99-1012 (1986), *reprinted in* 1986 U.S.C.C.A.N. 3868
FERC	Federal Energy Regulatory Commission
FPA	Federal Power Act
Initial Order	*Midwest Independent Transmission System Operator, Inc.*, 103 FERC ¶ 61,048 (2003)
OBRA	Section 3401 of the Omnibus Budget Reconciliation Act of 1986, 42 U.S.C. § 7178
OMOI	Office of Market Oversight and Investigations
Order No. 472	*Annual Charges Under the Omnibus Budget Reconciliation Act of 1986*, Order No. 472, 52 Fed. Reg. 21263 and 24153 (June 5 and 29, 1987), FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,746 (1987), *clarified*, Order No. 472-A, 52 Fed. Reg. 23650 (June 24, 1987), FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,750, *order on reh'g*, Order No. 472-B, 52 Fed. Reg. 36013 (Sept. 25, 1987), FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,767 (1987), *order on reh'g*, Order No. 472-C, 53 Fed. Reg. 1728 (Jan. 22, 1988), 42 FERC ¶ 61,013 (1988)
Order No. 641	*Revision of Annual Charges Assessed to Public Utilities*, Order No. 641, 65 Fed. Reg. 65,757, FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,109 (2000)
Order No. 641-A	*Revision of Annual Charges Assessed to Public Utilities*, Order No. 641-A, 66 Fed. Reg. 15793, 94 FERC ¶ 61,290 (2001)
Midwest ISO	Midwest Independent Transmission System Operator

New York ISO	New York Independent Transmission System Operator
NRC	Nuclear Regulatory Commission
PJM	PJM Interconnection, Inc.
Rehearing	*Midwest Independent Transmission System Operator, Inc.*, 104 FERC ¶ 61,060 (2003)
RTO	regional transmission organization
SMD NOPR	*Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design, Notice of Proposed Rulemaking*, 67 Fed. Reg. 55,452 (2002), FERC Stats. & Regs. ¶ 32,563 (2002)

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RESPONDENT.

ON PETITION FOR REVIEW OF ORDERS OF THE FEDERAL ENERGY REGULATORY COMMISSION

BRIEF OF RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

STATEMENT OF THE ISSUE

Whether the Commission reasonably denied a petition for rulemaking that reiterated policy concerns that had been raised and rejected in the rulemaking proceeding promulgating the current rule, where no showing was made of a substantial change in circumstances to warrant a new rulemaking.

STATUTORY AND REGULATORY PROVISIONS

The pertinent statutes and regulations are contained in the Addendum to this brief.

STATEMENT OF JURISDICTION

The Commission agrees with petitioners that this Court possesses jurisdiction over this appeal, and that *Five Flags Pipe Line Co. v. Department of Transportation*, 854 F.2d 1438 (D.C. Cir. 1988) does not bar this Court's jurisdiction. *See* Petitioners' Brief ("Br.") at 2-3 n.3. In addition to petitioners' arguments, this Court has jurisdiction over these petitions because the orders challenged address not only the methodology for assessing annual charges under § 3401 of the Omnibus Budget Reconciliation Act of 1986 ("OBRA"), 42 U.S.C. 7178, but also the propriety of allowing recovery of those annual charges in jurisdictional rates under the Federal Power Act ("FPA"). The latter finding is subject to review exclusively in the courts of appeals. FPA § 313(b), 16 U.S.C. § 825*l*. *See Midwest Independent Transmission System Operator, Inc.*, 103 FERC ¶ 61,048 at ¶ 15 and n.25, JA 240 (2003) ("Initial Order"), *on reh'g*, 104 FERC ¶ 61,060 at ¶ 19 and n. 35, JA 276 (2003) ("Rehearing Order").[1] When one statutory basis for an agency decision resting on more than one basis provides for exclusive jurisdiction in the courts of appeals, the entire decision is reviewable exclusively in the court of appeals. *Communities Against Runway Expansion, Inc. v. FAA*, 355 F.3d 678, 684 (D.C. Cir. 2004) (court of appeals has jurisdiction over review of FAA orders resting in part on section of Act providing for exclusive review in court of appeals); *Shell Oil v. FERC*, 47

[1] Both findings are challenged on appeal; the latter finding is challenged on the ground that it results in annual charges being indirectly assessed against non-public regional transmission organization ("RTO") or independent system operator ("ISO") member utilities, who are not otherwise subject to annual charges. *See* Pet. Br. at 28-29.

F.3d 1186, 1195 (D.C. Cir. 1995) (court of appeals has jurisdiction over two related petitions where one petition is subject to exclusive review in court of appeals). Any ambiguity, moreover, is properly resolved in favor of review in the court of appeals as the factfinding capacity of the district court is unnecessary to review the agency's decisionmaking here. *See Communities Against Runway Expansion*, 355 F.3d at 684 (citing *General Electric Uranium Management Corp. v. DOE*, 764 F.2d 896, 903 (D.C. Cir. 1985)). *See also Florida Power & Light Co. v. Lorion*, 470 U.S. 729, 744 (1985).

STATEMENT OF THE CASE

I. Nature of the Case, Course of Proceedings, and Disposition Below

As required by OBRA, the Commission's regulations provide for the payment of annual charges by public utilities, intended to recover the Commission's estimated electric regulatory program costs for each fiscal year. A 2000 FERC rulemaking determined that, in light of the Commission's increasing regulatory emphasis on assuring open access to transmission, it was no longer appropriate to allocate annual charge assessments based on both transmission and sales transactions, and that henceforth annual charges would be assessed to public utilities based on their transmission volumes. *Revision of Annual Charges Assessed to Public Utilities*, Order No. 641, 65 Fed. Reg. 65,757, FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,109 (2000), *on reh'g*, Order No. 641-A, 66 Fed. Reg. 15793, 94 FERC ¶ 61,290 (2001). No party appealed Order No. 641.

In 2002, Midwest Independent Transmission System Operator, Inc. ("Midwest ISO"), New York Independent System Operator, Inc. ("NYISO") and PJM

Interconnection, L.L.C. ("PJM") filed a petition asking the Commission to commence a rulemaking to forego the Order No. 641 annual charges methodology, and revert to its prior method of assessing annual charges on both transmission and sales. In the challenged orders, the petition was denied because the purported "policy" concerns it raised with regard to Order No. 641 had already been raised and rejected in the Order No. 641 rulemaking proceeding -- in which all petitioners participated -- and petitioners failed to show any substantial change that would justify their request for a new rulemaking. *Midwest Independent Transmission System Operator, Inc.*, 103 FERC ¶ 61,048 (2003), *on reh'g*, 104 FERC ¶ 61,060 (2003).

II. Statement of Facts

A. Electric Annual Charges Under Order No. 472

OBRA requires the Commission to "assess and collect fees and annual charges in any fiscal year in amounts equal to all of the costs incurred . . . in that fiscal year." 42 U.S.C. § 7178. The annual charges must be computed based on methods which the Commission determines to be "fair and equitable." *Id.*

To implement OBRA, in Order No. 472[2] the Commission formulated an annual charge billing procedure that was intended to recover FERC's estimated electric

[2] *Annual Charges Under the Omnibus Budget Reconciliation Act of 1986*, Order No. 472, 52 Fed. Reg. 21263 and 24153 (June 5 and 29, 1987), FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,746 (1987), *clarified*, Order No. 472-A, 52 Fed. Reg. 23650 (June 24, 1987), FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,750, *order on reh'g*, Order No. 472-B, 52 Fed. Reg. 36013 (Sept. 25, 1987), FERC Stats. & Regs., Regulations Preambles 1986-1990 ¶ 30,767 (1987), *order on reh'g*, Order No. 472-C, 53 Fed. Reg. 1728 (Jan. 22, 1988), 42 FERC ¶ 61,013 (1988).

regulatory program costs for that fiscal year. Under that procedure, annual charges were assessed to individual public utilities based on a ratio of each utility's sales and transmission volumes to total volumes of both sales and transmission.

B. Events Following Order No. 472

Following Order No. 472, the electric industry underwent dramatic changes. *See* Order No. 641 at 31,848, JA 124. While, historically, vertically integrated utilities sold generation, transmission and distribution services as part of a "bundled" package, significant technological advances and changes in the law increased entry into the wholesale power generation markets, which, in turn, spawned a need for greater access to transmission services. However, public utilities were using their monopoly control over interstate transmission facilities to gain advantage over potential competitors. To remedy this situation, the Commission issued Order No. 888,[3] which fundamentally altered the wholesale electric power market, requiring all jurisdictional public utilities (1) to file tariffs ensuring non-discriminatory open access transmission; and (2) functionally to unbundle wholesale power services. Order No. 888 at 31,635-36, 31,654-55.

[3] *Promoting Wholesale Competition Through Open Access Nondiscriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, FERC Stats. & Regs. 31,036, 61 Fed. Reg. 21,540 (1996), *clarified*, 76 FERC 61,009 and 76 FERC 61,347 (1996), *on reh'g*, Order No. 888-A, FERC Stats. & Regs. 31,048, 62 Fed. Reg. 12,274, *clarified*, 79 FERC 61,182 (1997), *on reh'g*, Order No. 888-B, 81 FERC 61,248, 62 Fed. Reg. 64,688 (1997), *on reh'g*, Order No. 888-C, 82 FERC 61,046 (1998), *aff'd sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *aff'd, New York et al. v. Federal Energy Regulatory Commission*, 535 U.S. 1 (2002).

