

**ORAL ARGUMENT HAS NOT BEEN SCHEDULED**

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

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**Nos. 04-1148, *et al.* (consolidated)**

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**NATIONAL ASSOCIATION OF REGULATORY  
UTILITY COMMISSIONERS, *et al.*,  
PETITIONERS,**

**v.**

**FEDERAL ENERGY REGULATORY COMMISSION,  
RESPONDENT.**

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**ON PETITIONS FOR REVIEW OF ORDERS OF THE  
FEDERAL ENERGY REGULATORY COMMISSION**

**BRIEF OF RESPONDENT  
FEDERAL ENERGY REGULATORY COMMISSION**

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**JULY 31, 2006**

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## CIRCUIT RULE 28(a)(1) CERTIFICATE

### A. Parties and Amici

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

### B. Rulings Under Review

1. *Standardization of Generator Interconnection Agreements and Procedures*, Order No. 2003, 104 FERC ¶ 61,103 (2003);

2. *Standardization of Generator Interconnection Agreements and Procedures*, Order No. 2003-A, 106 FERC ¶ 61,220 (2004);

3. *Standardization of Generator Interconnection Agreements and Procedures*, Order No. 2003-B, 109 FERC ¶ 61,287 (2004);  
and

4. *Standardization of Generator Interconnection Agreements and Procedures*, Order No. 2003-C, 111 FERC ¶ 61,401 (2005).

### C. Related Cases

The Order No. 2003 rulemaking challenged in this appeal concerns the standardization of interconnection agreements involving large generators. The case captioned *Consolidated Edison Co. v. FERC*, Nos. 06-1018, *et al.* (consolidated), currently pending before this Court, concerns the Order No. 2006 rulemaking on the standardization of small generator interconnection agreements. *Standardization of Small Generator Interconnection Agreements and Procedures*, Order No. 2006, 111 FERC ¶ 61,220 (2005), *on reh'g*, Order No. 2006-A, 113 FERC ¶ 61,195 (2005).

The case captioned *Entergy Services, Inc. v. FERC, et al.*, Nos. 05-1238, *et al.*, currently pending before the Court, challenges the Commission's action on remand of

*Entergy Services, Inc. v. FERC*, 391 F.3d 1240 (D.C. Cir. 2004), which includes application of the so-called “at or beyond” rule, which is also at issue in this appeal, and other issues concerning generator interconnections.

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July 31, 2006

## GLOSSARY

EPAct	Energy Policy Act of 1992, Pub. Law No. 102-486
FERC	Federal Energy Regulatory Commission
FPA	Federal Power Act
TAPS	<i>Transmission Access Policy Study Group v. FERC</i> , 225 F.3d 667 (D.C. Cir. 2000)

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**STATEMENT OF THE ISSUES**

Following notice and comment, the Federal Energy Regulatory Commission (Commission or FERC) issued a rule (Order No. 2003), requiring public utilities that own, control, or operate transmission facilities to have on file standard procedures and a standard agreement for interconnecting generators larger than 20 megawatts with their transmission systems. The issues presented in the consolidated challenges to that rule are:

1. Whether the Commission acted within its jurisdictional authority under the Federal Power Act (FPA), in requiring public utilities providing electric transmission service to amend their Commission-approved open access transmission tariffs to include standard procedures and an agreement for interconnecting their systems with large generators.

2. Whether the pricing policies established by Order No. 2003, particularly the requirement that electric Transmission Providers offer transmission service credits for the costs of Network Upgrades required by generator interconnection, paid upfront by interconnecting generators, are reasonable.<sup>1</sup>

3. Whether Petitioners' remaining attacks on specific terms and conditions of Order No. 2003 are without merit.

## **STATUTORY AND REGULATORY PROVISIONS**

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

## **INTRODUCTION**

A decade ago, in its Order No. 888 rulemaking, the Commission established the foundation for development of competitive bulk power markets in the United

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<sup>1</sup> Capitalized terms used throughout this brief are defined in the Standard Large Generator Interconnection Procedures and Agreement, Appendix C to Order No. 2003, JA 210-305.

States: non-discriminatory open access transmission services by public utilities.<sup>2</sup>

In the rulemaking challenged here, recognizing the critical role played by generator interconnections in assuring non-discriminatory open access to the interstate transmission grid, the Commission applied the principles established in Order No. 888 -- affirmed by this Court and the Supreme Court -- to the standardization of procedures for generator interconnections. *Standardization of Generator Interconnection Agreements and Procedures*, Order No. 2003, 104 FERC ¶ 61,103 (2003), JA 64, *on reh'g*, Order No. 2003-A, 106 FERC ¶ 61,220 (2004), JA 607, *on reh'g*, Order No. 2003-B, 109 FERC ¶ 61,287 (2004), JA 919, *on reh'g*, Order No. 2003-C, 111 FERC ¶ 61,401 (2005), JA 978.

On appeal, petitioners assert that various aspects of the rulemaking are inconsistent with Order No. 888 and other Commission precedent, and violate the jurisdictional bounds of the FPA. The Commission demonstrated that in Order No. 2003 it merely applied principles already established in Order No. 888 and other

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<sup>2</sup> *Promoting Wholesale Competition Through Open Access Non-discriminatory 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) (“TAPS”), *aff'd*, *New York v. FERC*, 535 U.S. 1 (2002).

precedent to generator interconnections, and in no way exceeded its FPA jurisdictional authority that was recognized and affirmed in Order No. 888.

The other principal area of contention concerns interconnection pricing and cost allocation. The Commission allocated interconnection costs in accordance with its long-standing policy that transmission system network facilities benefit all customers on the system. Therefore, the costs of Network Upgrades associated with interconnections, paid upfront by interconnecting generators, should be spread among all network customers and recovered through transmission service credits. On the other hand, Interconnection Facilities which merely link the generator with the network benefit only the generator which, therefore, should bear all the costs of those facilities. The Commission distinguished between Network Upgrades and Interconnection Facilities by means of its established “At or Beyond” policy, which provides that network facilities begin at the point where the Interconnection Facilities connect to the network.

## **STATEMENT OF FACTS**

### **I. ORDER NO. 888 RULEMAKING – NON-DISCRIMINATORY ACCESS TO TRANSMISSION**

In Order No. 888, the Commission promoted the development of competitive bulk power markets in the United States through non-discriminatory open access transmission services by public utilities. Order No. 2003 P 8, JA 67. Order No. 888 required transmission owners to provide transmission services to others, and

for such owners and their affiliates to take transmission on their own facilities, under the same terms and conditions offered to others. *New York*, 535 U.S. at 10; *Enron Power Marketing, Inc. v. FERC*, 296 F.3d 1148, 1151 (D.C. Cir. 2002). This requirement of non-discrimination or comparability is one of the foundations of Order No. 888. *Id.*

Under FPA sections 205 and 206, 16 U.S.C. §§ 824d-e, the Commission is required to address, and has authority to remedy, undue discrimination or preference in the provision of jurisdictional service. Order No. 2003 P 18, JA 69-70. The Commission must ensure that the rates, contracts, and practices affecting jurisdictional transmission service do not reflect an undue preference or advantage for particular transmission providers and are just and reasonable. *Id.*

The record underlying Order No. 888 showed that public utilities owning or controlling jurisdictional transmission facilities were discriminating in the bulk power markets, in violation of the FPA, by providing either inferior access to their transmission networks or no access at all to third-party wholesale suppliers of power. *New York*, 535 U.S. at 11; Order No. 2003 P 19 JA 70 (citing Order No. 888 at 31,679-84; Order No. 888-A at 30,209-10). The Commission further concluded that it had authority and responsibility to remedy the undue discrimination it had found by ordering open access transmission service on an industry-wide basis -- a conclusion which was affirmed by this Court and the

Supreme Court. Order No. 2003 P 19 JA 70 (citing Order No. 888 at 31,668-73, 31,676-79; Order No. 888-A at 30,201-12; *TAPS*, 225 F.3d at 687-88; *New York*, 535 U.S. at 1).

In Order No. 888, the Commission was required to assess and apply its statutory authority in light of the changes in the industry. Under FPA section 201, 16 U.S.C. § 824(a)-(b), FERC regulates wholesale sales and interstate transmission, and state agencies retain jurisdiction over bundled retail transactions, including the intrastate sale and distribution of electricity through local distribution facilities. *TAPS*, 225 F.3d at 691. Initially, this regulatory division was easily applied as most transactions involved either wholesale or retail sales, and correspondingly either jurisdictional transmission or local distribution facilities. *Id.*

As the electric industry evolved, however, this changed. In the past, utilities generally relied on each other to provide power to respond to demand spikes to avoid having to build additional generating capacity. Eventually, non-utility generators started producing electricity, and power marketers began to buy and resell electricity to other power marketers, utilities, or even directly to consumers. These market participants do not own transmission lines, so they rely upon the utilities that own such facilities to provide transmission services. In addition to their traditional bundled sales activity, vertically integrated utilities started

“unbundling” their own services and developing their own power marketing units to buy and sell electricity at wholesale. Some states even mandate unbundling of retail services. *Id.* As a result, “facilities once used solely for local distribution of bundled retail sales now engage regularly in unbundled wholesale transmissions and retail delivery as well.” *Id.* “Thus, while the electricity world was once neatly divided into spheres of retail versus wholesale sales, and local distribution versus transmission facilities, such is no longer the case.” *Id.*

In Order No. 888, “FERC reinterpreted FPA § 201 to accommodate the new industry practices and conditions.” *Id.* While the Commission in Order No. 888 did not assert jurisdiction over local distribution facilities, *New York*, 535 U.S. at 23, it found that, where facilities are used to provide delivery to both wholesale purchasers and end users, the Commission and the States have jurisdiction to set rates for the services that are within their respective jurisdictions. Order No. 888 at 31,969 n.13. The Commission’s “assertion of jurisdiction over all wholesale transmissions, regardless of the nature of the facility, is clearly within the scope of its statutory authority.” *TAPS*, 225 F.3d at 696. *See also, e.g., Detroit Edison Co. v. FERC*, 334 F.3d 48, 51 (D.C. Cir. 2003) (“when a local distribution facility is used in a wholesale transaction, FERC has jurisdiction over that transaction pursuant to its wholesale jurisdiction under FPA § 201(b)(1)”).

## II. ORDER NO. 2003 RULEMAKING – NON-DISCRIMINATORY ACCESS TO INTERCONNECTION

Order No. 888 did not directly address generator interconnection issues. In *Tennessee Power Co.*, 90 FERC ¶ 61,238 (2000), the Commission recognized that interconnection was a critical component of open access transmission service and thus was subject to the requirement that utilities offer comparable, non-discriminatory service under the terms of their open access transmission tariffs. Order No. 2003 P 9, JA 67. Interconnection plays a crucial role in bringing generation into the market as relatively unencumbered entry is necessary for competitive markets. *Id.* P 11, JA 68.

Prior to Order No. 2003, the Commission had addressed interconnection issues on a case-by-case basis, which resulted in complex, time-consuming disputes about interconnection feasibility, cost and cost responsibility. *Id.* This undermined the ability of generators to compete in the market and provided an unfair advantage to utilities that owned both generation and transmission facilities. *Id.* The Commission accordingly concluded that there was a pressing need for a single set of procedures for jurisdictional Transmission Providers and a single, uniformly applicable interconnection agreement for Large Generators.<sup>3</sup> *Id.* A

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<sup>3</sup> In a separate rulemaking, the Commission established procedures and an interconnection agreement applicable to Small Generators (any energy resource having a capacity of no more than 20 megawatts, or the owner of such a resource)

standard set of procedures as part of the open access transmission tariff for all jurisdictional transmission providers would minimize opportunities for undue discrimination and expedite the development of new generation, while protecting reliability and ensuring that rates are just and reasonable. *Id.*

Thus, the Commission found that interconnection is a critical component of open access transmission service, and standard interconnection procedures and a standard agreement applicable to Large Generators would serve several important functions: (1) limit opportunities for Transmission Providers to favor their own generation; (2) facilitate market entry for generation competitors by reducing interconnection costs and time; and (3) encourage needed investment in generation and transmission infrastructure. Order No. 2003 P 12, JA 68. At its core, Order No. 2003 was intended to ensure that generators independent of Transmission Providers and generators affiliated with Transmission Providers are offered Interconnection Service on comparable, non-discriminatory terms. Order No. 2003-A P 3, JA 610. Order No. 2003 required all public utilities that own, control, or operate facilities used for transmitting electric energy in interstate commerce to

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that seek to interconnect to jurisdictional Transmission Providers. *See Standardization of Small Generator Interconnection Agreements and Procedures*, Order No. 2006, 111 FERC ¶ 61,220 (2005), *on reh'g*, Order No. 2006-A, 113 FERC ¶ 61,195 (2005), *reh'g pending*. That rulemaking is currently under review before this Court in the case captioned *Consolidated Edison Co., et al. v. FERC*, D.C. Cir. Nos. 06-1018, *et al.* (consolidated).

have on file standard procedures and a standard agreement for interconnecting Large Generators to their Transmission Systems. Order No. 2003-B P 5, JA 920.