Following Order No. 888, virtually all public utilities filed open access tariffs, power resources were acquired over increasingly large regional areas, and interregional transfers of electricity increased. *Regional Transmission Organizations*, FERC Stats. & Regs. 32,541 at 33,689 (1999). Other industry-wide changes that occurred included: divestiture by many integrated utilities of some or all of their generating assets; increased numbers of new participants in the form of both power marketers and generators as well as independent power exchanges; increases in the volume of trade in the industry, particularly sales by marketers; state efforts to introduce retail competition; and, new and different uses of the transmission grid. *Id*. at 33,689-90.

The Commission found that "[t]he very success of Order Nos. 888 and 889, and the initiative of some utilities that have pursued voluntary restructuring beyond the minimum open access requirements, have placed new stresses on regional transmission systems stresses that call for regional solutions." *Id*. at 33,689. Accordingly, the Commission initiated a comprehensive inquiry of existing ISO policies, and concluded that transmission-related impediments were hindering a fully competitive wholesale electric market. *Id*. at 33,696.

In Order No. 2000,[4] the Commission concluded that regional institutions could address the operational and reliability issues confronting the industry, and the undue discrimination in transmission services that can occur when the operation of the

[4]*Regional Transmission Organizations*, Order No. 2000, FERC Stats. & Regs. ¶ 31,089 (1999), *on reh'g*, Order No. 2000-A, FERC Stats. & Regs. ¶ 31,092 (2000). *petitions for review dismissed sub nom., Public Utility District No. 1 of Snohomish County, Washington v. FERC*, 272 F.3d 607 (D.C. Cir. 2001).

transmission system remains in the control of a vertically integrated utility. Order No. 2000 at 30,993; 31,014-17. The Commission required all public utilities to file either a proposal to participate in an RTO or a description of efforts to participate in an RTO. *Id*. at 31,226-27.

C. Order No. 641

In light of the dramatic changes in the electric industry wrought by open-access transmission, functional unbundling of wholesale electric services, and the rapid movement to market-based power sales rates brought about by, *inter alia*, Order No. 888, state retail unbundling efforts, and Order No. 2000, the Commission concluded that its method of assessing annual charges no longer appropriately reflected FERC regulatory effort. Order No. 641 at 31,848, JA 132. The Order No. 472 methodology placed a heavy emphasis on power sales, *id*. at 31,851, JA 135, reflecting the fact that a significant part of the Commission's regulatory efforts concerned reviewing bulk power sale contracts. A shift occurred with the developments in the industry, as the Commission's electric regulatory program was increasingly devoted to assuring open and equal transmission access to public utilities' transmission systems. *Id*. at 31,849, JA 133. In contrast, the rapid movement to market-based power sales rates meant that wholesale power sales rates were increasingly disciplined by competitive market forces, not by FERC regulation. *Id*. The Commission therefore found it "fair and equitable," as required by OBRA, to change its methodology of assessing annual charges to one that relies solely on the volume of electric energy transmitted by public utilities in interstate

commerce. *Id*. at 31,849-50, JA 133-34. This approach also "is essentially the same as how annual charges are, in practice, assessed against gas pipelines." *Id*. at 31,849 n. 48, JA 133. The Commission rejected the argument that it was unfair to impose costs solely on transmission providers because the new methodology more appropriately reflected the current regulatory focus, *id*. at 31,851, JA 135, and power sellers will still pay some share of the annual charges, albeit indirectly, through providers' cost-based transmission rate, which will pass through the providers' annual charges to power sellers and other shippers. *Id*. at 31,849 n. 49, 31,850, JA 133, 134.

Consistent with Order No. 888, the Commission declined to assess annual charges based upon a public utility's bundled retail service that was not taken under a FERC-jurisdictional tariff. *Id*. at 31,850, JA 134 (citing Order No. 888-A at 30,217). This exception did not apply in the ISO or RTO context, however, because all transmission service on the integrated grid, including service for bundled retail, includes an unbundled transmission component and is jurisdictional service, taken pursuant to a FERC-jurisdictional tariff. *Id*. at 31,855 n. 69, JA 139. For example, PEPCO, a member of PJM (a mid-Atlantic ISO) takes service under the FERC-jurisdictional PJM tariff to serve its native load with bundled retail service, and in taking that service, it makes use of the entire PJM system and therefore obtains unbundled retail transmission service from other transmission-providing members of PJM. *Id*. Accordingly, the entire intra-ISO or RTO load, as well as other through (or export) transmission provided by the ISO or RTO, properly is made subject to annual charges assessments. *Id*.

The Commission found no inequity in this result because transmission providers (such as RTOs) that provide unbundled retail transmission service are providing comparatively more jurisdictional transmission service, and are therefore more responsible for the Commission's regulatory costs and should be assessed a comparatively higher annual charge. Order No. 641-A at 62,038, JA 148. The Commission also rejected the argument that this methodology would create disincentives for joining RTOs, finding that the Commission's assertion of jurisdiction over unbundled retail transmission, which was previously regulated by the state as part of bundled retail sales, should act to shift the regulatory burden and resulting costs from the state to the Commission, rather than creating a wholly new regulatory burden and resulting costs. *Id*. Further, the increase from assessing annual charges on unbundled retail transmission would result in only a small addition to transmission rates (and, unlike in the past, no addition to power sale rates). Order No. 641 at 31,851 and nn. 60-63, JA 135.

The Commission expects all public utilities (and others) to join RTOs which would avoid any unfairness between individual utilities in terms of assessments. *Id*. at 31,855 n. 68, JA 139. The Commission declined to postpone changing the methodology until that result was achieved, however, because it would benefit participants in the RTO development process to know earlier, rather than later, how the Commission intends to assess annual charges. *Id*. at 31,856, JA 140.

No party appealed Order No. 641.

D. Challenges to the First Annual Charges Implementing Order No. 641

In July 2002, the Commission issued the first bills under the new regulations, *see* R. 43 at 2, JA 152, and a number of parties, including petitioners, participated in proceedings on rehearing of those bills. *See Revision of Annual Charges to Public Utilities (California Independent System Operator, et al.)*, 101 FERC ¶ 61,043 at 61,161-62, *reh'g dismissed*, 101 FERC ¶ 61,326 (2002) ("Annual Charges Rehearing"), JA 200-04. Among other things, the parties argued the Commission's work load was no longer focused primarily on transmission; rather, they claimed power sale transactions occupy an equal amount of the workload, making it inequitable to allocate annual charges solely to transmission service. 101 FERC at 61,163, JA 202. Parties pointed to the Standard Market Design ("SMD") Notice of Proposed Rulemaking,[5] as an example of how both open access transmission and wholesale energy sales are subjects of attention, claiming that much of the Commission's current workload exhibits a similar dual focus. *Id*.

The Commission rejected the contention that its focus on transmission had changed since it enacted Order No 641.

> In addition, Order No. 641 pointed out that our attention was increasingly on transmission, where we are concentrating on assuring open and equal access for public utilities' transmission systems. This remains true. Compared to the 1980's and early 1990's, when our prior electric annual charges regulations were adopted, and annual charges were assessed to both those who sold electric energy and those who transmitted it, we are now focusing increasingly on transmission, through, for example, open access

[5] *Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design*, Notice of Proposed Rulemaking, 67 Fed. Reg. 55,452, FERC Stats. & Regs. ¶ 32,563 (2002) ("SMD NOPR").

> transmission-related filings and complaints, interconnection policy, and the formation and operation of Independent System Operators and Regional Transmission Organizations. Indeed, since the issuance of our Order Nos. 888 and 889, Order No. 641 is the first update to our electric annual charges regulations. And while the SMD NOPR does address wholesale markets, a primary focus of the SMD NOPR is transmission, in that it proposes a revised open access transmission tariff that is intended to remedy remaining undue discrimination in the use of the Nation's interstate transmission grid, and also proposes to establish a transmission congestion management system to ensure that the Nation's interstate transmission grid is managed efficiently.

Id. at 61,164, JA 203 (footnotes omitted).

No party appealed the Annual Charges Rehearing.

E. The Challenged Orders

On December 3, 2002, the Midwest ISO, the NYISO and PJM petitioned for commencement of a rulemaking to change the annual charges methodology back to the Order No. 472 methodology. Initial Order ¶ 7, JA 241. The Commission found that petitioners' arguments were belated attempts to seek rehearing of Order No. 641, and had, in any event, already been answered in Order No. 641 and the Annual Charges Rehearing. *Id*. ¶ 9, JA 241. While petitioners again disputed that FERC's workload continued to be primarily directed toward transmission, the Commission reiterated that it continues to focus on transmission. *Id*. ¶ 11, JA 241.

Petitioners pointed to Commission actions involving western markets, as well the SMD NOPR, as involving regulation of sales, but the Commission's primary efforts in reforming the western markets and the SMD NOPR has been on transmission. *Id*. ¶ 12, JA 242. "For example, the SMD NOPR proposes a revised open access transmission

tariff that is intended to remedy remaining undue discrimination in the use of the Nation's interstate transmission grid. The SMD NOPR also proposes to establish a transmission congestion management system to ensure that public utilities manage the Nation's interstate transmission grid efficiently." *Id*. Similarly, much of the Commission's efforts involving western markets go to whether public utilities have used transmission schedules and constraints to manipulate prices or exercise market power. *Id*.

The Commission reiterated its finding that annual charges are a legitimate cost of providing transmission service and therefore can be recovered in an RTO's rates. *Id*. ¶ 15, JA 242. "In this regard, they are no different than any other cost incurred by an RTO and may be recovered in the RTO's rates like any other costs incurred by the RTO." *Id*. The Commission rejected the contention that this constitutes assessing annual charges to nonjurisdictional utilities. *Id*. n. 25, JA 242. The charges are assessed to jurisdictional public utilities, such as RTOs or ISOs, who, in turn, properly recover these and their other costs in jurisdictional rates that are paid by all users of their services. *Id*.