Order No. 2003 did not, however, expand the Commission's jurisdiction beyond that asserted in Order No. 888 and upheld by this Court and the Supreme Court. Order No. 2003-A P 6, JA 610; Order No. 2003-B P 7, JA 921. Order No. 2003 applies only to an interconnection to a public utility's Transmission System that, at the time the interconnection is requested, is used either to transmit electric energy in interstate commerce under a Commission-filed open access transmission tariff or to sell electric energy at wholesale in interstate commerce. *Id.*

To develop the standard interconnection procedures and agreement, the Commission issued an Advance Notice of Proposed Rulemaking on October 25, 2001. *Standardizing Generator Interconnection Agreements and Procedures, Advance Notice of Proposed Rulemaking*, 66 Fed. Reg. 55,140, FERC Stats. & Regs. ¶ 35,540 (2001). As a point of departure, the Advance Notice of Proposed Rulemaking presented the Standard Generator Interconnection Agreement of the Electricity Reliability Council of Texas. Order No. 2003 P 13, JA 68. The Commission supplemented and modified the Texas interconnection documents with various "best practices" that were based, in part, on generator interconnection procedures and agreements that had been approved by the Commission in past cases. *Id.*

The Advance Notice of Proposed Rulemaking initiated a consensus-making process in which members of various segments of the electric power industry, government and the public had an opportunity to provide input. *Id.* This effort resulted in two documents, the Consensus Large Generator Interconnection Procedures and the Consensus Large Generator Interconnection Agreement, that largely shaped the Large Generator Interconnection Notice of Proposed Rulemaking that followed. *See Standardization of Generator Interconnection Agreements and Procedures, Notice of Proposed Rulemaking*, 67 Fed. Reg. 22,250, FERC Stats. & Regs. ¶ 32,560 (2002). The Commission received numerous comments on the Notice and the two documents. Order No. 2003 P 14, JA 69. Although the commenting parties did not reach consensus on every issue, the Standard Large Generator Interconnection Procedures and the Standard Large Generator Interconnection Agreement, as ultimately promulgated, reflect substantial agreement among diverse interests. *Id.* P 15, JA 69.

### **III. ORDER NO. 2003 DETERMINATIONS**

The Commission findings challenged in this appeal, discussed in greater detail *infra* in the Argument Section of this brief, can be summarized as follows:

The Commission applied the jurisdictional determinations of Order No. 888 in asserting jurisdiction over: (i) interconnections for wholesale sales over distribution facilities; (ii) interconnections for wholesale sales made pursuant to a

net metering arrangement where the entity subject to net metering is a net seller; (iii) interconnections for transmitting power generated by a special type of “qualifying facility” to third parties in interstate commerce; and (iv) interconnections to the public utility-owned portion of facilities jointly-owned with non-jurisdictional entities. Order No. 2003 PP 804, 807 & n.130, 813 n.136, JA 183, 184, 185-186; Order No. 2003-A, PP 730, 747 JA 717, 720; Order No. 2003-C P 51, JA 987-988.

The comparability principle of Order No. 888 -- requiring a transmission owner to provide service to others on the same terms and conditions as it provides service to itself and its affiliates -- supported Order No. 2003: (i) requiring public utilities to exercise their right of eminent domain on behalf of an Interconnection Customer *if* the public utility exercises eminent domain rights for its own interconnections; (ii) permitting non-jurisdictional entities to interconnect so long as they provide the affected public utility comparable reciprocal service; and (iii) requiring transmission providers to pay interconnection customers for reactive power within the established power factor range if the transmission provider pays its own or affiliated generators for reactive power in that range. Order No. 2003 PP 391, 843 & n.146, JA 122, 141; Order No. 2003-A PP 300, 416, 775, JA 646, 662-663, 724; Order No. 2003-C P 48, JA 987.

The need to preclude public utility favoritism toward its own and affiliated generation justified: (i) affording more flexibility in pricing to independent transmission providers than that provided to non-independent transmission providers; and (ii) requiring additional disclosures for affiliate interconnection requests as compared to the disclosures required for non-affiliated interconnection requests. Order No. 2003-A PP 107, 587, JA 622, 690.

The long-standing policy that network facilities benefit all system customers justified generally charging the cost of network upgrades, needed to accommodate interconnection, to all customers, while directly assigning to the generator the cost of the facilities connecting the generator to the network, as differentiated by the established “At or Beyond” test. Order No. 2003 P 21 & n.24, JA 70; Order No. 2003 P 66 & n.52, JA 78.

Generators are required to fund network upgrades initially, subject to repayment through credits against the bills they receive for transmission service, in order to provide the transmission owner with funds to construct upgrades and provide the generators incentives to make efficient siting decisions and good faith interconnection requests. Order No. 2003 PP 720, 723 JA 167; Order No. 2003-A P 613, JA 696. As the generator’s upfront payment is in the nature of a loan, the transmission owner is required to pay interest, and to repay the loan within 20 years, which is the approximate minimum life of typical network upgrades. Order

No. 2003-A P 618, JA 697; Order No. 2003-B P 36, JA 927-928; Order No. 2003-C P 9 n.9, JA 980.

To provide the transmission owner an incentive to construct interconnection and network facilities on schedule, parties were permitted -- but not required -- to include liquidated damages clauses in the interconnection agreement. Order No. 2003-A P 249, JA 639.

To ensure the quality of transmission access necessary to compete in the energy marketplace, Order No. 2003 established Network Energy Resource Interconnection Service, requiring the Transmission Provider to undertake Interconnection Studies and Network Upgrades needed to integrate a Generating Facility into the Transmission System, in a manner comparable to which the Transmission Provider integrates its own generating facilities to serve native load customers. Order No. 2003-A PP 500, 506; JA 672, 673.

## SUMMARY OF ARGUMENT

### I.

In Order No. 2003, the Commission asserted no jurisdiction beyond that exercised in Order No. 888 and affirmed by this Court and the Supreme Court. Nevertheless, Petitioners claim Order No. 2003 improperly asserted jurisdiction over: (i) interconnections for making wholesale sales that require use of distribution facilities; (ii) interconnections involving facilities jointly owned by jurisdictional and non-jurisdictional entities; (iii) interconnections involving net metering participants which are net sellers into the market; (iv) interconnections for the purpose of transmitting Qualifying Facility power in interstate commerce to third parties; and (v) interconnections requiring the use of utilities' state eminent domain powers to obtain property rights.

To the contrary, however, each of these matters falls well within the Commission's established jurisdiction over wholesale sales, transmissions in interstate commerce, and the public utilities engaging in such transactions. The minimal label affixed to the facilities over which service is provided, and to which the interconnecting generator seeks access, is not controlling; the presence of a FERC-jurisdictional activity is.

## II.

Order No. 2003's pricing and crediting policies for Interconnection Facilities are reasonable and should be sustained.

The Commission applied its previously-established policy that facilities at or beyond the point of interconnection are Network Upgrades, the costs of which are assigned to the Transmission Provider. Contrary to Petitioners' argument, the agency did not previously employ a policy authorizing direct assignment of costs to Interconnection Customers for facilities at the interconnection point. Nor has the Court rejected the Commission's use of the At or Beyond test.

Order No. 2003's assignment of Network Upgrade costs to the Transmission Provider is reasonable and well within the Commission's FPA authority. This policy choice is based on the finding, endorsed by this Court, that, in an integrated transmission system, network facilities benefit all customers on the system and should not be assigned to a particular customer. In this regard, the agency adequately ensured that a Transmission Provider's customers would not subsidize Interconnection Customers.

Moreover, the Commission appropriately allowed independent Transmission Providers, such as Regional Transmission Organizations, greater latitude in allocating interconnection costs. Because of their independence, such Transmission Providers have no reason to discriminate against new generators

interconnecting with the system, while non-independent Transmission Providers have the incentive to favor their own generators.

Order No. 2003's determination that upfront payments by Interconnection Customers for interconnection costs must be reimbursed by Transmission Providers within 20 years, the approximate minimum life of Network Upgrades, is likewise reasonable.

### III.

Petitioners' remaining contentions are without merit. The Commission adequately explained that Network Resource Interconnection Service is necessary because it differs from and does not overlap with already available transmission delivery services.

The Commission applied the Order No. 888 reciprocity requirement in permitting non-public utilities to avail themselves of the Order No. 2003 interconnection procedures and agreements so long as the non-public utilities offer interconnection service on their own system comparable to that offered to their own or affiliated generation. This means that a non-public utility is not required to pay transmission credits for Network Upgrades unless the non-public utility similarly pays credits to its own or affiliated generation for Network Upgrades. Order No. 2003 also appropriately required Transmission Providers to pay interconnected generators for the provision of reactive power (necessary to

maintain transmission line voltage) to the same extent as they paid their own generators.

The Commission's determination that the identity of affiliates making interconnection requests must be disclosed, even though the identity of other customers seeking interconnection does not have to be disclosed, does not unduly discriminate against affiliates of the interconnecting public utility. The additional disclosure is required to address concerns that transmission providers will favor affiliated entities through preferential access to information.

Finally, contrary to Petitioners' contention, Order No. 2003 does not mandate that a Transmission Provider be subject to a liquidated damages provision in an Interconnection Agreement. Rather, relevant sections of the rule include a liquidated damages provision as merely one option for negotiation.

## ARGUMENT

### I. STANDARD OF REVIEW

The “deferential standard” of *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984), applies to “an agency’s interpretation of its own statutory jurisdiction.” *TAPS*, 225 F.3d at 694. On other issues, the Commission’s orders are reviewed under the arbitrary and capricious standard, under which a “court must consider whether the decision was based on a consideration of relevant factors and whether there has been a clear error of judgment. . . . The court is not empowered to substitute its judgment for that of the agency.” *ExxonMobil Gas Marketing Co. v. FERC*, 297 F.3d 1071, 1078 (D.C. Cir. 2002) (citations and internal quotation marks omitted). *See also, e.g., Central Vermont Pub. Serv. Corp. v. FERC*, 214 F.3d 1366, 1369 (D.C. Cir. 2000).

“[I]n light of the technical nature of rate design, involving policy judgments at the core of the regulatory function,” review of the Commission’s ratemaking decisions is “highly deferential.” *Entergy Services, Inc. v. FERC*, 319 F.3d 536, 541 (D.C. Cir. 2003) (*Entergy I*), citing *Sithe/Independence Power Partners v. FERC*, 165 F.3d 944, 948 (D.C. Cir. 1999). Finally, the finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. FPA § 313(b), 16 U.S.C. § 825l(b).

## **II. THE COMMISSION, APPLYING THE DETERMINATIONS AND POLICIES OF ORDER NO. 888, ACTED ENTIRELY WITHIN ITS JURISDICTION.**

In Order No. 2003, the Commission confined its assertion of jurisdiction to the limits set in Order No. 888 and affirmed by this Court and the Supreme Court. Nonetheless, Petitioners offer a number of arguments that the Commission exceeded its jurisdiction under the FPA. As recognized by the Commission in the Order No. 2003 series of orders, however, none of these arguments has any merit, and the Commission has stayed within its jurisdiction at all times.

### **A. The Commission Properly Asserted Jurisdiction Over Interconnections For The Purpose Of Making Wholesale Sales.**

#### **1. Commission Jurisdiction Extends To Wholesale Sales Employing Distribution Facilities.**

Order No. 2003 “applies to interconnections to the facilities of a public utility’s Transmission System that, at the time the interconnection is requested, may be used either to transmit electric energy in interstate commerce or to sell electric energy at wholesale in interstate commerce pursuant to a Commission-filed [open access transmission tariff].” Order No. 2003-C P 51, JA 987; Order No. 2003 P 804, JA 183. *See also* Order No. 2003-A P 710, JA 713-714. The Commission’s assertion of jurisdiction over interconnections in Order No. 2003 thus rested on two grounds: first, and primarily, the Commission’s FPA jurisdiction over “transmission” facilities, which may be used for wholesale sales

or unbundled retail sales and which are subject to an open access transmission tariff; and, second, the Commission’s FPA jurisdiction over wholesale sales, made under an open access transmission tariff, which require the use of “local distribution” facilities. Order No. 2003-C PP 51, 53, JA 987, 988-989.<sup>4</sup>

Utility and Governmental Petitioners challenge the second jurisdictional ground, asserting that FPA § 201(b), which precludes Commission jurisdiction over local distribution facilities, also precludes jurisdiction over wholesale sales occurring over such facilities. Utility Br. 8-11; Governmental Br. 18-25. This would, however, write out of the statute Congress’ specific grant of jurisdiction to the Commission over wholesale sales.

FPA section 201(b)(1) confers jurisdiction on the Commission over the transmission of electric energy in interstate commerce, and sales of electric energy at wholesale in interstate commerce. FPA § 201(b)(1) further provides Commission jurisdiction over “all facilities for such transmission or sale of electric energy” except that it “shall not have jurisdiction, except as specifically provided in this Part and the Part next following, over . . . facilities used in local distribution. . . .” *Id.*

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<sup>4</sup> The term “distribution” usually refers to lower voltage lines that are not networked and that carry power in one direction. Order No. 2003 P 803, JA 183; Order No. 2003-A P 710 n. 157, JA 713. The term “local distribution” is a legal term, and under FPA § 201(b)(1) the Commission lacks jurisdiction over “local distribution” facilities. *Id.*

FPA § 201(b)(1) thus provides the Commission jurisdiction over interstate transmission and wholesale sale transactions separate from its jurisdiction over facilities used to complete those transactions. Accordingly, FERC has jurisdiction over a wholesale sale, even if the sale transaction occurs over a local distribution facility. *Detroit Edison*, 334 F.3d at 51. As this Court held on review of Order No. 888, FPA § 201(b) denies FERC jurisdiction over local distribution facilities “*except as specifically provided in this subchapter and subchapter III.*” 225 F.3d at 696 (emphasis in *TAPS*) (quoting FPA § 201(b)). FPA § 201(a) “makes clear that all aspects of wholesale sales are subject to federal regulation, regardless of the facilities used.” *Id.* Thus, FERC’s assertion of jurisdiction over all wholesale transmissions, regardless of the nature of the facility used, is “clearly within the scope” of its statutory authority. *Id.* See also *New York*, 535 U.S. at 23 (affirming that Order No. 888 did not improperly assert jurisdiction over local distribution facilities).

Similarly, states have jurisdiction over local distribution service – *i.e.*, the service of delivering electricity to retail end users – even where that service is provided over facilities that include no identifiable local distribution facilities. *Detroit Edison*, 334 F.3d at 51. Thus, whatever the classification of the facility involved, customers must take any FERC-jurisdictional service under a utility’s FERC-filed open access transmission tariff, but must take any non-jurisdictional

service, such as unbundled retail distribution, under a state tariff. *Id.* See Order No. 888 at 31,969 n. 13 (where facilities are used to provide delivery to both wholesale purchasers and end users, the Commission and the States have jurisdiction to set rates for services that are within their respective jurisdictions).

In Order No. 2003, the Commission exercised the same jurisdiction asserted in Order No. 888 and affirmed in *TAPS* and *New York*. Order No. 2003-A PP 705, 731, JA 712, 717. The Commission would continue to exercise exclusive jurisdiction over the rates, terms, and conditions of the Commission-jurisdictional service provided over “distribution” facilities, but would not assert jurisdiction over all uses of those facilities, because the regulation of “local distribution” of electricity to end users is reserved to the states. *Id.* In other words, the Commission would regulate the entire transmission component (rates, terms and conditions) of the wholesale transaction – whether the facilities used to transmit are labeled “transmission” or “local distribution” – but it would not regulate the “local distribution” facility itself, which remains state jurisdictional. Order No. 2003-C P 53, JA 988-989.

**2. The Commission’s Determination Is Fully Consistent With *Detroit Edison*.**

Petitioners contend the Commission’s jurisdictional determination is contrary to *Detroit Edison*, 334 F.3d at 54. Utility Br. 10; Governmental Br. 19, 22-23.

However, *Detroit Edison* does not prohibit the Commission from asserting

jurisdiction over wholesale sales, even if the sales occur over local distribution facilities. Order No. 2003-A P 730, JA 717 (citing *Detroit Edison*, 334 F.3d at 51). To the contrary, *Detroit Edison* expressly found that “when a local distribution facility is used in a wholesale transaction, FERC has jurisdiction over that transaction pursuant to its wholesale jurisdiction under FPA § 201(b)(1).” Order No. 2003-C P 52 & n.41, JA 988 (citing *Detroit Edison*, 334 F.3d at 51).

*Detroit Edison* recognized that “FERC has jurisdiction over all interstate transmission service and over all wholesale service, but FERC has no jurisdiction over unbundled retail distribution service, *i.e.* unbundled retail service over local distribution facilities.” *Detroit Edison*, 334 F.3d at 51. Customers take any FERC-jurisdictional transmission service under a utility’s open access transmission tariff, and take non-FERC-jurisdictional service, such as unbundled retail distribution, under a state tariff. *Id.* States retain jurisdiction over local distribution service even where there are no identifiable local distribution facilities. *Id.* (citing Order No. 888 at 31,783). *Detroit Edison* found that FERC exceeded its statutory jurisdiction by asserting jurisdiction over *all* transactions occurring on “distribution” facilities, including unbundled retail distribution service, based on the fact that jurisdictional wholesale transactions also occurred over those facilities. *Id.* at 53-54.

Thus, *Detroit Edison* prohibited the Commission from asserting *exclusive* jurisdiction over local distribution facilities used for both unbundled retail distribution and wholesale sales. Order No. 2003-A P 706, JA 712-713. *Detroit Edison* did not prohibit the Commission from asserting jurisdiction over wholesale sales that use “distribution” facilities. *Id.* P 730, JA 717 (citing *Detroit Edison*, 334 F.3d at 51). While the Commission may not assert jurisdiction over a non-jurisdictional activity based simply on the provisions of a voluntarily-filed tariff, *see Columbia Gas Transmission Corp. v. FERC*, 404 F.3d 459, 463 (D.C. Cir. 2005), cited in Governmental Br. 20-21, that is not the case here where FERC is only exercising authority over jurisdictional wholesale sales occurring on distribution facilities that are already accommodating jurisdictional service under an open access transmission tariff.

### **3. The Order No. 888 Seven-Factor Test Is Inapplicable.**

Governmental Petitioners assert that the Commission should have employed its so-called seven-factor test<sup>5</sup> from Order No. 888 to determine whether distribution facilities at issue are state or FERC-jurisdictional. Governmental Br. 23-25. However, as this Court explained on review of Order No. 888, “[t]he seven factor test applies only to *unbundled retail sales*, where FERC seeks to regulate

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<sup>5</sup> The seven-factor test evaluates on a case-by-case basis whether the activities of the facilities in question correspond with seven indicators of local distribution. *See* Order No. 888 at 31,981.

pursuant to the separate grant of jurisdictional authority over transmission in interstate commerce.” *TAPS*, 225 F.3d at 696 (emphasis added). *See also* Order No. 888 at 31,783; Order No. 2003-A P 711 n. 158, JA 714. In contrast, here, the Commission is asserting jurisdiction only over *wholesale sales* occurring on “distribution” facilities that already accommodate wholesale sales under an open access transmission tariff. Thus the nominal classification of such facilities does not determine eligibility for FERC-jurisdictional interconnection. Order No. 2003-A P 711, JA 714.

**4. The Commission Reasonably Addressed Identification Of Facilities Subject To The Open Access Transmission Tariff.**

Governmental Petitioners further contend that the Commission’s assertion of jurisdiction over distribution facilities covered by an open access transmission tariff “remains profoundly problematic” because it is unclear what specific facilities are covered by open access transmission tariffs. Governmental Br. 25. However, in most cases there will be no controversy about whether a facility is under the open access transmission tariff. Order No. 2003-A P 712, JA 714. Almost all interconnections to lower-voltage or “distribution” facilities will be under state jurisdiction. *Id.* P 732, JA 717. Such facilities are not subject to Order No. 2003, which applies to facilities already operating under a FERC-jurisdictional open access transmission tariff. *Id.* P 735, JA 718. Distributed generation

facilities almost always interconnect to lower-voltage facilities that are not subject to an open access transmission tariff. *Id.* P 739, JA 718-719.

When there is a dispute, there may be no simple method of determining whether a facility is under an open access transmission tariff, and a review of the Transmission Provider's rate filings may still not allow a determination. *Id.* Accordingly, the Commission concluded that the only reasonable method for identifying which facilities are subject to a Transmission Provider's open access transmission tariff is to rely on the Transmission Provider in the first instance to make this information available to the Interconnection Customer during the scoping meeting or earlier. *Id.* If the Interconnection Customer disagrees with the Transmission Provider's conclusion that the facility in question lies within or outside of the Transmission Provider's open access transmission tariff, it should bring the issue to the attention of the Commission. *Id.*

Governmental Petitioners contend that this solution is unworkable because "FERC lacks the staff, experience and expertise to oversee distribution-level interconnections," and the issue will "quickly overwhelm the FERC's resources." Governmental Br. 27. This ignores in the first instance FERC's finding that, in most cases, there will be no controversy about whether a facility is under the open access transmission tariff. Order No. 2003-A P 712, JA 714. Further, FERC is entitled to deference to its reasonable predictions of the effect of its policy and its

own capacity to make the determinations necessary to effectuate that policy. *See, e.g., Louisiana Energy & Power Auth. v. FERC*, 141 F.3d 364, 370 (D.C. Cir. 1998) (Court “ordinarily defer[s]” to a “reasonable agency prediction about the future impact of its own regulatory policies”); *Environmental Action, Inc. v. FERC*, 939 F.2d 1057, 1064 (D.C. Cir. 1991) (“It is within the scope of the agency's expertise to make . . . a prediction about the market it regulates, and a reasonable prediction deserves our deference . . . .”)

**B. The Commission Properly Asserted Jurisdiction Over Public Utilities’ Share of Facilities Jointly-Owned With Non-Jurisdictional Entities.**

Order No. 2003 followed the Commission’s treatment of jointly-owned facilities in Order No. 888. In Order No. 888, governing open access transmission service, the Commission required each public utility that owned interstate transmission facilities jointly with a non-jurisdictional entity to offer service over its share of the joint facilities, even if the joint ownership contract prohibits service to third parties. Order No. 888 at 31,962. The Commission required public utilities to file a proposed revision (mutually agreeable or unilateral) to their contracts with the non-jurisdictional owners to permit third party access. *Id.* The revision had, at a minimum, to permit third party use of the public utility’s share of the joint facilities and must provide for any needed cost allocation procedures between the public utility and the non-jurisdictional owners. *Id.* Absent this

requirement, the Commission reasoned, jurisdictional public utilities would be able to evade the open access requirements simply by contracting with non-jurisdictional entities. *Id.*

In Order No. 888-A, the Commission rejected arguments that it could not properly require a public utility to file unilaterally a modification to agreements concerning joint transmission facilities that a non-jurisdictional entity opposes:

It is without question that the Commission has the exclusive authority to regulate public utilities engaged in the sale for resale and/or transmission of electric energy in interstate commerce to assure that rates, terms and conditions are just and reasonable and not unduly discriminatory. The fact that a public utility may jointly own, with a non-jurisdictional entity, transmission facilities through which it engages in sales for resale and/or transmission of electric energy in interstate commerce does not alter the Commission's authority to regulate the public utility. If the Commission finds that a matter needs to be remedied, it may issue an order directed at the public utility. The fact that such an order may affect a non-jurisdictional joint owner does not undermine the validity of the Commission's order. Otherwise, a public utility could simply enter into joint agreements with non-jurisdictional utilities to the frustration of the Commission's mandate to protect consumers from undue discrimination.

Order No. 888-A at 30,219 (footnotes omitted).

Applying this principle, the Commission in Order No. 2003, governing open access to interconnection service, similarly concluded that joint ownership does not affect the Commission's authority to regulate a public utility, and therefore that the Interconnection Procedures and Agreement applied to Interconnection Service provided by a public utility on its portion of a jointly-owned facility. Order No.

2003 P 807 & n. 130, JA 184 (citing Order No. 888 at 31,692; Order No. 888-A at 30,219). “If a portion of a facility is owned by a jurisdictional public utility, the Interconnection Customer seeking interconnection for a Commission-jurisdictional purpose will be able to secure interconnection to that facility under the terms of Order No. 2003 through the jurisdictional co-owner of the facility.” Order No. 2003-A P 753 & n.176, JA 721 (citing Order No. 888 at 31,692). Moreover, if the joint ownership agreement prohibits or restricts the right of the public utility to offer interconnection service to third parties, the public utility must file proposed revisions (mutually agreeable or unilateral) to its contracts with the non-jurisdictional co-owners to remove those restrictions. *Id.* P 754 & n.177, JA 721 (citing Order No. 888 at 31,692).