On rehearing, petitioners again argued that the Commission's focus is no longer on transmission. Rehearing Order ¶¶ 12-15, JA 277-78. The Commission continued to find that "the thrust of the Commission's current work involves the regulation of transmission." Id. ¶ 18, JA 278. While petitioners again asserted that the Commission places more emphasis on energy sales, "[t]he way to make electric energy markets work more efficiently, however, is to remedy undue discrimination in transmission and to establish a transmission congestion management system to ensure that public utilities manage the Nation's interstate transmission grid efficiently." *Id*. Nonetheless, the

Commission left open the possibility that "the issues may merit further consideration at a later time and we will reevaluate whether a new rulemaking is warranted at that later time." *Id*. ¶ 16, JA 278. Even though the petition for rulemaking was a belated attempt to seek rehearing of Order No. 641, the Initial Order answered each of the points raised in the petition. *Id*. ¶ 17, JA 278.

On the transmission/sales question, the SMD NOPR emphasizes "the Commission's commitment to ensuring that public utilities do not use transmission schedules and constraints to manipulate market prices and exercise market power." *Id*. and n. 34, JA 278. To the extent that FERC orders directly address electric energy (*i.e*. sales) markets themselves, they propose tariff conditions that should make the need for such orders increasingly uncommon. *Id*. n. 34, JA 278 (citing *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 103 FERC ¶ 61,349 (2003)). Likewise, the California market-related matters are moving toward resolution. *Id*. (*see* California proceedings cited therein). The Commission staff's Final Report on Price Manipulation in Western Markets, (Docket No. PA02-2-000 Mar. 26, 2003), does not demonstrate a shift in focus to electric sales, as many activities that staff seeks to change involve improper use of the Nation's transmission network. *Id*. n. 33, JA 278.

The Commission rejected petitioners' speculation that the Order No. 641 annual charges methodology would discourage RTO participation, finding that RTOs have the ability and flexibility to recover annual charges from their ratepayers, and petitioners had failed to cite a single instance where RTO participation had been discouraged, noting that "in this regard, progress in the Midwest continues apace, notwithstanding the issuance of

Order No. 641." *Id*. ¶ ¶ 19-20, JA 278-79. The Order No. 641 methodology does not recover annual charges, directly or indirectly, from utilities that are not FERC-jurisdictional. Rather, the charges are assessed only to jurisdictional public utilities. *Id*. n. 35, JA 279. RTOs (or, indeed, any FERC-jurisdictional public utility) assessed annual charges may, in turn, seek to recover such costs in its rates for its transmission services. Nonjurisdictional entities that take such service must pay the filed rate for it, but inclusion of the annual charges as one cost component to be recovered in rates is not the same as the Commission collecting annual charges from non-jurisdictional utilities. *Id*. In fact, rate recovery for the charges does not differ from recovery of any other costs RTOs (or FERC-jurisdictional public utilities) legitimately incur in providing service. *Id*.

The Commission likewise rejected the contention that the treatment of electric annual charges conflicted with the treatment of natural gas annual charges. *Id*. n. 37, JA 279. "While our natural gas annual charges regulation nominally still assesses annual charges against natural gas pipelines, it does so based on natural gas 'subject to the Commission's regulation which was sold and transported.'" *Id*. (citing 18 C.F.R. § 382.202 (2003)). "That regulation, in other words, assesses natural gas annual charges only against natural gas pipelines and only on their natural gas sales subject to the Commission's regulation, *i.e*. only on 'jurisdictional sales volumes,'" which petitioners concede are now largely insignificant. *Id*. While the natural gas annual charge assessment nominally covers natural gas sales, for virtually all intents and purposes those assessments are primarily against transportation. *Id*.

SUMMARY OF ARGUMENT

OBRA requires that the Commission assess annual charges to recover its yearly regulatory program costs. Following OBRA's enactment, the Commission initially assessed electric annual charges based on each utility's power sales and transmission volumes. In 2000, in light of the Commission's increasing regulatory emphasis on assuring open access to transmission, Order No. 641 implemented a new methodology for annual charge assessments based on transmission volumes.

In 2002, the Midwest ISO, NYISO and PJM filed a petition for rulemaking urging the Commission to revert back to the prior method of assessing annual charges based on both transmission and sales. Petitioners raised "policy" concerns with the Order No. 641 methodology: (1) assessing annual charges only on transmission is unjustified so long as FERC regulates power sales; (2) assessing annual charges for bundled retail loads that are transmitted over RTO/ISO FERC-jurisdictional facilities creates disincentives for utilities to join RTOs; (3) including load of non-FERC jurisdictional RTO members in the calculation of the RTO's annual charge assessment constitutes improperly indirectly assessing annual charges to such utilities; and (4) assessing electric annual charges only on transportation conflicts with the Commission's treatment of gas annual charges.

These "policy" concerns were all raised and rejected in the Order No. 641 proceeding, in which petitioners participated, and from which they did not seek review. Accordingly, these "policy" concerns are collateral attacks on Order No. 641 that the Court lacks jurisdiction to hear.

Even if not jurisdictionally barred, petitioners' claims lack merit. The Commission reasonably exercised its discretion under OBRA in assessing annual charges based on transmission where transmission was increasingly the focus of regulation and power sellers would continue to contribute to payment of the annual charges, albeit indirectly, through the cost-based rates that they pay for transmission services. The Commission's treatment of electric annual charges reflects the reality of how gas annual charges are assessed as, on the gas side, gas sales by FERC-jurisdictional pipelines are negligible.

The Commission properly declined to assess annual charges for bundled retail load that does not use jurisdictional transmission service. For bundled retail loads carried across RTO/ISO facilities, however, annual charges are properly assessed because transmission over the RTO/ISO grid necessarily involves jurisdictional service. This is neither inequitable to nor penalizes RTOs; it merely ensures that annual charges are assessed where service under a FERC-jurisdictional tariff is being provided. There is no evidence that this allocation methodology discourages RTO participation, and the relative insignificance of annual charges in comparison to overall expenses of RTO/ISOs makes it unlikely that an increased annual charge would act as a significant disincentive.

The Commission also properly included the load of non-FERC jurisdictional RTO members in calculating annual charges to be assessed to RTOs, despite the fact that such entities' load would not have been subject to annual charges if the entity had not joined the RTO. ISOs and RTOs are public utilities that provide jurisdictional transmission service across their entire service areas pursuant to tariffs regulated by the Commission,

and that jurisdictional transmission service is properly subject to annual charges. RTOs can pass the annual charge assessments through their jurisdictional rates, notwithstanding the fact that some customers for jurisdictional services may not be FERC-jurisdictional entities, as recovery of annual charges, like recovery of any other cost properly included in jurisdictional rates, is appropriate from all those who use, and benefit from, the service.

As petitioners' "policy" concerns were all addressed and rejected in Order No. 641, their resurrection now constitutes an impermissible collateral attack on that order. To avoid this jurisdictional bar, petitioners contend significant changed circumstances since Order No. 641 – an alleged shift in the Commission's focus from assuring open access to regulating sales – requires that the Court compel institution of a new rulemaking. The Commission properly found no changed circumstances, given its continuing focus on assuring open access transmission as the means to achieve properly functioning energy markets. What the petitioners point to as market-related initiatives or activities are really transmission-related, primarily to alleviate congestion problems.

ARGUMENT

I. STANDARD OF REVIEW

The Court's review of the Commission's decision not to initiate further rulemaking on annual charges is "extremely limited." *National Labor Relations Board Union v. FLRB*, 834 F.2d 191, 196 (D.C. Cir. 1987); *WWHT, Inc. v. FCC*, 656 F.2d 807, 817 (D.C. Cir. 1981). The Commission has broad discretion in how to respond to requests to institute proceedings or promulgate rules. *See Action for Children's Television v. FCC*, 564 F.2d 458, 479 (D.C. Cir. 1977). "Administrative rulemaking does not ordinarily comprehend any rights in private parties to compel an agency to institute such proceedings or promulgate rules." *Id*. (quoting *Rhode Island Television Corp. v. FCC*, 320 F.2d 762, 766 (D.C. Cir. 1963)). Thus, "[i]t is only in the rarest and most compelling of circumstances that this court has acted to overturn an agency judgment not to institute rulemaking." *WWHT*, 656 F.2d at 818.

The judgment of the Commission not to proceed with rulemaking at this time must be left undisturbed if the Commission "adequately explained the facts and policy concerns it relied on, and there is nothing to indicate that the opinions of the Commission are unlawful, arbitrary, capricious or wholly irrational." *Id*. at 820. Further, where Congress has expressly delegated to an agency the responsibility for setting fees, the agency in exercising that authority "is at the zenith of its powers," and its fee determinations are "entitled to more than mere deference or weight." *Central and Southern Motor Tariff Association v. United States*, 777 F.2d 722, 729 (D.C. Cir. 1985) (quoting *American Trucking Association, Inc. v. United States*, 627 F.2d 1313, 1320 (D.C. Cir. 1980)).

As to the Commission's selection of rate methodology, because issues of rate design are fairly technical and involve policy judgments lying at the core of the regulatory mission, this Court's review of whether a particular rate design is just and reasonable is highly deferential. *Louisiana Public Serv. Comm'n v. FERC*, 174 F.3d 218, 231 (D.C. Cir. 1999); *Northern States Power Co. v. FERC*, 30 F.3d 177, 180 (D.C. Cir. 1994). The Court requires only that the Commission have made "a reasoned decision based upon substantial evidence in the record." *Town of Norwood v. FERC*, 962 F.2d 20, 22 (D.C. Cir. 1992). The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. FPA § 313(b), 16 U.S.C. § 825*l*(b).