Utility Petitioners attempt to distinguish the interconnections addressed in Order No. 2003 from the transmission service addressed in Order No. 888, asserting that, factually, Order No. 888 open-access transmission, unlike Order No. 2003 Interconnection Service, can be provided solely over a jurisdictional co-owner’s portion of the facilities. Utility Br. 11-12 & n.7. However, transmission capacity is no more subject to division than interconnection capacity and, in any event, in both cases modifications to a joint contract “affect” the non-jurisdictional co-party. Order No. 888-A at 30,219 (cited in Order No. 2003 P 807 & n.130, JA 184). The point is that an effect on a non-regulated party cannot preclude the

Commission from regulating a jurisdictional public utility and its contracts. Order No. 2003-A P 754 & n.176, JA 721 (citing Order No. 888 at 31,692).

Indeed, the authorities cited by Utility Petitioners illustrate this point. *Mid-Continent Area Power Pool*, 89 FERC ¶ 61,135 at 61,387 (1999), and *Bonneville Power Admin. v. FERC*, 422 F.3d 908, 922 (9<sup>th</sup> Cir. 2005), both found that the Commission lacked jurisdiction to impose tariff remedies on non-jurisdictional parties to joint agreements. Utility Br. 13. In both cases, however, it was also recognized that the Commission nevertheless had authority, in regulating jurisdictional parties to the joint agreement, to modify the joint contracts even though there were non-jurisdictional parties to them. In *MidContinent Area Power Pool*, the Commission had jurisdiction to modify a joint pool-wide open access transmission tariff and agreement, even though there were non-jurisdictional members of the pool. 89 FERC at 61,387-88. Following *MidContinent Area Power Pool*, subsequent breach of contract proceedings in federal court found a non-jurisdictional party to the pool tariff and contract bound by FERC's regulatory changes to the tariff and contract, even though FERC could not regulate the non-jurisdictional entity directly. *Alliant Energy v. Nebraska Public Power Dist.*, 347 F.3d 1046, 1050-51 (8<sup>th</sup> Cir. 2003). Citing *Alliant*, *Bonneville* recognized that a non-jurisdictional entity that enters into a contract subject to FERC regulation can

be liable to the other parties to the agreement for breaches of the agreement as modified by the Commission. *Bonneville*, 422 F.3d at 925.

Thus, FERC has authority to regulate the jurisdictional contract of a public utility, even though the regulation of that contract affects a non-jurisdictional co-party to the contract. *See, e.g., New York State Electric & Gas Corp. v. FERC*, 638 F.2d 388, 395 (2<sup>nd</sup> Cir. 1980) (Commission could order modification of public utility contract with non-jurisdictional entity where the order is directed to the public utility and precludes the public utility from enforcing certain provisions of the contract, notwithstanding that modification of the agreement will affect the non-jurisdictional contracting party).

Any other result would permit jurisdictional utilities to avoid regulation simply by partnering with non-jurisdictional utilities. Order No. 888-A at 30,219. Further, a non-jurisdictional entity contracts with a jurisdictional public utility with the explicit knowledge that the contract will be filed with the Commission and that the Commission can regulate the rates, terms and conditions of the contract with respect to the jurisdictional services provided thereunder by the public utility. *Id.* If and when the public utility unilaterally files either to amend or terminate the agreement, the non-jurisdictional party is free to raise any arguments it wishes to support its position that no changes are necessary to ensure that the contract is just and reasonable and not unduly discriminatory or preferential. *Id.* If the non-public

utility disagrees with a Commission determination, it is free to request rehearing, and, if aggrieved, to seek judicial review as appropriate. *Id.* at 30,288.

Utility Petitioners also contend that Order No. 2003 requires jurisdictional co-owners having tariff administration responsibility for jointly-owned facilities to bear an inequitable financial burden, as they must provide the generator transmission credits on behalf of the non-jurisdictional owners. Utility Br. 13. However, in Order No. 2003-C, the Commission clarified that operators of jointly owned systems are *not* required to reimburse Interconnection Customers for upfront payments for Network Upgrades received by the non-public utility owners of the system. Order No. 2003-C P 18, JA 982. Rather, the operator's responsibilities for flowing through credits and reimbursing the Interconnection Customer for its upfront payment do not extend beyond its normal duties as the tariff administrator. *Id.* Each jurisdictional owner of a jointly-owned system has the financial responsibility under its own Commission-regulated tariff to provide transmission credits and final reimbursement to the Interconnection Customer for the upfront payments that jurisdictional owner has received. *Id.* Thus, the public utility co-owner of a jointly-owned facility has no obligation to pay credits for Network Upgrades which were financed through upfront payments made to a non-public utility co-owner.

**C. The Commission Properly Asserted Jurisdiction Over Net Metering Sales When The Generator Is A Net Seller.**

Net metering allows a retail electric customer to produce and sell power onto the Transmission System without being subject to the Commission's jurisdiction. Order No. 2003-A P 744, JA 719. A participant in a net metering program must be a net consumer of electricity, but for portions of the day or portions of the billing cycle it may produce more electricity than it can use itself. *Id.* This electricity is sent back onto the Transmission System to be consumed by other end users. *Id.* Since the program participant is still a net consumer of electricity, it receives an electric bill at the end of the billing cycle that is reduced by the amount of energy that it sold back to the utility. *Id.* Essentially, the electric meter "runs backwards" during the portion of the billing cycle when the load produces more power than it needs, and runs normally when the load takes electricity off the system. *Id.*

In Order No. 2003-A, the Commission found that, in most circumstances, it would not exert jurisdiction over a net metering arrangement when the owner of a generator receives a credit against its retail power purchases from the selling utility. Order No. 2003-A P 747, JA 720 (citing *MidAmerican Energy Co.*, 94 FERC ¶ 61,340 at 62,263 (2001) (Commission would not assert jurisdiction when an individual home owner or farmer or similar entity installs generation and accounts for its dealings with the utility through netting)). Instead, the Commission would only assert jurisdiction when the Generating Facility produces

more energy than it needs and makes a net sale of energy to a utility over the applicable billing period. *Id.* (citing *MidAmerican*, 94 FERC at 62,263, holding that, if there is a net sale of energy to a utility, and the generator is not exempt from FERC regulation, the generator's owner must comply with the requirements of the FPA). In order for the Interconnection Procedures and Agreement to apply, the net metering customer at the time it requests interconnection has to both seek interconnection to a facility subject to a Commission-approved open access transmission tariff and intend to make net sales of energy to a utility. *Id.*

Governmental Petitioners contend that this holding is contrary to *MidAmerican*, which found that power flowing from a generator participating in a State-established net metering program to its interconnected electric utility does not constitute a wholesale sale subject to FERC jurisdiction. Governmental Br. 29. It is true that *MidAmerican* found no sale where the generator was a net purchaser of energy. 94 FERC at 62,263. However, *MidAmerican* also held that, if there is a net *sale* of energy to a utility, and the generator is not otherwise exempt, the generator's owner must comply with the requirements of the FPA. Order No. 2003-A P 747 n.174, JA 720 (citing *MidAmerican*, 94 FERC at 62,263). Thus, there is no inconsistency between *MidAmerican* and the approach taken in Order No. 2003.

**D. The Commission Properly Asserted Jurisdiction Over Qualifying Facility Power Transmitted In Interstate Commerce.**

The Commission's existing regulations govern utility interconnections with Qualifying Facilities, which are cogeneration or small power production facilities that are exempt from most FERC regulation.<sup>6</sup> Order No. 2003 P 813, JA 185-186 (citing 18 C.F.R. § 292.303, 292.306). When an electric utility is obligated to interconnect under § 292.303 of the Commission's regulations implementing PURPA (*i.e.*, when it purchases the Qualifying Facility's total output), the relevant state authority has jurisdiction over the interconnection and the allocation of interconnection costs. *Id.* P 813 n.136 (citing *Western Massachusetts Elec. Co.*, 61 FERC ¶ 61,182 at 61,661-62 (1992), *aff'd*, *Western Massachusetts Elec. Co. v. FERC*, 165 F.3d 922, 926 (D.C. Cir. 1999)). But when an electric utility interconnecting with a Qualifying Facility does not purchase all of the Qualifying Facility's output, and instead transmits the Qualifying Facility power in interstate commerce for another utility purchaser, the Commission exercises FPA jurisdiction over the rates, terms and conditions affecting or relating to such service, such as interconnections. *Id.* (citing *Western Massachusetts*, 61 FERC at 61,661-62).

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<sup>6</sup> Congress enacted section 210 of the Public Utility Regulatory Policies Act of 1978 ("PURPA"), 16 U.S.C. § 824a-3, to encourage the development of cogeneration and small power production facilities. *Southern California Edison*

Governmental Petitioners contend that this assertion of jurisdiction is contrary to *Western Massachusetts*, in which Governmental Petitioners claim that FERC delegated virtually all regulatory oversight over Qualifying Facility transactions to the states. Governmental Br. 30-31. As the Commission found, however, Order No. 2003 P 813, JA 185-186, *Western Massachusetts* fully supports the result reached here.

That case *rejected* arguments that states in general have regulatory authority over all interconnection agreements between electric utilities and Qualifying Facilities. *Western Massachusetts*, 61 FERC at 61,661. Rather, the scope of state authority with regard to interconnection costs is limited to purchases or sales of power between the local electric utility and the interconnected Qualifying Facility. *Id.* at 61,662 (citing 18 C.F.R. §§ 292.303, 292.306). State authority under PURPA does not extend to transactions involving utilities transmitting Qualifying Facility power in interstate commerce. *Id.* When a utility transmits Qualifying Facility power in interstate commerce to another utility, a FERC-jurisdictional transaction under the FPA takes place. In that unusual circumstance, the

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*Co. v. FERC*, 443 F.3d 94, 95 (D.C. Cir. 2006). As required by PURPA, to counter traditional electric utilities' reluctance to deal with these nontraditional facilities, the Commission requires electric utilities to purchase electric power from, sell power to, and interconnect with qualifying cogeneration and small power production facilities (collectively, "Qualifying Facilities"). *Id.* See 16 U.S.C. § 824a-3(a)(1)-(2).

transmission of Qualifying Facility power in interstate commerce and the agreement affecting or relating to such service (and the rates for such service) are subject to the Commission's exclusive FPA jurisdiction. *Id.* See also Order No. 2003 P 814, JA 186.

Governmental Petitioners complain that the Commission is asserting jurisdiction over a Qualifying Facility's interconnection if the Qualifying Facility's owner sells *any* of the Qualifying Facility's output to a third party. Governmental Br. 30. However, the Commission's exclusive jurisdiction over the charges assessed in conjunction with the provision of interstate transmission service necessitates the Commission's exercise of jurisdiction over the related interconnection costs. *Western Massachusetts*, 61 FERC at 61,662. Accordingly, the Commission rejected arguments that it should establish jurisdiction over Qualifying Facility interconnections based on the amount of energy sold to a third party. Order No. 2003 P 814, JA 186. The fact that the facilities used to support the jurisdictional service might also be used to provide various non-jurisdictional services does not vest state regulatory authorities with authority to regulate matters subject to the Commission's exclusive jurisdiction. Order No. 2003 P 813 n.137, JA 186 (citing *Western Massachusetts*, 61 FERC at 61,662).

Thus, where a utility plans to provide FERC-jurisdictional transmission service to supply Qualifying Facility power to a third party utility purchaser,

interconnection costs and agreements, in these unusual circumstances, become subject to the Commission's exclusive jurisdiction. *Western Massachusetts*, 61 FERC at 61,662.

**E. The Commission Did Not Exceed Its Jurisdiction Regarding Eminent Domain Authority.**

Article 5.13 of the Interconnection Agreement requires that, if any part of the Transmission Provider's Interconnection Facilities or Network Upgrades is to be installed on land owned by a third party, the Transmission Provider shall assist the Interconnection Customer in securing rights to use that land. Order No. 2003-A PP 293, 300, JA 644-645, 646. Specifically, the Transmission Provider is required to undertake efforts similar to those that it typically undertakes on its own behalf to site its own facilities, including any eminent domain authority the Transmission Provider has, consistent with state law. *Id.*

Utility Petitioners contend that the Commission lacks authority to compel a public utility to use its state-granted eminent domain authority, citing *Prinz v. United States*, 521 U.S. 898 (1997), and *New York v. United States*, 505 U.S. 144, 188 (1992). Utility Br. 14-15. *Prinz* and *New York* are inapposite as they concern federal action imposing mandatory action *on state officials* in carrying out a federal program. *See Prinz*, 521 U.S. at 904 (Congress commandeered state sheriffs to determine the lawfulness of gun sales); *New York*, 505 U.S. at 175-76 (Congress required states either to enact legislation regarding disposal of radioactive waste in

accord with Congressional direction or to implement an administrative solution).