II. THE COMMISSION PROPERLY DENIED THE PETITION FOR RULEMAKING.

Petitioners' so-called "policy" concerns (Br. at 23) with the Order No. 641 methodology assert that: (1) assessing annual charges only against transmission cannot be justified so long as FERC regulates power sales, Br. at 15, 26, 33; (2) assessing annual charges for bundled retail loads that are transmitted over RTO/ISO FERC-jurisdictional facilities creates disincentives for utilities to join RTOs, Br. at 23-26; (3) including the load of non-FERC jurisdictional RTO members in the calculation of RTO annual charge assessments constitutes improperly indirectly charging such utilities annual charges, Br. at 28-29; and (4) assessing electric annual charges only on transportation conflicts with the Commission's treatment of gas annual charges, Br. at 37-38.

These "policy" concerns were all raised and rejected in the Order No. 641 proceeding, in which petitioners participated, and from which they did not seek review.

Accordingly, as the time period for seeking review of Order No. 641 has long since expired, these "policy" concerns are no more than collateral attacks on Order No. 641 that the Court lacks jurisdiction to hear. Initial Order ¶ 9, JA 241; Rehearing Order ¶ 17, JA 278. *See Georgia Industrial Group v. FERC*, 137 F.3d 1358, 1363-64 (D.C. Cir. 1998) (to the extent petitioner raised issues that were considered in earlier rulemaking, those challenges were an impermissible collateral attack over which the Court lacks jurisdiction); *City of Nephi, Utah v. FERC*, 147 F.3d 929, 934 (D.C. Cir. 1998) (same). Even if they were not jurisdictionally barred, petitioners' claims lack merit.

To avoid the jurisdictional bar, petitioners attempt to show that circumstances since issuance of Order No. 641 have undergone such a "radical change," *see American Horse Protection Association, Inc. v. Lyng*, 812 F.2d 1, 4-5 (D.C. Cir. 1987) (cited Br. at 13), that the Court must compel institution of a new rulemaking. The radical change alleged is petitioners' view that the Commission's workload since Order No. 641 has shifted from transmission back to market (sales) regulation. The Commission reasonably rejected these "changed circumstances" claims, finding that its regulatory focus had not materially changed since Order No. 641.

A. Petitioners' Policy Arguments Are Impermissible Collateral Attacks On Order No. 641 And Are, In Any Event, Without Merit.

1. Assessing Annual Charges Solely To Transmission Providers When The Commission Also Regulates Sales

Petitioners contend that the Commission can justify assessing annual charges solely to transmission providers only by showing that "*no time* and/or *no Commission resources* were required to carry out FERC's regulatory responsibilities with respect to

power sales," because petitioners conclude that the methodology "exclude[s] wholesale sellers from annual charge assessments." Br. at 26. *See also* Br. at 15 (arguing FERC's annual charges are not fair and equitable because "the Commission's resources have not been dedicated solely to transmission issues"). According to petitioners, "[u]nless and until FERC disavows any continuing responsibility over merchant transactions," it is "indefensible for FERC's annual charges assessments to be calculated exclusively on transmission volumes." Br. at 33.

This argument was raised by numerous commenters in the Order No. 641 proceedings. *See, e.g.*, Comments of Arizona Public Service Company, R. 12 at 2, JA 45 ("Further, while Commission Staff's time may be 'increasingly devoted' to transmission-related issues, this does not mean 'entirely devoted' to such issues, and the proposed change effectively foists the entire program costs on transmission-related issues."); Comments of Avista Corporation, R. 22 at 10, JA 94 ("Further, FERC only asserts that *more* of the costs of FERC's electric regulatory program are associated with transmission. Even assuming that FERC should recover from transmission utilities the costs associated with transmission-related filings, it does not follow that *all* costs associated with all aspects of electric regulation should be recovered only from within the transmission sector.") (emphasis in original); Comments of the American Electric Power System, R. 26 at 2, JA 111 ("While it is true that the Commission's electric utility regulatory matters may be 'increasingly' devoted to transmission-related issues, the Commission cannot say that its activities are exclusively related to such activities. Certainly, part of the Commission's responsibilities relate to administration of market-

based rates; and indeed, the whole thrust of its regulatory program is directed to the development of competitive power markets for the benefit of consumers and the protection and benefit of all participants in those markets. Yet, under this proposal, only transmission owning public utilities will be assessed a charge for the Commission's regulatory fees.").

In Order No. 641, the Commission determined that the existing Order No. 472 methodology was no longer fair and equitable because it places a "heavy emphasis on power sales," when "the Commission has been reducing its regulation of the power sale business and that trend is continuing and even accelerating." Order No. 641 at 31,851, JA 135. Instead, the Commission determined "that the annual charges be borne by the entities and services on which we are now increasingly focusing," *i.e*. transmission providers and service. *Id*. This approach was fair and equitable, even though it involved "directly charging only those public utilities that provide transmission service," because "[a]ll parties involved in the generation and sale of electric energy rely on the transmission system to move their product. Thus, power sellers will be contributing to the Commission's recovery of its electric regulatory program costs in that they will be using the transmission system and, in any cost-based rates that they pay for transmission service that they may take, will pay, albeit indirectly, their share of the Commission's costs." *Id*. at 31,849 n. 49, JA 133. Accordingly, contrary to petitioners' contentions, *see* Br. at 26, the Order No. 641 methodology does not insulate power sellers from annual charges. Even though sales are not computed in the allocation factors, sellers pay a

portion of the costs through cost-based transmission rates and thus fund the increasingly smaller amounts of sales regulation done by FERC.

The Commission's approach is "expressly authorized by the Budget Act and the accompanying Conference Report." Order No. 641-A at 62,039, JA 149. OBRA requires the Commission to recover its costs by annual charges computed based on methods the Commission determines are "fair and equitable." *Id*. The Conference Report accompanying OBRA states that annual charges assessed to a person "may reasonably be based on" the "amount of energy – electricity, natural gas, or oil – transported or sold subject to Commission regulation by such person during such year." *Id*. (quoting H.R. Conf. Rep. No. 99-1012 at 238 (1986), *reprinted in* 1986 U.S.C.C.A.N. 3868, 3883 ("Conference Report")). This language permits the Commission to look to "each individual jurisdictional public utility's transmission in assessing an annual charge to that public utility." *Id*. *See also id*. at n. 28 (quoting Conference Report at 239 (1986 U.S.C.C.A.N. at 3884)) ("the Conference Report also stated that the conferees expected the Commission 'to assess annual charges proportionately on the basis of annual sales or volumes transported.'").

Thus, because in Order No. 641 the Commission considered and rejected the same "policy" concern that petitioners reassert here, such reassertions are an impermissible collateral attack (*see* Initial Order ¶ 9, JA 241; Rehearing Order ¶ 17, JA 278) over which the Court lacks jurisdiction.

Moreover, the Commission correctly found this choice of allocation methodology well within its discretion under OBRA. *See* Order No. 641-A at 62,039, JA 149. *See*

also Initial Order ¶ 9, JA 241; Rehearing Order ¶ 8, JA 277 (incorporating by reference responses to petitioners' arguments in Order Nos. 641 and 641-A). OBRA directs cost recovery through fees or annual charges "computed on the basis of methods that the Commission determines, by rule, to be fair and equitable." 42 U.S.C. § 7178(b). The statute does not direct what methodology is to be employed, nor does it require that annual charges be assessed on all regulated persons or transactions. In *Florida Power & Light Co. v. United States*, 846 F.2d 765 (D.C. Cir. 1988), the Nuclear Regulatory Commission ("NRC") assessed annual charges under an OBRA provision, 42 U.S.C. § 2213 -- which directed the NRC to "collect annual charges from its licensees" in an amount "reasonably related to the regulatory services provided by the Commission" -- on only one group of licensees, excluding all other licensees. *See Florida Power*, 846 F.2d at 770. The Court affirmed the methodology as within the NRC's discretion, notwithstanding arguments that the statute required charges to all licensees, in proportion to their size or profitability. *Id*. Here, the statute does not even arguably address how the Commission should allocate its costs among regulated entities or transactions. Thus, no statutory basis supports petitioners' contention that annual charges must be assessed against sales as well as transmission volumes.

The Conference Report provides that annual charges may be reasonably based on the amount of electricity "transported or sold subject to Commission regulation." 1986 U.S.C.C.A.N. 3883. The use of the disjunctive "or" permits the Commission to base its annual charges on the amount of *either* jurisdictional transportation *or* sales. *See Northwest Airlines, Inc. v. FAA*, 14 F.3d 64, 69 (D.C. Cir. 1994) (statute directing

approval of passenger facility charges for projects that will preserve capacity, reduce noise or enhance competition permitted FAA to approve charges for any project meeting "any *one* of the three statutory criteria.") (emphasis in original); *Brickner v. FDIC*, 747 F.2d 1198, 1202-03 (D.C. Cir. 1984) ("The use of the disjunctive 'or' between the words 'willful' and 'continuing' in the statute reveals a clear intent to make either one an offense.") *Five Flags Pipe Line Co. v. United States*, 1992 U.S. Dist. LEXIS 3881 at *32 (D.D.C. 1992), considered an OBRA provision requiring pipeline safety regulation fees to be based on usage in "reasonable relationship to volume-miles, miles, revenues, or an appropriate combination thereof." 49 U.S.C. App. § 1682a(a)(1). Use of mileage as the sole allocation criterion was upheld because the disjunctive statutory language "plainly contemplates that any of the three specified criteria could serve as the sole usage determinant, and gives the agency discretion to select among them." *Five Flags*, 1992 U.S. Dist. LEXIS 3881 at *32. Here, allocation based on transportation is permitted because the statute specifies no criteria, and the disjunctive language of the Conference Report suggests annual charges reasonably may be allocated on either jurisdictional transportation or sales. *See* Order No. 641-A at 62,039, JA 149.