Here, the Commission's orders require no action by the state or its officials.

Indeed, the Commission does not require utilities to exercise their eminent domain powers for Interconnection Customers unless the utilities exercise eminent domain on their own behalf and the exercise of eminent domain complies with state law. Interconnection Agreement Article 5.11, as originally proposed, required that Transmission Providers be required to use reasonable efforts, including eminent domain, to facilitate interconnection. Order No. 2003 P 384, JA 121. In response to concerns such as those express by Petitioners, the Commission modified that requirement in recognition that "a mandatory eminent domain requirement can be difficult for a Transmission Provider or Transmission Owner." *Id.* P 391, JA 122. In the Final Rule, Article 5.13 only required that a utility exercise its right of eminent domain *if* it similarly exercises eminent domain rights for the benefit of its own interconnections, *and* the exercise of eminent domain authority is consistent with state law. Order No. 2003 P 391, JA 122; Order No. 2003-A P 300, JA 646. A cornerstone of the Order No. 888 open access rulemaking -- the model for the later Order No. 2003 interconnection rulemaking -- was the same comparability requirement, that utilities take transmission service for themselves under the same terms and conditions as they offer that service to others. *See TAPS*, 225 F.3d at 682.

As Transmission Providers are not required to use their eminent domain authority at all unless they choose to use it to benefit themselves, Utility Petitioners err in contending that the condemnation requirement is an impermissible taking. Utility Br. at 15. *See, e.g., Bowles v. Willingham*, 321 U.S. 503, 517-18 (1944) (rent regulation ordinance was not an unconstitutional taking where landlords were free to keep their buildings vacant or sell them without being subject to government price regulation); *The Meriden Trust and Safe Deposit Co. v. FDIC*, 62 F.3d 449, 455 (2<sup>nd</sup> Cir. 1995) (no unconstitutional taking where statute did not subject bank to liability automatically but only if bank chose to continue on as a FDIC-insured institution).

Moreover, as Utility Petitioners concede, any condemnation of land is undertaken at the Interconnection Customer's expense. Utility Br. 15. Further, the Interconnection Agreement does not just provide that the landowner will be compensated, *see id.*, but that the Transmission Provider's "efforts" on the Interconnection Customer's behalf will be compensated. Interconnection Agreement Article 5.13; Order No. 2003-B P 89, JA 937-938. It is precisely because compliance with Article 5.13 may require participation in lengthy and contentious proceedings, *see* Utility Br. 15, that the Commission required the Interconnection Customer to pay for the Transmission Provider's efforts, unlike the permitting assistance under 5.14 where such payment is not required. *Id.* As this

Court has recognized, even if there were a “taking,” there is no inherent constitutional defect if just compensation is available. *TAPS*, 225 F.3d at 690.

### **III. ORDER NO. 2003’S REQUIREMENTS FOR PRICING AND FINANCING INTERCONNECTION FACILITIES ARE BASED ON REASONABLE POLICY CHOICES AND SHOULD BE SUSTAINED.**

#### **A. The Rule’s Pricing and Crediting Requirements**

In Order No. 2003, the Commission drew on its prior interconnection case law to allocate the responsibility between the Interconnection Customer and the Transmission Provider for the costs of interconnections. Under this precedent, the agency had identified two categories of facilities necessary for interconnection between a generator and transmission system: (1) Interconnection Facilities, “found between the Interconnection Customer’s Generating Facility and the Transmission Provider’s Transmission System,” which are designed solely to serve the interconnecting generator (Order No. 2003 P 21, JA 70); and (2) Network Upgrades, “facilities *at or beyond* the point where the Interconnection Customer’s Generating Facility interconnects to the Transmission Provider’s Transmission System,” which benefit not only the Interconnection Customer, but also all existing transmission customers on the Transmission Provider’s system. *Id.* & n.22 (emphasis added), JA 70 (citing *Entergy Gulf States, Inc.*, 98 FERC ¶ 61,014 at 61,023, *reh’g denied*, 99 FERC ¶ 61,095 (2002), and *Public Service Co. of*

*Colorado*, 59 FERC ¶ 61,311 (1992), *reh'g denied*, 62 FERC ¶ 61,013 at 61,061 (1993)).

In prior cases, the Commission had employed the “At or Beyond” policy to determine which facilities should be considered Network Upgrades (and thus paid for by all of the system’s transmission customers) and which should be considered Interconnection Facilities (the costs of which of which are assigned to the Interconnection Customer). On this question, Order No. 2003 relied on the Commission’s “well-established precedent” that no “case-specific determination” is needed to establish that “all users benefit from Network Upgrade[s];” rather, the Commission only looks to “whether the upgrade is *at or beyond* the Point of Interconnection.” Order No. 2003 P 66 & n.52, JA 78 (emphasis added) (citing *Entergy I; Southern Co. Services, Inc.*, 101 FERC ¶ 61,309 (2002); *American Electric Power Service Corp.*, 101 FERC ¶ 61,194 (2002); *Tampa Electric Co.*, 99 FERC ¶ 61,192 (2002)).

Order No. 2003 also referred to Commission case law to determine which party would be responsible for the costs of these two different types of facilities, *i.e.*, Interconnection Facilities and Network Upgrades:

Most improvements to the Transmission System, including Network Upgrades, benefit all transmission customers, but the determination of who benefits from such Network Upgrades is often made by a non-independent transmission provider, who is an interested party. In such cases the Commission has found that it is just and reasonable for the Interconnection Customer to pay for Interconnection Facilities but not

for Network Upgrades. Agreements between the Parties to classify Interconnection Facilities as Network Upgrades, or to otherwise directly assign the costs of Network Upgrades to the Interconnection Customer, have not been found to be just and reasonable and have been rejected by the Commission.

Order No. 2003 P 21 & n.24, JA 70 (citing *Illinois Power Co.*, 103 FERC ¶ 61,032 (2003); *American Electric Power Service Corp.*, 101 FERC ¶ 61,194 (2002)).

However, while Order No. 2003 required that Network Upgrades would be paid for by the Transmission Provider, it further provided that such upgrades “will be funded initially by the Interconnection Customer (unless the Transmission Provider elects to fund them),” with the Interconnection Customer “entitled to a cash equivalent refund (*i.e.* credit) equal to the total amount paid for Network Upgrades, including any tax gross-up or other tax-related payments.” *Id.* P 22, JA 71.

Thus, Order No. 2003 required that “the Interconnection Customer is entitled to a full refund of the payments it makes toward the cost of Network Upgrades within five years after the Commercial Operation Date” of the Generating Facility, as long as the Generating Facility remains in operation throughout the period. *Id.* P 720, JA 167.

These basic pricing principles remained consistent throughout the course of the rulemaking, although various details were clarified or adjusted. *See* Order No. 2003-A PP 7-11, JA 611-612; Order No. 2003-B PP 8-10, JA 921-922; Order No.

2003-C PP 1-2, JA 978. However, the time period for repayment became an issue of particular reexamination. The Commission reconsidered the five-year repayment provision in Order No. 2003-A, and substituted an open-ended period for reimbursement of credits. Order No. 2003-A P 616, JA 696-697. Finally, in Order No. 2003-B, the Commission once again instituted a payment deadline, revising the Large Generator Interconnection Agreement “to state that full reimbursement shall not extend beyond twenty (20) years from the Commercial Operation Date” of the Generating Facility. Order No. 2003-B P 35, JA 927.

Order No. 2003 further determined that independent Transmission Providers -- Regional Transmission Organizations and Independent System Operators that have no reason to discriminate against interconnecting generators -- would be authorized to allocate the costs of Network Upgrades using other, more flexible methods. Order No. 2003-A PP 48, 691-696, JA 615, 710-711.

Additionally, the Commission concluded that an Affected System, *i.e.*, a transmission system “other than that of the Transmission Provider that may be affected by the proposed interconnection,” would be governed by the same cost allocation rules as those applicable to Transmission Providers. Order No. 2003 P 736 & n.118, JA 170. Thus, a non-independent Affected System, like a non-independent Transmission Provider, would receive upfront financing from an Interconnection Customer for Network Upgrades required by the interconnection,

but also would be obligated to repay the funds to the Interconnection Customer by means of transmission credits, with any remaining balance at the end of 20 years payable in a lump sum. Order No. 2003-C, P 13, JA 981.

Petitioners' challenge to Order No. 2003's pricing policies focuses on two related but distinct issues. One is the method by which the Commission determines that a facility is an Interconnection Facility, which will be paid for solely by the Interconnection Customer (operating the Generating Facility), or a Network Upgrade, for which the Transmission Provider will pay over time. In Order No. 2003, adopting existing case law, the Commission made this determination by employing the At or Beyond test.

The second issue is the manner in which the costs of Network Upgrades should be assigned among the Transmission Providers' customers, *i.e.*, rolled into the transmission rate of all the Transmission Providers' customers, or assigned solely to the transmission rate payable by the Interconnection Customer. In Order No. 2003, the Commission answered this question by applying its long-standing principles for transmission pricing that Network Upgrades benefited *all* transmission customers on the integrated system, and that their costs should be allocated to all beneficiaries.

**B. The At Or Beyond Test For Determining Whether An Interconnection Facility Is A Network Facility Is Reasonable And Fully Consistent With Precedent.**

The Commission determined that for Transmission Providers that are not independent entities, it would generally “continue to apply its current interconnection pricing policy.” Order No. 2003 P 693, JA 160. Under that policy, the Commission explained, the Interconnection Customer would “be solely responsible for the costs of Interconnection Facilities, which are defined as all facilities and equipment between the Generating Facility and the Point of Interconnection with the Transmission System.” *Id.* P 676, JA 156. Network Upgrades, on the other hand, “which are defined as all facilities and equipment constructed *at or beyond* the Point of Interconnection for the purpose of accommodating the new Generating Facility,” would ultimately be the responsibility of the Transmission Provider. *Id.* (emphasis added) JA 157. *See also* Order No. 2003-A PP 584-585, JA 689-690.

Petitioners attack the At or Beyond test for determining the status of facilities as arbitrarily departing from Commission precedent. Governmental Br. 31; Utility Br. 16-17. For example, Utility Petitioners maintain that “prior policy authorizing . . . direct assignment” to the Interconnection Customer of the costs of Generating Facilities located “at the Interconnection point” had been in place “at least [since] *Pennsylvania Electric Co.*, 60 FERC ¶ 61,034 at 61,129 (1992).” Utility Br. 16.

In this regard, both petitioner groups rely on this Court’s decision in *Entergy Services, Inc. v. FERC*, 391 F.3d 1240 (D.C. Cir. 2004) (*Entergy II*), as recognizing that the Commission’s policy of allocating the cost of facilities at or beyond the interconnection point to all transmission customers was an unexplained departure from FERC’s former policy of requiring direct cost assignment of facilities at the interconnection point. Governmental Br. 31-32; Utility Br. 16. As we now demonstrate, Petitioners’ contention is without merit.

In *Entergy II*, decided subsequent to the issuance of Order No. 2003, this Court made plain that it had no objection to the Commission employing a purely locational test for determining whether a particular facility was a Network Upgrade or an Interconnection Facility. Indeed, the Court explained that the agency had “set forth an overarching defense of at least a ‘From’ test” (*i.e.* assignment to transmission customers of the costs of all new facilities *from* the point where the generator connects to the grid). 391 F.3d at 1249. Reviewing the Commission case law on the matter, the Court observed that:

recounting the Commission’s development of a “From” test, tracing its transformation into an “At or Beyond” test, and keeping in mind the Commission’s subsequent assertions that the two tests are one and the same, we are left with the conclusion that the “At or Beyond” test represents an apparent departure from [the] “From” test. That departure may be slight, but it is a departure nonetheless.