Thus, petitioners' assertions that the Commission cannot assess annual charges solely based on transmission so long as it also regulates sales is an impermissible collateral attack on Order No. 641 and, in any event, lacks merit because the Commission was well within its discretion in adopting the Order No. 641 methodology.

2. Assessing Annual Charges To RTOS Based On Total Transmission

Petitioners contend that the Order No. 641 methodology is inequitable to public utility members of RTOs and creates a disincentive to RTO/ISO participation, because annual charges are assessed to RTO/ISOs based on total transmission, whereas public utilities that do not belong to RTOs are not assessed annual charges for service of bundled retail load "unless its load serving entity directly takes transmission service under a FERC jurisdictional transmission service tariff." Br. at 24.

This issue was raised in the Order No. 641 proceedings. Petitioners Midwest ISO Transmission Owners argued that the proposed methodology would create disincentives to RTO membership. *See* Comments, R. 15 at 6-7, JA 73-74. The Midwest ISO similarly argued that annual charges should only be recovered from FERC-jurisdictional transmission service under the Midwest ISO's tariff, which would exclude bundled retail load. Comments of the Midwest ISO, R. 28 at 6, JA 120. *See also* Comments of the Electric Power Supply Association, R. 5 at 4, JA 15 (arguing that excluding bundled retail load from utility assessments but not RTO assessments could create incentives not to join RTOS); Comments of Commonwealth Edison Company, R. 7 at 3-4, JA 26-27 (arguing that assessing annual charges against all Midwest ISO transmission service, including that taken by utilities on behalf of bundled retail load, would potentially create trapped costs for utilities). [6]

[6] In the Annual Charges Rehearing, the NYISO expressly recognized that "[a] number of commenters on the Proposed Regulation [Order No. 641 NOPR] protested that the changes envisioned by the Commission would unfairly and perversely shift a

As the Commission explained in Order No. 641, the assessment of annual charges, appropriately, turns on whether or not service is being provided under a FERC-jurisdictional tariff. *See* Order No. 641 at 31,849-50, 31,855 and nn. 58 and 69, JA 133-34, 139. Order No. 641 continued the approach taken in Order No. 888, holding that bundled retail service is not subject to Commission regulation. Order No. 641 at 31,850 and n. 58, JA 134 (citing Order No. 888-A at 30,217). In the past, retail sales occurred almost exclusively on a bundled basis, and, as the FPA reserved to states the right to regulate retail sales, the entire bundled transaction was left to state regulation. Order No. 888-A at 30,339. Accordingly, where a transmission provider purchases power on behalf of its native load customers, the Commission does not have jurisdiction over the transmission of the purchased power to the bundled retail customers insofar as the transmission takes place over such transmission providers' facilities, and the transmission provider was not required to take such service under its Order No. 888 *pro forma* tariff. *Id*. at 30,217.

However, to the extent that the transmission of the bundled retail sale takes place on the interstate facilities of other public utilities, the Commission does have jurisdiction

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disproportionate share of Commission electric program costs toward the very regions that had responded to the Commission's call for the formation of ISOs or Regional Transmission Organizations." Request for Rehearing of NYISO of first annual charges bills, R. 43 at 3, JA 153. The NYISO reasserted that argument, urging the Commission to impose annual charges on all bundled retail service. *Id*. at 12 and n. 5, JA 162, 152. The Midwest ISO and the Midwest ISO Transmission owners filed in support of the NYISO. Midwest ISO Motion to Intervene and Comments, R. 52 at 5, JA 197; Midwest ISO Transmission Owners Answer, R. 48 at 2-3, JA 191-92. The Commission held that it "rejected this approach in Order No. 641 and we are not inclined, in response to an untimely and collateral attack on Order No. 641, to overturn the tack taken in our electric annual charges regulations." Annual Charges Rehearing ¶ 15, JA 203.

over the transmission. *Id*. at 30,217 n. 128. Further, increasingly, retail transactions are broken into separate transmission and generation products. *Id*. at 30,339. When that occurs, the unbundled retail transmission is transmission in interstate commerce within the Commission's jurisdiction. *Id*.

Accordingly, in Order No. 641, the Commission determined that annual charges should not be assessed on a public utility's service of bundled retail customers on its own system, since any transmission involved would not be provided under that utility's FERC-jurisdictional tariff. Order No. 641 at 31,850, JA 134 (citing Order No. 888-A at 30,217). Conversely, annual charges are assessed on all FERC-jurisdictional transmission service, *i.e*. both wholesale and retail unbundled transmission (and bundled wholesale transmission). *Id*. at 31,849, JA 133. In the RTO/ISO context, all transmission service – even for bundled retail customers – is provided under the RTO/ISO FERC-jurisdictional tariff, over facilities of more than one public utility, and therefore is subject to the assessment of annual charges. *Id*. at 31,855 n. 69, JA 139. For example, when PEPCO takes service under the PJM tariff to serve its native load with bundled retail service, it makes use of the entire PJM system and, as such, obtains unbundled retail transmission service to the extent that the load is transmitted across the facilities of other transmission-providing members of PJM. *Id*.

As the Commission found, there is no inequity, *see* Br. at 24, nor penalty, *see* Br. at 35, in treating bundled and unbundled retail service differently for purposes of assessing annual charges. Order No. 641-A at 62,038, JA 148. *See also* Initial Order ¶ 9, JA 241; Rehearing Order ¶ 8, JA 277 (incorporating by reference responses to petitioners'

arguments in Order Nos. 641 and 641-A). Transmission providers (such as RTOs) providing unbundled retail transmission service are providing comparatively more jurisdictional transmission service, and are therefore more responsible for the Commission's regulatory costs and should be assessed a comparatively higher annual charge. Order No. 641-A at 62,038, JA 148.

Nor should this outcome operate as a disincentive to RTO membership. As bundled retail sales are regulated by the states, the Commission's assertion of jurisdiction over unbundled retail transmission should act to shift the regulatory burden and the resulting costs from the state to the Commission, rather than create a wholly new regulatory burden and attendant costs. *Id*.[7] The Commission also found that the increase from assessing annual charges on unbundled retail transmission would be small compared to the revenues currently being collected for unbundled retail transmission itself, and would be spread across all public utilities, resulting in only a small addition to transmission rates (with, unlike in the past, no addition to power sale rates). Order No. 641 at 31,851 and nn. 60-63, JA 135 (the Commission's 1999 total costs collected in annual charges (based on data reported for calendar year 1998) were $54,596,000, or less then 3 percent of total 1998 revenues collected just for "transmission for others" of approximately $2,000,000,000, and less than 0.2 percent of total revenues for "sales for

[7] Some three quarters of the lower 48 states collect regulatory assessments. Order No. 641 at 31,851, JA 135.

resale" (which includes a transmission component) that were in excess of $29,000,000,000).

The Commission declined to postpone implementing its regulations until RTOs were more widespread. *See* Br. at 24-25. The Commission's expectation that all individual public utilities (as well as others) would join RTOs would eliminate any claimed unfairness between individual utilities in terms of assessment of annual charges. Order No. 641 at 31,855 n. 68, JA 139. It was appropriate to proceed with the final rule before that expectation was realized, however, because the Commission believed that knowing earlier, rather than later, how the Commission intends to assess annual charges would benefit participants in the RTO process. *Id*. at 31,856, JA 140.

Thus, as this issue was likewise fully explored and rejected in the Order No. 641 proceedings, petitioners' reiterated claims here are collateral attacks and must be dismissed. In any event, the Commission's response to the same claims in Order No. 641 was fully adequate.

Moreover, the challenged Rehearing Order likewise rejected as speculation claims that the Order No. 641 annual charges methodology would discourage RTO participation. Rehearing Order ¶ 20, JA 279. *See also* Initial Order ¶ 9, JA 241; Rehearing Order ¶ 8, JA 277 (incorporating by reference responses to petitioners' arguments in Order Nos. 641 and 641-A). Petitioners failed to cite a single instance where it has done so. Rehearing Order ¶ 20, JA 279. Petitioners' contention on brief that they presented evidence of a single cooperative refusing to join the Midwest ISO because of the annual fees, *see* Br. at 35, does not withstand scrutiny. This evidence consisted of the following statement: "In

fact, the possibility of incurring additional costs associated with the FERC's annual fee has caused Eastern Kentucky Power Cooperative to delay its membership in the Midwest ISO until its Board is informed of such liability." Rulemaking Petition, R. 55 at 9, JA 213. The Commission could hardly have been expected to interpret this statement as evidence that Eastern Kentucky declined to join the Midwest ISO based on FERC's annual charges, much less as evidence that other entities were unwilling to join RTOs due to the annual charge expense.