391 F.3d at 1251.

Thus, the Court remanded the case for further explanation, whether it be a clarification establishing that the Court had “misread the Commission’s apparent direct assignment of costs occurring precisely at the point of interconnection,” or, alternatively, an explanation of “why it has departed from that policy.” *Id.* The Court emphasized that it was not mandating the manner in which the Commission should assign the costs at issue, as “the same substantial evidence appears to support either test.” *Id.*

On remand, the Commission issued orders explaining “why it is reasonable to treat facilities ‘at’ the point of interconnection as network facilities.” *Nevada Power Co.*, 111 FERC ¶ 61,161 P 12, *reh’g denied*, 113 FERC ¶ 61,007 (2005), *appeal pending sub nom. Entergy Services, Inc. v. FERC, et al.*, D.C. Cir. Nos. 05-1238, *et al.* The Commission explained:

The point of interconnection is typically an electrical substation or a tap point into an existing transmission line. Rarely is the point of interconnection located at the generating facility itself; in virtually all cases, interconnection facilities (*e.g.*, a radial line, poles, supports, switches, meters) must be constructed to provide an electrical connection between the generating facility and the transmission system at the point of interconnection. Thus, when we refer to “interconnection facilities,” we are not referring to facilities “at” the point of interconnection. Rather, “interconnection facilities” refer to all facilities and equipment from the generating facility up to (but not including) the point of interconnection.

*Nevada Power Co.*, 111 FERC ¶ 61,161 P 13.

The Commission further explained that while it had “first articulated the locational test for determining whether a facility is a network facility,” it had used “the vague term ‘from’ the point of interconnection instead of the more precise ‘at or beyond’ the point of interconnection.” *Id.* P 15. In the Commission’s view, its “adoption of clearer terminology was not a change in policy.” *Id.* & n.31, citing *Entergy Gulf States*, 99 FERC ¶ 61,095 at 61,399-400. Thus, it had not allowed direct assignment of facilities which were located at the point of interconnection in the cases discussed by the Court. Rather, its view (as in Order No. 2003) had consistently been that “[t]he network begins at the point where the interconnection facilities connect to the transmission system, not somewhere beyond that point.” *Id.* at P 16 (footnote omitted). *See* Order No. 2003 P 21, JA 70.

In sum, the use of the At or Beyond policy in Order No. 2003 for determining whether facilities would be considered Interconnection Facilities or Network Upgrades on the Transmission System was fully consistent with the relevant agency case law before and since. As the Court in *Entergy I* indicated, “an agency’s interpretation of its own precedent is entitled to deference by the court.” 319 F.3d at 541 (citing *Cassell v. FCC*, 154 F.3d 478, 483 (D.C. Cir. 1998)). Thus, Petitioners’ claim that the At or Beyond rule represents an unexplained departure from precedent should be rejected.

**C. Order No. 2003's Assignment of the Costs of Network Upgrades To The Transmission Provider Is Reasonable.**

**1. The Commission's Decision Is Consistent With Longstanding Cost Causation Principles.**

In Order No. 2003, to determine the appropriate cost allocation method for interconnection facilities, the Commission applied its long-established ratemaking principles that, as a general rule, the cost of Network Upgrades on a Transmission Provider's system, which benefit the entire system even though they are necessitated by the interconnection with a Generating Facility, would be assigned to the Transmission Provider, to be collected in its transmission rates. Order No. 2003 PP 675-678, JA 156-157; Order No. 2003-A PP 601-602, JA 693-694.

Petitioners assert that Order No. 2003's assignment of Network Upgrade costs to Transmission Providers violates the basic principle of cost causation that costs should be allocated only "to those who cause the costs to be incurred and receive the benefits from them (*i.e.*, Interconnection Customers)." Governmental Br. 34 (footnote omitted); *see also* Utility Br. 17-18.

However, the Commission's decision that Network Upgrades should be recovered in the rates of the Transmission Provider is grounded in its determination -- affirmed by this Court -- that, in an integrated transmission system, network facilities benefit all customers on the system and cannot be

assigned to a particular customer. As the Commission previously explained in *Public Service Co. of Colorado*, which was cited by Order No. 2003:

The Commission has long held that an integrated transmission grid is a cohesive network moving energy in bulk. Because the grid operates as a single piece of equipment, the Commission has consistently priced transmission service based on the cost of the grid as a whole.

62 FERC at 61,061 (footnote omitted); *see also* Order No. 2003 P 21 n.22, JA 70.

Therefore, the Commission has reasoned, the cost of facilities that are part of the transmission system (*i.e.*, network facilities, such as the Network Upgrades here), can be rolled in to a utility's transmission rate and thus spread among all transmission customers on the network:

The Commission has rejected the direct cost assignment of grid facilities even if the grid facilities would not be installed but for a particular customer's service. The Commission has reasoned that, even if a customer can be said to have caused the addition of the grid facility, the addition represents a *system* expansion used by and benefiting *all* users due to the integrated nature of the grid. Recognizing that the grid is a cohesive network in a dynamic state of development, the Commission has even included remote facilities in the grid on the ground that they were merely the first segment of what would eventually become a network loop. The Commission has reserved direct assignments for only those transmission facilities which fall into what we have referred to as an "exceptional category" consisting of radials that are so isolated from the grid that they are and will remain non-integrated.

\* \* \*

There continues to be only one service B service over the entire grid B and both native load and third party customers "use" the *entire* grid, including any expansion. Similarly, both native load and third party customers benefit from integrated system upgrades.

*Id.* (footnotes omitted) (emphasis in original).

This concept has been specifically endorsed by this Court. In *Western Massachusetts Electric Co. v. FERC*, 165 F.3d 922, 927 (D.C. Cir. 1999), the Court referred to the Commission's

consistent policy to assign the costs of system-wide benefits to all customers on an integrated transmission grid. We have approved the underlying rationale of this policy. When a system is integrated, any system enhancements are presumed to benefit the entire system.

(citations omitted) (affirming the Commission's determination of the allocation of interconnection costs). *See also Midwest ISO Transmission Owners v. FERC*, 373 F.3d 1361, 1369-70 (D.C. Cir. 2004) (affirming spreading of administrative costs of independent transmission system operator among all users of the system); *Entergy I*, 319 F.3d at 543-544.

Petitioners further maintain that the Commission's assumption that Network Upgrades necessarily will benefit all customers on an integrated transmission system, so that the Network Upgrade costs accordingly should be assigned to the Transmission Provider, is contradicted by specific evidence in the record, namely, the affidavit of an electrical engineer named James M. Howell, Jr. *See* Governmental Br. 34-36; Utility Br. 17-18. According to Mr. Howell, "the construction of new facilities in order to interconnect a new generator often results in decreasing system reliability," as it "increases the probability of equipment failure by adding numerous station components." Howell Affidavit ¶ 9, JA 862.

Petitioners thus rely on Mr. Howell’s affidavit to demonstrate that “FERC erred in holding, contrary to the record evidence, that all networked transmission facilities provide a system benefit.” Utility Br. 17, citing Order No. 2003 P 65, JA 77. *See also* Governmental Br. 34.

The Court should reject this argument. As discussed above, this issue is already settled: the Court has previously endorsed the Commission’s finding -- adopted prior to Order No. 2003, applied by Order No. 2003, and currently applied by the Commission -- that Network Upgrades benefit the entire transmission system, so that their cost can be assigned to transmission customers. *See Entergy I*, 319 F.3d at 543-44; *Western Massachusetts Electric Co.*, 165 F.3d at 927.

## **2. The Commission’s Pricing Decision Is Consistent With the Agency’s Statutory Authority**

Petitioners also advance a theory that Order No. 2003’s pricing regime violates the Energy Policy Act of 1992, Pub. L. No. 102-486 (EPAAct). *See* Governmental Br. 32-34; Utility Br. 19-21. Thus, Government Petitioners argue that “EPAAct prohibits the spreading of costs of facilities required to provide interconnection service to other transmission customers, including retail customers.” Governmental Br. 32 (footnote omitted) (citing FPA section 212 (EPAAct section 722), 16 U.S.C. § 824k(a)). Utility Petitioners similarly maintain that both EPAAct’s “legislative history and FERC’s own Transmission Pricing

Policy<sup>7</sup>]” establish that EAct’s policy to avoid native load customers subsidizing transmission systems “is to be applied under [FPA] Sections 205 and 206.” Utility Br. 20.

As the Commission explained in some detail in Order No. 2003-A, however, Petitioners’ EAct argument is baseless. First, while section 212 of the FPA “applies only to Transmission Service ordered under section 211” of the statute, Order No. 2003 was promulgated by the Commission under FPA sections 205 and 206, pursuant to its mandate under these sections to identify and remedy unduly discriminatory or preferential practices in the provision of transmission service. Order No. 2003-A P 596, JA 692. *See also* Order No. 2003 P 20, JA 70.

Second, contrary to the Utility Petitioners’ claim here, “[t]he Commission’s Transmission Pricing Policy Statement does not state that Section 212 applies to service under Sections 205 or 206 or that the two provisions are identical.” Order No. 2003-A P 596, JA 692. Rather, the Commission indicated that under *any* of these statutory provisions, “we do not believe that third-party transmission customers should subsidize existing customers.” Transmission Pricing Policy Statement at 31,143-44. However, there is no such improper subsidization when

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<sup>7</sup> *Inquiry Concerning the Commission’s Pricing Policy for Transmission Services Provided by Public Utilities Under the FPA; Policy Statement, 1991-96 FERC Stats. & Regs., Regs. Preambles ¶ 31,005 (1994).*

existing transmission customers that benefit from the construction of Network Upgrades pay the costs associated with that construction. *See* Order No. 2003-A PP 579-581, JA 688-689. *See also Entergy I*, 319 F.3d at 544-45 (noting that “the Commission has long rejected the argument that transmission credits for network upgrades result in ‘cross-subsidization’ by native load customers as based on the faulty premise that native load customers receive no benefit from the upgrades”).

Finally, the Commission noted that “even if section 212 did apply to this rulemaking,” it would not forbid “rolled-in pricing of an upgrade to the transmission grid simply because the immediate impetus for that upgrade is the interconnection of a new Generating Facility.” Order No. 2003-A P 598, JA 692-693. In this regard, the agency observed, FPA section 212 requires the Commission to ensure, “to the extent practicable,” that the “costs incurred in providing the wholesale transmission services, *and properly allocable to the provision of such services*, are recovered” from the interconnection customer “and not from a transmitting utility’s existing wholesale, retail, and transmission customers.” *Id.* P 598, quoting FPA section 212 (emphasis the Commission’s). As the Commission explained, “we do not believe that the costs of Network Upgrades required to interconnect a Generating Facility to the Transmission System of a non-independent Transmission Provider are *properly allocable* to the Interconnection Customer through direct assignment,” as the upgrades benefit all

transmission customers. *Id.* P 599, JA 693 (emphasis in original). *See also id.* P 600 & n.118 (noting that there was “ample evidence” in EPA’s legislative history “that Congress carefully decided not to either endorse or reverse the Commission’s transmission pricing policies,” contrary to the wishes of several representatives).

**3. Order No. 2003 Does Not Cause Native Load Customers To Subsidize Interconnection Customers.**

Contrary to Petitioners’ claim (*see* Utility Br. 18-21), native load customers of Transmission Providers (*i.e.*, the customers on behalf of whom the Transmission Provider has undertaken to construct and operate the system) will simply not subsidize Generating Facilities because of Order No. 2003’s requirement that Network Upgrades be paid by all transmission customers. As the Commission explained:

[U]nder our interconnection pricing policy, the Transmission Provider continues to have the option to charge a transmission rate that is the higher of the incremental cost rate for network upgrades required to interconnect its generating facility or an embedded cost rate for the entire transmission system (including the cost of the Network Upgrades) . . . . Allowing the transmission providers to charge the higher of an incremental cost rate or an embedded cost rate ensures that other transmission customers, including the Transmission Provider’s native load, will not subsidize Network Upgrades required to interconnect merchant generation.

Order No. 2003-A P 580, JA 688 (footnote omitted).

“[I]n most instances,” the Commission indicated, “the additional usage of the transmission system by a new Interconnection Customer will generally cause the average embedded cost transmission rate to decline for all remaining customers,” so that rolled-in pricing will not only prevent native load customers from subsidizing a newly-interconnected Generating Facility, but may well decrease their bills. *Id.* P 581, JA 689. It bears emphasis that the logic employed by the Commission here is well-grounded in Commission precedent, and has been approved by this Court. *See Pennsylvania Electric Co.*, 58 FERC ¶ 61,278, *reh’g denied*, 60 FERC ¶ 61,034, *reh’g denied*, 60 FERC ¶ 61,244 (1992), *aff’d*, *Pennsylvania Electric Co. v. FERC*, 11 F.3d 207 (D.C. Cir. 1993) (cited in Order No. 2003-A, P 580, n.106, JA 688).