To the contrary, the Commission observed that "progress in the Midwest [ISO development] continues apace, notwithstanding the issuance of Order No. 641." Rehearing Order ¶ 20, JA 279. Petitioners' own petition for rulemaking substantiates this finding. "The Commission has assisted the Midwest ISO materially in creating positive incentives for RTO participation," which has permitted the Midwest ISO "to increase[] its footprint substantially, and thus stand[] in a position to reduce its administrative adder as it is spread over a greater load." R. 55 at 7, JA 211. Among other things, approval of TRANSLink's participation in the Midwest ISO "has been an essential vehicle to secure the participation of public power entities on the western border of the Midwest ISO." *Id.*

Similarly, by enabling PJM to expand to include the Allegheny Power system, PJM's scope increased substantially, thus allowing its costs to spread over a larger load. *Id.* American Electric Power Company, Dayton Power & Light Company, Commonwealth Edison Company and Virginia Electric & Power Company also recently agreed to join PJM. *Id.* These observations support FERC's conclusion that RTO expansion was not hindered by the Order No. 641 methodology. In the face of such

concrete evidence, all petitioners could muster was vague speculation that "[i]f FERC asserts authority to assess annual charges to non-jurisdictional entities that may consider joining RTOs, some non-jurisdictional entities that have participated in RTOs voluntarily could decide to reevaluate their decisions." *Id*. at 9, JA 213. The Commission's conclusion is thus supported.

Petitioners also point to the alleged quadruple increase in the annual charges for the American Transmission Company LLC, as evidence that the methodology discourages RTO participation. *See* Br. at 34. [8] Nothing in this assertion undercuts the Commission's findings. The annual charge assessments are so small relative to overall expenses that they would not operate as a disincentive. *See* Order No. 641 at 31,851 and nn. 60-63, JA 135. *See also* Initial Order ¶ 9, JA 241; Rehearing Order ¶ 8, JA 277 (incorporating by reference responses to petitioners' arguments in Order Nos. 641 and 641-A). For example, in 2002, the NYISO was assessed annual charges of approximately $6.2 million. Request for Rehearing of NYISO, R. 43 at 1, JA 151. This represents less than 0.15 percent of the NYISO's total market expenses (including energy, ancillary services, congestion, losses and uplift expenses) of $4.6 billion. *See* NYISO 2002 Annual Report, available online at www.nyiso.com. Likewise, the American Transmission Company LLC (*see* Br. at 34) (a company providing only transmission service), was assessed annual charges of $ 2.4 million in 2002, Request for Rehearing of American Transmission

[8] Although petitioners also state in footnote 71 that PJM's annual charges in 2002 increased by $7.8 million, there is no statement of how that increase relates to prior annual charges or to PJM's overall expenses.

Company, LLC, R. 45 at 1, JA 166, or less than 2 percent of its total operating expenses of $131 million, ATCLLC 2002 Annual Report, available online at www.atcllc.com.

3. Including Load Of Non-Jurisdictional RTO Members In The Calculation Of Annual Charges

Petitioners contend that the Commission erred in including the load of non-FERC jurisdictional RTO members in the calculation of the RTO's annual charge assessment. Br. at 28-29. *See also* Br. at 36. According to petitioners, because "the transactions by non-jurisdictional entities would not have been used in calculating the FERC annual assessment if these non-jurisdictional entities had not joined an RTO," the Commission cannot "use RTO participation as an indirect means of exerting jurisdiction over non-jurisdictional entities." Br. at 28 n. 60.

This issue was also raised and rejected in the Order No. 641 proceeding. The Midwest ISO Transmission Owners contended that including annual fees in the transmission revenue requirements of RTO transmission owners would result in shifting program costs to entities not regulated by FERC, violating cost causation principles and the intent of OBRA § 3401 that the annual charges be based on the amount of energy subject to Commission regulation." Comments, R. 15 at 7-8, JA 74-75 (emphasis in original). Likewise, the NYISO objected to the payment of annual charges by RTOs because it would result in non-jurisdictional utility members of the RTO being subject to the annual charges. Comments of the NYISO, R. 16 at 4-5, JA 82-83. *See also* Joint Initial Comments of the Long Island Power Authority and the Power Authority of the State of New York, R. 6 at 4, JA 21 (expressing concern that, as they are non-

jurisdictional entities that are transmission-owning members of the NYISO, assessing annual charges against the NYISO may result in the "inadvertent collection" of annual charges from them or their customers if the NYISO passes on the charges through its rate schedule applicable to all NYISO transactions).

In Order No. 641, the Commission rejected the notion that ISOs or RTOs should be required to identify and to separate out for different rate treatment transmission service provided over the transmission systems owned by RTO member municipalities and other entities that are not "public utilities" under the FPA. Order No. 641 at 31,854-55 and n. 69, JA 138-39. ISOs and RTOs are public utilities that provide jurisdictional transmission service across their entire service areas pursuant to tariffs regulated by the Commission. *Id*. at 31,855 n. 69, JA 139. [9] In ISOs or RTOs, regional transmission services are provided over the system of more than one public utility, and thus all retail transactions involve an unbundled retail transmission component which is jurisdictional transmission. *Id*. Thus, it is appropriate that annual charges be assessed based on all the transmission that the ISO or RTO public utility provides. *Id*.

As petitioners' argument was raised and rejected in the Order No. 641 proceedings, and those proceedings were never appealed, the Court lacks jurisdiction to

[9] An RTO or ISO-wide rate charge avoids the prior problem of "pancaked" rates under which shippers had to pay a different rate to each transmission owner for use of its system. Now, an RTO or ISO collects a single rate for transmission across all facilities in its system. Each then allocates the rate revenues among all transmission owners (including nonjurisdictional owners) whose facilities were used. *See Pacific Gas and Electric Co. v. FERC*, 306 F.3d 1112, 1115 (D.C. Cir. 2002).

hear this argument now. As the Commission's response in Order No. 641 demonstrates, the argument, in any event, lacks merit.

The challenged orders again rejected the contention that the Order No. 641 methodology constitutes improperly assessing annual charges to non-jurisdictional utilities. Initial Order ¶ 15 and n. 25, JA 242; Rehearing Order n. 35, JA 279. *See also* Initial Order ¶ 9, JA 241; Rehearing Order ¶ 8, JA 277 (incorporating by reference responses to petitioners' arguments in Order Nos. 641 and 641-A). The annual charges are assessed to the RTOS or ISOs as jurisdictional public utilities, and the annual charges may be flowed through to all customers of the RTO's or ISO's jurisdictional services. Initial Order n.25, JA 242; Rehearing Order n. 35, JA 279. "In this regard, they are no different than any other cost incurred by an RTO and may be recovered in the RTO's rates like any other costs incurred by the RTO." Initial Order ¶ 15, JA 242. Petitioners fail to explain, because they cannot, how these annual costs differ from any other cost an RTO (or any other public utility) seeks to recover from all its customers in its rates. Rehearing Order n. 35, JA 279.

Permitting a jurisdictional public utility to recover legitimate costs of providing transmission service from all customers of that service, including those that are non-jurisdictional entities, follows proper cost causation principles and is not the same as collecting annual charges from those entities. *Id.* Rather, the annual charges, just like all other transmission-related costs, can be included in the rates charged to all customers for the transmission service. The fact that an entity paying the rate may not itself be

jurisdictional does not mean it should not have to pay this portion of the rate. Initial Order n. 25, JA 242.

Contrary to petitioners' assertions, see Br. at 29 (citing *Richmond Power & Light v. FERC*, 574 F.2d 610,620 (D.C. Cir. 1978)), this does not constitute the Commission doing indirectly what it cannot do directly. Rather, as the Commission has repeatedly recognized, non-jurisdictional utilities that use an ISO's or RTOs' service benefit from that service, and are thus properly required to pay their fair share of all costs of that service. *See, e.g., Midwest Independent Transmission System Operator, Inc.*, 101 FERC ¶ 61,113 (2002), *on reh'g*, 103 FERC ¶61,038 (2003), *appeal pending Midwest ISO Transmission Owners v. FERC*, No. 03-1163 (D.C. Cir.).[10] This Court has affirmed allocation of all costs to all customers on an integrated transmission grid, because all customers benefit from the integrated system. *Western Massachusetts Electric Co. v. FERC*, 165 F.3d 922, 927 (D.C. Cir. 1999).

Indeed, petitioners' proposed return to the pre-Order No. 641 annual charges would be equally suspect, because it assessed annual charges on sales and transmission of all users, including non-public utility ratepayers. Rehearing Order n. 35, JA 279. Not only would petitioners' proposal require jurisdictional customers to subsidize use of the

[10] RTOs benefit all users of the grid by: (1) improving efficiencies in grid management; (2) improving grid reliability; (3) removing opportunities for discriminatory practices; (4) improving market performance; and (5) facilitating lighter handed regulation. *See Public Utility District No. 1 of Snohomish County, Washington v. FERC*, 272 F.3d 607, 611 (D.C. Cir. 2001). Indeed, commenters in the Order No. 641 proceeding argued that it would be unfair not to require non-jurisdictional utilities to bear their share of all RTO costs for their use of the RTO system. *See, e.g.*, Comments of New England Power Company, R. 10 at 5, JA 32; Comments of the Edison Electric Institute, R. 25 at 6, JA 107; Answer of PJM, R. 46 at 9, JA 188.

system by non-jurisdictional users, but it would also invalidate any system of annual charges, and thus not be consonant with OBRA. *Id*. (citing Order No. 641-A, 94 FERC at 62,039).

4. Consistency With Treatment of Gas Annual Charges

Petitioners also contend that FERC's treatment of electric annual charges is inconsistent with its treatment of gas annual charges. Br. at 37-38. Again, this issue was raised in the Order No. 641 proceedings. The Commission expressly observed in Order No. 641 that its proposed approach was "essentially the same as how annual charges are, in practice, assessed against gas pipelines." Order No. 641 at 31,849 n. 48, JA 133. Commenters in that proceeding also observed that the proposed apportionment methodology was similar to the methodology used in the gas industry. *See* Comments of Northeast Utilities, R. 11 at 2, JA 37; Comments of the California ISO, R. 14 at 5 n. 8, JA 56. At least one commenter argued that there were differences in the gas and electric industries which warranted different treatment. Comments of Avista Corporation, R. 22 at 4-6, JA 88-90.

In any event, the challenged orders fully explained why treatment of annual charges on the gas side was consistent with Order No. 641. Rehearing Order n. 37, JA 279. "While our natural gas annual charges regulation nominally still assesses annual charges against natural gas pipelines, it does so based on natural gas 'subject to the Commission's regulation which was sold and transported.'" *Id*. (citing 18 C.F.R. § 382.202 (2003)). Gas sales are no longer regulated by FERC. *See* Natural Gas Wellhead Decontrol Act of 1989, Pub. L. No. 101-60, 103 Stat. 157. In other words,

natural gas annual charges are assessed "only against natural gas pipelines and only on their natural gas sales subject to the Commission's regulation, *i.e*. only on 'jurisdictional sales volumes,'" which petitioners concede are now largely insignificant. *Id*. "Thus, for virtually all intents and purposes, the Commission no longer assesses natural gas annual charges against natural gas sales, but instead assesses them now only against transportation." *Id*. That the Commission has not yet formally revised its natural gas annual charges does not bar updating electric annual charges. *Id*. In light of the increasing regulatory focus on transmission noted by the Commission, failing to update the electric annual charges would be contrary to OBRA. *Id*. (citing Order No. 641-A, 94 FERC at 62,039.)

Petitioners do not dispute that gas annual charges are, for all practical purposes, assessed based on transportation rather than on sales. Br. at 37. They assert that application of the same rule on the electric side would be unfair because, unlike gas, a significant amount of the load across public utility transmission facilities continues to be bundled retail service. *Id*. at 37-38. However, such bundled retail service is not taken under a jurisdictional tariff, and is therefore not subject to annual charges because bundled retail sales are not subject to Commission review and the Commission incurs no costs associated with their regulation. Order No. 641-A at 62,037-38, JA 147-48.

B. Petitioners Have Failed To Show A "Radical Change" In Circumstances That Would Justify Requiring A New Rulemaking.

To avoid the jurisdictional bar and lack of merit to their "policy" objections to the Commission's methodology, petitioners argue that significant changed circumstances

since the promulgation of the Order No. 641 require that the Commission undertake a new rulemaking. *See* Br. at 16-23.

As this Court has specified, "an agency may be forced by a reviewing Court to institute rulemaking proceedings if a significant factual predicate of a prior decision on the subject (either to promulgate or not to promulgate specific rules) has been removed." *WWHT*, 656 F.2d at 819. No significant factual predicate has been removed since Order No. 641. As a result, petitioners' cases based on the presence of a significant change, *see* Br. at 13, are inapposite, and petitioners' claims must be rejected. *See* Rehearing Order ¶ 21, JA 279 (rejecting petitioners' reliance on *Tesoro Alaska Petroleum Co. v. FERC*, 234 F.3d 1286 (D.C. Cir. 2000), because it was limited to a specific set of rates, not a rulemaking, and in any event it was inapplicable where, as here, there are no substantially changed circumstances).

Petitioners recognized the substantial change in circumstances between Order No. 472 and Order No. 641. When Order No. 472 was issued, "the bulk of the Commission's time was dedicated to reviewing the prices set forth in bulk power sales contracts pursuant to section 205 of the Federal Power Act." Petition for Rulemaking, R. 55 at 11, JA 215. By the time of Order No. 641, with the "evolution of market-based sales certificates and the issuance of Order No. 888, the focus of the Commission's efforts shifted dramatically from sales to providing open access nondiscriminatory transmission access according to the strictures of Order No. 888." *Id*. at 11-12, JA 215-16. "In addition, the Commissioners themselves began a push for more ISOs and ultimately RTOs, and that initiative culminated in Order No. 2000." *Id*. at 12, JA 216. These

dramatic changes in the regulatory landscape warranted the Order No. 641 modification of the annual charges methodology. *Id*. *See* Order No. 641 at 31,848-49, JA 132-33.

Having conceded the premises for enacting Order No. 641, petitioners argue here that there has been a "radical change," *see American Horse*, 812 F.2d at 4-5, in the Commission's Order No. 641 focus on transmission that requires reverting back to the sales-oriented Order No. 472 methodology. This purported "radical change" allegedly is evidenced by FERC's response to the California market crisis with its resulting effects and investigations, Br. at 19-20, and Commission market oversight initiatives, such as SMD and the development of the Office of Market Oversight and Investigations ("OMOI"), Br. at 21.

Petitioners' radical change claims are, like its other claims, nothing new. Numerous commenters in the Order No. 641 proceeding argued that the Commission's caseload contained too much emphasis on market-related matters for the Order No. 641 methodology to be fair and equitable. *See* Comments of New England Power Company, R. 10 at 3-4 and n. 2, JA 30-31 (asserting that many then-current Commission matters directly relate to "market disputes, market rules and procedures, market-based rate requests, etc., and do not implicate transmission schedules or tariffs"); Comments of Arizona Public Service Company, R.12 at 2, JA 45 (noting FERC Staff is "involved in evaluating filings dealing with cost-of-service based power sales rates" that had been set for hearing); Comments of Avista Corporation, R.22 at 10, JA 94 (arguing all costs should not be charged to transmission because, "[a]s the Commission itself has acknowledged, there are significant costs associated with the filings of non-transmission

entities."); Comments of the Operating Companies of the American Electric Power System, R. 26 at 2, JA 111 (arguing all costs should not be assessed based on transmission, because "[c]ertainly, part of the Commission's responsibilities relate to administration of market-based rates, and, indeed, the whole thrust of its regulatory program is directed to the development of competitive power markets for the benefit of consumers and the protection and benefit of all participants in those markets"). Thus, petitioners' perceived emphasis on markets now represents no radical shift away from the circumstances at the time of Order No. 641.

Further, intervenor NYISO raised the same arguments raised here in the Annual Charges Rehearing, contending, *inter alia*, that the forecasted changes in the electric market on which Order No. 641 was based have failed to materialize. R. 43 at 9, JA 159. NYISO claimed that, since 2000, the Commission continued to place "tremendous emphasis and resources on investigating (and curbing) electric trading and market power abuses," including "proposing a Standard Market Design for national application," *id*. at 10, JA 160, and that, following the California market crisis, many states reversed or slowed retail unbundling, *id*. at 11, JA 161. *See also* Answer of PJM, R. 46 at 6, JA 185 (arguing that "[o]ver the last year, the Commission has spent countless hours devoted to wholesale markets issues, conducting numerous market manipulation investigations, addressing pricing disputes, and holding conferences on standard market design," and established OMOI). The Midwest ISO filed comments in support of the NYISO request for rehearing. R. 52 at 4, JA 196. The Commission considered and rejected all these claims, which are now echoed by petitioners. Annual Charges Rehearing at 61,164, JA

203. As judicial review of the Annual Charges Rehearing was never sought, the Court lacks jurisdiction to consider collateral attacks on that rejection again in this proceeding.

In any event, the Annual Charges Rehearing and the challenged orders reasonably disagreed that FERC's regulatory focus had changed since Order No. 641, finding still that "the thrust of the Commission's current work involves the regulation of transmission." Rehearing ¶ 18, JA 278. Aside from FERC's obvious ability to summarize its own workload, nothing suggests that the Commission has, since Order No. 641, disavowed or limited its effort to further Order No. 888 and Order. No. 2000 goals throughout the electric industry; rather restructuring the market to ensure open access to the transmission of electricity remains a primary regulatory focus:

> In addition, Order No. 641 pointed out that our attention was increasingly on transmission, where we are concentrating on assuring open and equal access for public utilities' transmission systems. This remains true. Compared to the 1980's and early 1990's, when our prior electric annual charges regulations were adopted, and annual charges were assessed to both those who sold electric energy and those who transmitted it, we are now focusing increasingly on transmission, through, for example, open access transmission-related filings and complaints, interconnection policy, and the formation and operation of Independent System Operators and Regional Transmission Organizations. Indeed, since the issuance of our Order Nos. 888 and 889, Order No. 641 is the first update to our electric annual charges regulations.

Annual Charges Rehearing ¶ 14, JA 203 (footnotes omitted). *See also* Initial Order ¶ 11, JA 241.

Petitioners assert that market monitoring initiatives, such as the SMD, evidence a shift back to regulation of sales rather than transmission. *See* Br. at 21-22. Petitioners fail to appreciate the Commission's efforts to make electric energy markets more efficient

by "remedy[ing] undue discrimination in transmission and [establishing] a transmission congestion management system to ensure that public utilities manage the Nation's interstate transmission grid efficiently." Rehearing ¶ 18, JA 278. Open access transmission counters the fact that, "[h]istorically, electrical utilities were vertically integrated, owning generation, transmission, and distribution facilities and selling these services as a 'bundled' package to wholesale and retail customers in a limited geographical service area." *Public Utility District No. 1 of Snohomish County*, 272 F.3d at 610 (D.C. Cir. 2001). While economic changes and significant technological advances resulted in many new entrants into generating markets able to sell energy at lower prices, barriers to a competitive wholesale market nonetheless remained, because utilities still controlled the transmission facilities and favored their own generation in transmission. *Id*.