Furthermore, the Commission observed, in the event a Transmission Provider were to charge an incremental transmission rate for interconnection-related Network Upgrades, there is no question of a subsidy by native load customers. In that case, the agency explained

[t]he issue of whether crediting results in native load or other Transmission Customers ultimately bearing the cost of the Network Upgrades becomes somewhat irrelevant. This is because the incremental rate approach ensures that the costs associated with those Network Upgrades will not be included in the transmission rates charged to other customers.

Order No. 2003-A P 581 n.107, JA 689.

Utility Petitioners take issue with this conclusion. They rely once again on the affidavit of Mr. Howell, who argued that an incremental rate could not be developed for an Interconnection Customer because the Transmission Provider may not know if the customer “will take delivery service and, if so, what the capacity and duration of that service would be.” Utility Br. 21, quoting Howell Affidavit ¶ 4, JA 859.

Mr. Howell’s concerns are entirely speculative. The Commission has indicated that Interconnection Customers may be expected to request Interconnection Service and transmission delivery service at the same time. *See* Order No. 2003-A P 535, JA 680-681. In any event, should transmission delivery details necessary to establish an incremental rate be lacking, the Commission has made plain its willingness to consider other reasonable pricing proposals. As the Commission explained:

An important objective of our interconnection pricing policy continues to be the protection of existing Transmission Customers, including the Transmission Provider’s native load, from adverse rate implications associated with Interconnection Facilities and Network Upgrades required to interconnect a new Generating Facility. Despite the unsupported hypothetical generalizations of some petitioners, we have not been presented with any evidence that native load and other Transmission Customers cannot be held harmless under our existing pricing policy. If a Transmission Provider (or an existing Transmission Customer) believes that, for an actual interconnection, it faces circumstances where native load and other customers are not held harmless, it should make that demonstration in an actual transmission rate filing.

Order No. 2003-B P 56, JA 931. The Commission went on to observe that while it could not “envision any circumstances where our existing pricing policy will not fully protect native load and other Transmission Customers,” it would be “willing to consider alternative pricing proposals under the facts of a specific case.” *Id.*; *see also id.* at P 57, JA 932 (noting that the agency was not “prescribing generic rules at this time” as to the calculation of incremental rates).

#### **4. Order No. 2003 Encourages Efficient Generator Siting.**

Finally, Utility Petitioners assert that the Order No. 2003’s rule with respect to cost assignment will cause inefficiencies in generator siting. Utility Br. 22. In this regard, the Utility Petitioners emphasize the Commission’s acknowledgment that payment of credits by the Transmission Provider for transmission facilities necessary for interconnection “mutes somewhat the [Generator’s] incentive to make an efficient siting decision.” Utility Br. 23 (quoting Order No. 2003 P 695, JA 161). This concession, Petitioners claim, contradicts later assurances by the Commission that the requirement for the Interconnection Customer to make “up front funding to finance the cost of the Interconnection Facilities . . . will provide the Interconnection Customer with a strong incentive to make efficient siting decisions.” Order No. 2003-A P 627, JA 699.

The Commission’s reasoning, however, is sound. While there may be some inherent tension in the rule’s requirements arising from the Commission’s need to balance the interests of the two respective parties (Interconnection Customers and Transmission Providers), the fact remains that Interconnection Customers will have to expend a substantial amount of money in order to set up an interconnection with a Transmission Provider, both to pay for the Interconnection Facilities and to initially fund the Network Upgrades. While the latter are ultimately recovered through the transmission rates of the Transmission Provider, the Interconnection Customer nonetheless will be paying for them upfront, and receiving refunds in the form of transmission credits for up to a 20-year period. In this situation, it is clear the Generating Facility has a strong interest in selecting a site that is economically efficient. *See* Order No. 2003-B P 33, JA 927 (Commission’s interconnection pricing policy “promote[s] efficient investment decisions” and “provides a reasonable balance between the objectives of promoting competition and infrastructure development, protecting the interests of Interconnection Customers, and protecting native load and other Transmission Customers”).<sup>8</sup>

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<sup>8</sup> In this context, the Commission also observed “that a number of the factors that influence siting decisions are beyond the control of both the Interconnection Customer and the Commission,” but are under the control of state authorities. Order No. 2003-A P 627, JA 699. Thus, the agency’s pricing policy will only play a limited role in the selection of interconnection sites by merchant generators.

**D. Order No. 2003 Reasonably Distinguished Between Independent Transmission Providers, Such As Regional Transmission Organizations, and Those That Are Not Independent.**

In Order No. 2003, the Commission held that its general policy for the pricing of Network Upgrades would not necessarily apply to independent Transmission Providers. Order No. 2003 PP 28, 698, JA 72, 162. Instead, for such entities as Regional Transmission Organizations or Independent System Operators, “the Commission continues to allow flexibility regarding the interconnection pricing policy that each independent entity chooses to adopt, subject to Commission approval.” *Id.* P 698, JA 162. *See, e.g., Public Util. Dist. No. 1 of Snohomish County v. FERC*, 272 F.3d 607, 610-12 (D.C. Cir. 2001) (explaining development of FERC initiatives promoting the development of independent transmission providers, including Regional Transmission Organizations).

Thus, independent Transmission Providers would have the option of “participant funding” of Network Upgrades, *i.e.*, direct assignment of the cost of Network Upgrades to the Interconnection Customer, while non-independent Transmission Providers generally would be limited to the crediting approach (discussed above).<sup>9</sup> Independent Transmission Providers have no competitive

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<sup>9</sup> The Commission indicated, however, that by permitting an Independent Transmission Provider to assign “the cost of certain Network Upgrades” to the Interconnection Customer, it was not “abandoning the goals [it] has established for

interest in frustrating rival generators, the Commission reasoned, unlike non-independent Transmission Providers that own competing generating facilities. Permitting the latter to subjectively decide the network facilities for which the Interconnection Customer alone would pay “creates opportunities for undue discrimination.” Order No. 2003 P 696, JA 161. Specifically, the Commission explained:

[A] Transmission Provider that is not an independent entity has the ability and the incentive to exploit this subjectivity to its own advantage. For example, such a Transmission Provider has an incentive to find that a disproportionate share of the costs of expansions needed to serve its own power customers is attributable to competing Interconnection Customers. The Commission would find any policy that creates opportunities for such discriminatory behavior to be unacceptable.

*Id.* (JA 162) On the other hand, if an independent Transmission Provider – such as a Regional Transmission Organization – is performing transmission planning and cost allocation, no such danger of discrimination arises.

Petitioners attack the Commission’s differing pricing policies for independent and non-independent Transmission Providers as violating the FPA’s stricture against undue discrimination. Governmental Br. 40-44; Utility Br. 24-25.

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interconnection pricing.” Order No. 2003 P 700, JA 162. For example, even if the cost of certain Network Upgrades might be assigned to the Interconnection Customer, it would not amount to forbidden “and” pricing (*i.e.*, the customer paying both an incremental and rolled-in rate), “if, for example, the Interconnection Customer is allowed to receive well-defined capacity rights that are created by the upgrades.” *Id.*

As Utility Petitioners put it, the regulation “treats similarly-situated customers in an incomparable manner by requiring customers of non-[independent] Utilities to bear substantially all of the costs of Generator Interconnection, while customers of ‘independent’ utilities share such costs with Generators.” Utility Br. 24. In support, Petitioners rely on court decisions “that agency policies must be non-discriminatory and not treat similarly situated entities in a disparate manner.” Government Br. 40, citing *Town of Norwood v. FERC*, 202 F.3d 392, 402 (1<sup>st</sup> Cir. 2000), and *City of Frankfort v. FERC*, 678 F.2d 699, 707 (7<sup>th</sup> Cir. 1982); *see also* Utility Br. 24.

However, the very cases relied on by Petitioners refute their argument. As the court observed in *Town of Norwood*, with respect to the statutory discrimination standard, “differential treatment does not necessarily amount to *undue* preference where the difference in treatment can be explained by some factor deemed acceptable by the regulators (and the courts).” *Town of Norwood*, 202 F.3d at 402 (emphasis the court’s) (citing *Cities of Newark v. FERC*, 763 F.2d 533, 546 (3rd Cir. 1985), and *City of Frankfort*, 678 F.2d at 706 (“differences in facts” be they “cost of service or otherwise” may justify a “rate disparity”)). *See generally* *Cities of Bethany v. FERC*, 727 F.2d 1131, 1139 (D.C. Cir. 1984).

Here, the factual differences relied on by the Commission are obvious and rational. A non-independent Transmission Provider that is in competition with

interconnecting Generator Facilities has motive and opportunity to unfairly shift costs of Network Upgrades to its competitors, while an independent Transmission Provider operates only out of concern that costs to all customers are allocated equitably. *See* Order No. 2003 P 696, JA 161-162. While Petitioners reject this reasoning by the agency as mere conjecture and theory (Governmental Br. 41; Utility Br. 25), it is, in fact, a cornerstone of Order No. 2003. One of the “important functions” served by standard interconnection procedures for Large Generators, the Commission has recognized, is to “limit opportunities for Transmission Providers to favor their own generation.” Order No. 2003 P 12, JA 68. Furthermore, this is a significant part of the same reasoning upon which the Commission established non-discriminatory open-access transmission service in its Order No. 888 rulemaking, which was upheld by both this Court and the Supreme Court. *See supra* page 5.

Finally, Petitioners assert that potential discrimination by interested Transmission Providers can be addressed by the Commission by its review of individual Interconnection Agreements. Governmental Br. 40-41; Utility Br. 26. It is, of course, correct that the Commission can address specific pricing issues and proposals in specific cases. *See* Order No. 2003-B P 56, JA 931-932. However, the fact that a federal agency may enforce its regulatory authority in individual cases does not deprive it of the right to make rules of general applicability. *See*

*Public Utility District No. 1 of Snohomish County*, 272 F.3d at 620. This is especially true where, as here, these rules are designed to hold all transmission customers harmless and to keep all utilities and market participants free of undue discrimination.

**E. The Requirement In Order No. 2003 That A Generating Facility Providing Upfront Financing Must Be Reimbursed In Full By The End of 20 Years Is Reasonably Related To The Rule’s Regulatory Goal.**

Petitioners argue that Order No. 2003’s requirement that Interconnection Customers must be fully reimbursed (through credits) within 20 years, for the costs of Network Upgrades, *see* Order No. 2003-B P35, JA 927, is arbitrary and capricious. They prefer the result reached in Order No. 2003-A, where “the Commission properly reasoned that removing a date certain would ensure that the risk associated with the Network Upgrades would be borne by the Interconnection Customer.” Governmental Br. 38; *see also* Utility Br. 26.

Petitioners’ contentions concerning the 20-year repayment period are without merit. The Commission offered the following rationale for choosing the 20-year period:

Although the appropriate length of the repayment period for such a load is not a number that can be determined with great precision, we note that 20 years reflects the approximate minimum life of facilities that typically constitute Network Upgrades that generally would be needed to accommodate an Interconnection Customer’s generator interconnection.

Order No. 2003-C, P 9 n.9, JA 980. As the Commission further indicated, this Court has recognized the occasional need for a federal agency to “adopt a value within a range, as long as the chosen value is related to the problem being addressed.” *Id.* (citing *ExxonMobil Gas Marketing Co.*, 297 F.3d at 1085; *Prometheus Radio Project v. FCC*, 373 F.3d 372, 410 (D.C. Cir. 2004); *Sinclair Broad. Group, Inc. v. FCC*, 284 F.3d 148, 159 (D.C. Cir. 2002)).

Thus, contrary to the claims of Petitioners, the Commission adequately explained its rationale for departing from Order No. 2003-A’s elimination of a date certain for repayment. As the Commission observed, its previous “removal of a date certain for the repayment of Network Upgrade costs was inconsistent with the notion that the upfront payment is, in essence, a loan to the Transmission Provider designed to facilitate construction of Network Upgrades.” Order No. 2000-B P 36, JA 927. It is hardly unreasonable for a financing agreement to include a repayment deadline.

Nor is the Commission’s requirement of a balloon payment, if necessary, at the end of 20 years, unreasonable. As the Commission explained:

Any Interconnection Customer whose Generating Facility is used as intended . . . normally will be required to take Firm Point-to-Point Transmission Service or Network Integration Transmission Service and therefore will have ample opportunity to use its transmission credits to obtain reimbursement of its upfront payment.

Order No. 2003-B P 37, JA 928. However, a rule of general application, such as Order No. 2003, must account for the extreme as well as the typical situation. Thus, the agency had to take into account the probably rare occasion when cost recovery would not occur in 20 years or less. Moreover, that a Generating Facility failed to recover sufficient transmission credits within a 20 year period does not necessarily mean that the Network Upgrades required for its interconnection were of no benefit to the Transmission Provider's system and customers.