Thus, a major impediment to competitive wholesale sales markets is the transmission owners' use of their transmission systems to benefit their own generation over that of others. *See Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 683-84 (D.C. Cir. 2000). "The exercise of transmission market power allows transmission providers with power marketing interests to benefit in the short-run by making more power sales at higher prices, and benefit in the long-run by deterring entry by other market participants. As a result, prices to the Nation's electricity consumers will be higher than need be." *Regional Transmission Organizations*, FERC Stats. & Regs. ¶ 32,541 at 33,704-05. Accordingly, promoting competitive wholesale electric sales

markets requires curbing utilities' ability and incentive to exercise market power through discriminatory access to transmission.

The Commission's initiatives to which petitioners point address this very discrimination. "Both the SMD NOPR and the more recent White Paper on a Wholesale Market Platform emphasize the Commission's commitment to ensuring that public utilities do not use transmission schedules and constraints to manipulate market prices and exercise market power." Rehearing ¶ 18 and n. 34, JA 278 (citing Initial Order ¶¶ 10-12; Annual Charges Rehearing ¶ 14, and White Paper (Docket No. RM01-12-000 April 28, 2003)). The SMD NOPR recognized that "across most of the nation, barriers to entry remain for new generators and new load-serving entities," and are "directly attributable to the continued ability of vertically integrated transmission providers to exercise some degree of transmission market power to advantage their own or affiliated generation." SMD NOPR ¶¶ 38-39. The SMD NOPR proposed a revised open access transmission tariff that is intended to remedy remaining undue discrimination, and to establish a transmission congestion management system that will improve the efficiency of the Nation's interstate transmission grid. Annual Charges Rehearing ¶ 14, JA 203; Initial Order ¶ 12, JA 241-42.

Petitioners rely upon references to improving energy sales markets in the 2001 and 2002 Annual Performance Reports as evidence of FERC's emphasis on sales rather than transmission. *See* Br. at 20-21, nn. 40, 41. Such reliance confuses the goal with the means. The Commission's regulatory focus is designed to assure true open access transmission as the key to successful competitive power sales markets. While the

Commission's goal remains completing "the transition to competitive energy markets as quickly and comprehensively as possible," the "best sustainable path" to reach this goal "is to establish regional transmission organizations (RTOs) implementing fair market rules." *See, e.g.*, Annual Performance Report for Fiscal Year 2003 (available online at http://www.ferc.gov/about/strat-docs/FY03-PR.pdf).

Similarly, the *Standards of Conduct for Transmission Providers*, Order No. 2004, 105 FERC ¶ 61,248 (2003), Br. at 22 and n. 46, involves regulation of transmission market power. The regulation set forth new standards so that "Transmission Providers cannot extend their market power over transmission to wholesale energy markets by giving their Energy Affiliates unduly preferential treatment." *Id*. ¶ 1. *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 105 FERC ¶ 61,218 (2003), see Br. at 22 n. 46, imposes market behavior rules, such as the prohibition of transactions manipulating market prices, that are applicable to transmission services, *id*. ¶ 31; prohibitions on submitting false information, which includes transmission-related matters such as scheduling, *id*. ¶ 59; prohibitions on transactions that create artificial congestion and then "relieve" the congestion, *id*. ¶ 70; and prohibitions on utilities commingling transmission and wholesale merchant personnel, *id*. ¶ 126.

While petitioners tout the creation of OMOI as "the establishment of an entirely new organization within the FERC," OMOI actually "bring[s] together all of the Commission staff devoted to energy market oversight and enforcement." FERC 2002 Annual Report at 11 (available online at http://www.ferc.gov/about/strat-docs/annual_report.pdf). In other words, OMOI was created by reorganization to

centralize staff members working on oversight issues. Reorganizing staff scarcely constitutes "the establishment of an entirely new organization," nor is OMOI's role limited to enforcement of sales issues, but addresses transmission issues as well.

As "strong indications that FERC's involvement in merchant activities is far from over," petitioners point to "market-based congestion management systems and real-time imbalance markets" and the "adoption of day-ahead and real-time energy markets and the creation of industry-wide Financial Transmission rights to hedge the risks of congestion." Br. at 32. This argument merely serves to prove the Commission's point, as these matters relate to transmission, specifically to management of congestion, which occurs when demand for transmission over particular facilities is greater than the capacity of those facilities. Market-based congestion management systems provide incentives to alleviate congestion problems. The operation of day-ahead and real-time energy markets aids in managing congestion. *See* SMD NOPR ¶ 221. Financial transmission rights (or congestion revenue rights) are financial tools that allow customers to hedge against the costs of transmission congestion. *Id*. ¶ 208. Similarly, an energy imbalance, "the difference between the energy the transmission customer schedules a day ahead on the system and the amount that it takes off the system in real time," affects the rate paid by a transmission customer, and thus is also a transmission-related concept. *Id*. ¶ 222.

While FERC orders still directly address electric energy markets, the Commission is proposing to implement tariff conditions that should reduce the need for such orders. Rehearing Order n. 34, JA 278 (citing *Investigation of Terms and Conditions of Public Utility Market-Based Rate Authorizations*, 103 FERC ¶ 61,349 (2003)).

Likewise, the Commission's actions involving the western markets focus on whether public utilities have used transmission rate schedules and constraints to manipulate prices or exercise market power. Initial Order ¶ 12, JA 242. For example, the Commission staff's Final Report on Price Manipulation in Western Markets, (Docket No. PA02-2-000 March 26, 2003), while addressing electric sales, focuses significantly on activities that involved improper use of the transmission network. Rehearing Order n. 33, JA 278. *See, e.g.*, Final Report at 12 (describing trading strategy known as "load shift" which involved submitting artificial load schedules to obtain interzonal transmission congestion payments); *id*. at 26 (describing trading strategies known as "non-firm exports," "death star" and "wheel-out," all of which are designed to generate payments for relieving transmission congestion by "fooling" the California ISO's computerized congestion management program).

Further, the California market crisis was in effect a "perfect storm" that has not reoccurred, and whose effects are being resolved. The spikes in electricity prices experienced in California during the summer of 2000 were caused by a confluence of increased natural gas costs, a general electricity supply shortage, and significant flaws in the California market structure after restructuring. *See In re California Power Exchange Corp.*, 245 F.3d 1110, 1116 (9th Cir. 2001). The lack of new capacity in California, notwithstanding the state's rapid economic growth, made the California market vulnerable. This vulnerability was exposed in 2000 by a series of other conditions: a severe drought that curtailed hydropower energy imports; virtually non-existent demand side response in part because of fixed retail rates; and a hot summer followed by a cold

winter. *See generally* Annual Performance Report for Fiscal Year 2001 at 5 (available online at http://www.ferc.gov/about/strat-docs/FY01-PR.pdf).

The Commission remedied the market flaws by, *inter alia*, ordering a number of prospective structural and rule changes for the California electricity market, *San Diego Gas & Electric Co*., 93 FERC ¶ 61,294 (2000), and determining appropriate refunds, *San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services Into Markets Operated by the California Independent System Operator and the California Power Exchange*, 102 FERC ¶ 61,317, *on reh'g*, 105 FERC ¶ 61,066 (2003). Investigations examined whether any entity manipulated prices in electricity or natural gas markets or otherwise exercised undue influence over wholesale electricity prices. *Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Prices*, 98 FERC ¶ 61,165 (2002). Entities that appeared to have engaged in anomalous market behavior were ordered to show cause why they should not be found in violation of gaming practice provisions. *See, e.g., American Electric Power Corp.,* 103 FERC ¶ 61,345 (2003). Appeals of these Commission orders are currently pending. *See Public Utilities Commission of the State of California v. FERC*, Nos. 01-71051, *et al.* (9th Cir.). Final FERC orders concerning long-term contracts, *see* Br. n. 37, have issued, and appeals of those orders are also pending. [11] Thus, to the extent that the Commission is still involved

[11] *See Public Utility Commission of the State of California v. FERC*, Nos. 03-74207, *et al*. (9th Cir.) (appeals of *Public Utility Commission of the State of California v. Sellers of Long Term Contracts to the California Department of Water Resources, et al*., 103 FERC ¶ 61,354 (2003)); *Public Utility District No. 1 of Snohomish County, Washington v. FERC*, Nos. 03-74208, *et. al* (9th Cir.) (appeals of *Nevada Power Co. v.*

in California market-related matters, those matters are being resolved. Rehearing Order n. 34 (*see* California proceedings cited therein), JA 278. In view of this, the Commission properly viewed its activities as a one-time effort to cure a highly unusual situation, not as a harbinger of the future direction of its regulatory actions.

Given that petitioners' purported strong indicators of continued involvement in merchant activities are either transmission-related or nearing FERC resolution, petitioners have failed to support their claim that the trend toward greater emphasis in FERC's operation on transmission open access, which formed the basis for Order No. 641, has radically changed since then. Without a "radical change" from circumstances that supported Order No. 641, there are no grounds to compel the Commission to start a new rulemaking in this area. Accordingly, the petition should be denied.

Enron Power Marketing, Inc., 105 FERC ¶ 61,185 (2003)); *PacifiCorp v. FERC*, No. 04-1060, *et al*. (appeals of *PacifiCorp v. Reliant Energy Services, Inc*., 105 FERC ¶ 61,184 (2003)).

CONCLUSION

For the reasons stated, the Commission's orders should be affirmed in all respects.

Respectfully submitted,

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June 7, 2004

Midwest Independent Transmission System Operator, Inc., et al. v. FERC,
D.C. Cir. No. 03-1238

CERTIFICATE OF COMPLIANCE

In accordance with Circuit Rule 28(d)(1), I hereby certify that this brief contains 13,161 words, not including the tables of contents and authorities, the certificate of counsel, this certificate and the addendum.

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