**F. The Commission's Requirement That Interest Be Paid On Credits Is Reasonable.**

Governmental Petitioners object to Order No. 2003's requirement, *see* Order No. 2003-A P 618, JA 697, that Transmission Providers pay interest on the funds loaned to them by the Interconnection Customer to build Network Upgrades.

Governmental Br. 36. Because the Interconnection Customer alone controls when transmission credits are paid, Governmental Petitioners reason, they could game the system for maximum interest profitability, to the detriment of Transmission Providers.

Governmental Petitioners' argument is specious. Generating Facilities will be receiving credits based on their use of the Transmission Provider's system, which in turn will depend on their ability to attract customers in the marketplace. This can hardly be described as a process that they "alone control." In any event, as the Commission indicated, "if the Transmission Provider believes it can obtain

financing for the Network Upgrades at a more favorable rate, it always has the option to finance Network Upgrades itself and immediately include the associated costs in rates.” Order No. 2003-A P 618, JA 697.

#### **IV. PETITIONERS’ REMAINING CONTENTIONS ARE WITHOUT MERIT.**

##### **A. The Commission Adequately Explained The Operation Of Network Resource Interconnection Service.**

In Order No. 2003, the Commission established two different levels of interconnection service to be offered by the Transmission Provider to the Interconnection Customer. The first, Energy Resource Interconnection Service, allows the Generating Facility to connect to the transmission system and makes it eligible to deliver its output using the existing firm or non-firm capacity of the Transmission System on an “as available” basis. Order No. 2003 P 753, JA 173. No objections to this type of service have been raised on appeal.

The second, Network Resource Interconnection Service, is the subject of Governmental Petitioners’ objections (Br. 45-48). This type of service is more comprehensive and requires the Transmission Provider to do what is necessary in the way of Interconnection Studies and Network Upgrades in order “to integrate the Generating Facility” into the Transmission Provider’s transmission system “in a manner comparable to that in which the Transmission Provider integrates its own generators to serve native load customers.” Order No. 2003 P 754, JA 173.

Thus, an Interconnection Customer receiving this superior service would be in a position to obtain Network Integration Transmission Service, which is firm transmission delivery service offered under a Transmission Provider's open access transmission tariff. *Id.* P 756; JA 174. In other words, "once the Interconnection Customer has obtained Network Resource Interconnection Service, requests for Network Integration Transmission Service from the Generating Facility to points inside the Transmission Provider's Transmission System will not require additional Interconnection Studies or additional upgrades." Order No. 2003-A P 501, JA 672.

The Commission emphasized that Network Resource Interconnection Service differs from the transmission delivery services required by Order No. 888 to be offered by a Transmission Provider under the open access transmission tariff. While both types of service "include a capability to move power onto the system," actual delivery service is provided to transmission customers only by the open access transmission tariff's Network Integration Transmission Service or Point to Point Transmission Service, both of which "specify one or more Points of Delivery on the Transmission System at which the injected output will be withdrawn." Order No. 2003-A P 516, JA 675.

Put in more imprecise but simpler terms, Network Resource Interconnection Service gets the Interconnection Customer into the Transmission Provider's system, but does not get the Interconnection Customer to its own customers.

However, to cross the remaining part of the transmission system and deliver energy to customers, the Interconnection Customer must still also obtain transmission delivery service.

Governmental petitioners make what appears to be a broad-based attack on Order No. 2003's requirement that Transmission Providers offer Network Resource Interconnection Service, with a heading of their brief trumpeting violations of "EPAct" and "Commission Precedent." Governmental Br. 45. However, the text of the section advances two significantly more circumscribed contentions, neither of which is meritorious.

First, Governmental Petitioners argue that Network Resource Interconnection Service violates cost causation principles by "requir[ing] all users of the transmission system, which are primarily native load customers," to bear the cost of Network Upgrades as if the Interconnection Customer "were serving native load." *Id.* at 47. But this is just a rehash of their attacks on Order No. 2003's pricing policies, which we have already addressed in section III, *supra*.

Second, Governmental Petitioners contend that Network Resource Interconnection Service is inherently flawed and internally inconsistent. In this regard, they point out that while the Commission has opined that Network Resource Interconnection Service "does not convey 'a reservation of transmission capacity or the right to begin taking firm or non-firm service,'" Governmental Br.

48 & n.102 (quoting Order No. 2003 P 778, JA 178), the rule nonetheless allows an Interconnection Customer taking this service “to qualify as a designated Network Resource on the Transmission Provider’s system without additional Network Upgrades.” *Id.* at 48 & n.103 (quoting Order No. 2003 at P 768, JA 176). Governmental Petitioners object that this would “appear[] to require a transmission reservation” on the part of the Interconnection Customer, because that would be the only way “to ensure that additional Network Upgrades would not be needed.” *Id.* at 48.

But as the Commission explained in some detail (Order No. 2003-A PP 516-518, JA 675-679), the two different types of transmission services (Order No. 2003’s interconnection services and the previously-established delivery services offered by Transmission Providers under their open access transmission tariffs) fit together harmoniously. An Interconnection Customer availing itself of Network Interconnection Transmission Service, in order to get it well into the Transmission Provider’s system, can also be expected to take Network Integration Transmission Service, to be able to deliver to its customers the power it generates and injects into the system and will, therefore, make a transmission reservation as part of this service. *See* Order No. 2003-A P 535, JA 680-681.

Furthermore, the Commission established that once an Interconnection Customer has designated its delivery points, “the Transmission Provider may charge a delivery service reservation fee.” Order No. 2003-A P 517, JA 676.

In sum, the alleged contradiction of which Governmental Petitioners complain does not in reality exist.

**B. The Commission Properly Applied The Reciprocity Requirement.**

Under Order No. 2003, the responsibility of paying Transmission Credits to an Interconnection Customer does not extend to a non-public utility transmission owner or operator. Order No. 2003-C P 18, JA 982 (citing Order No. 2003 P 843, JA 191) (non-public utilities are not required to provide transmission credits for Network Upgrade costs in order to satisfy the Commission’s reciprocity condition). A non-jurisdictional entity subject to the reciprocity requirement need not adhere to the crediting policy for Transmission Providers in Order No. 2003, including the payment of interest, unless it applies the same crediting policy to its own generation. *Id.* P 48, JA 987. Order No. 2003-A clarified that for rate matters, the reciprocity condition only requires comparability. *Id.* (citing Order No. 2003-A P 777, JA 724).

Utility Petitioners contend that exempting non-jurisdictional entities from the Transmission Credit requirement is an arbitrary and capricious departure from Order No. 888’s pre-existing reciprocity requirement. Utility Br. 27-28. The

Order No. 888 reciprocity policy permits a non-public utility to gain access to a public utility's Transmission System under the public utility's open access transmission tariff so long as the non-public utility seeking the access agrees to offer comparable (not unduly discriminatory) service in return. Order No. 2003-A P 771, JA 724 (citing Order No. 888-A at 30,285).

Order No. 2003 in no way altered the reciprocity policy articulated in Order No. 888 and reflected in the open access transmission tariff. Order No. 2003 P 840, JA 190. Contrary to Utility Petitioners' contentions, *see* Utility Br. 27-28, comparability does not require that the rates, terms and conditions of the reciprocal non-public utility service be identical to those offered by the public utility. Order No. 2003-A P 775, JA 724. Rather, the reciprocity policy requires only that the non-public utility charge rates comparable to the rates the non-public utility charges itself. Order No. 2003 P 843 & n. 146 (JA 191) (citing Order No. 888 at 31,761; *Long Island Power Authority*, 84 FERC ¶ 61,280 at 62,333 (1998)).

Thus, a non-public utility can meet the reciprocity requirement by offering all interconnection customers Interconnection Service identical to that offered to its own or affiliated generation. Order No. 2003-A P 775, JA 724. It may apply interconnection cost recovery and other terms and conditions of Interconnection Service to third parties in a manner comparable to the process it applies to itself. *Id.* P 777, JA 724.

Accordingly, a non-public utility must treat upgrade payments in a manner comparable to the manner in which it treats its own upgrade costs, and it will only be required to refund transmission upgrade costs if it affords itself comparable treatment. *Id.* PP 778-79, JA 724-725. Otherwise, it would not be required to refund transmission upgrade costs. *Id.*

**C. FERC's Requirements For Scoping Meetings Are Not Discriminatory.**

Interconnection Procedure § 3.3.4 requires the Transmission Provider and the Interconnection Customer to hold a scoping meeting within 30 calendar days from receipt of an interconnection request to discuss the interconnection, including technical information concerning the Transmission Provider's Transmission System. Order No. 2003-A P 101, (JA 621).

However, the Commission's Standards of Conduct, 18 C.F.R. § 358.5, require that if the Transmission Provider discloses transmission or market information to its wholesale merchant function or power marketing Affiliate, it must also disclose such information simultaneously to the public.<sup>10</sup> Order No.

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<sup>10</sup> *Standards of Conduct for Transmission Providers*, Order No. 2004, FERC Stats. & Regs., Regulations Preambles ¶ 31,155 (2003), *on reh'g*, Order No. 2004-A, FERC Stats. & Regs. ¶ 31,161, 107 FERC ¶ 61,032 (2004), *on reh'g*, Order No. 2004-B, FERC Stats. & Regs. ¶ 31,166, 108 FERC ¶ 61,118 (2004), *on reh'g*, Order No. 2004-C, 109 FERC ¶ 61,325 (2004), *on reh'g*, Order No. 2004-D, 110 FERC ¶ 61,320 (2005), *appeal pending*, *National Fuel Gas Supply Corp., et al. v. FERC*, D.C. Cir. Nos. 04-1183, *et al.*

2003-A P 103, JA 621. A separate, but related, Code of Conduct is imposed on a case-by-case basis when the Commission grants market-based power sales rate authorization, and generally contains a provision that all market information shared between the Transmission Provider and the Affiliate is to be disclosed to the public. *Id.* P 104 & n. 28, JA 621. The Standards and Code of Conduct were based on the general principle that a Transmission Provider must treat all customers, affiliated and non-affiliated, on a non-discriminatory basis, and cannot operate its transmission system to prefer its affiliates.

Following Order No. 2003, clarification was sought concerning whether a Transmission Provider would violate the Commission's Standards of Conduct or Code of Conduct if it shares technical information concerning its Transmission System with an Interconnection Customer that is an affiliate. *Id.* P 102, JA 621.

Determining the proper response to the request for clarification required balancing the competing interests involved. The Commission found:

To balance the need to treat affiliated and non-affiliated Interconnection Customers alike, adhere to the intent of the Code of Conduct and Standards of Conduct, and ensure that Critical Energy Infrastructure Information is not released to the public, we are adopting an approach here that is similar to the one taken in Order No. 2004. We will allow the Transmission Provider to share technical information related to its Transmission System with an Affiliate without having to simultaneously release the information to the public as long as the information relates solely to a valid request for Interconnection Service. In addition, we will require the following additional safeguards: the Transmission Provider must (1) post an advance notice to the public on its OASIS of its intent to conduct a

Scoping Meeting with its Affiliate; (2) transcribe the meeting in its entirety; and (3) retain the transcript for three years. . . .

Order No. 2003-A P 107, JA 622.

Utility Petitioners contend that the requirement of posting notice of scoping meetings with affiliates is unduly discriminatory because the identities of other Interconnection Customers do not have to be disclosed. Utility Br. 29. According to Utility Petitioners, the Commission has shown no factual basis to differentiate between affiliates and other customers, contrary to case law holding that FERC cannot treat similarly situated customers in a discriminatory fashion. *Id.* (citing *Pub. Serv. Co. of Indiana v. FERC*, 575 F.2d 1204, 1212 (7<sup>th</sup> Cir. 1978); *Town of Norwood*, 202 F.3d at 402). Utility Petitioners also assert that the Commission has offered “contradictory” justifications for disparate treatment of affiliate and non-affiliate Interconnection Customers. *Id.*

To the contrary, the Commission has consistently held that affiliated and non-affiliated Interconnection Customers are not similarly situated. Order No. 2003-B P 137, JA 946; Order No. 2003-C P 30, JA 984. *See also* Order No. 2003-A PP 103, 107, JA 621-622. That is why the Commission created the Code of Conduct and Standards of Conduct for affiliated Interconnection Customers. Order No. 2003-B P 137, JA 946. Transmission Providers can transfer market power to affiliated businesses not governed by standards of conduct by, *inter alia*, providing preferential access to information to the affiliate about the Transmission Provider,

its customers or other affiliates. Order No. 2004-A PP 5, 12 (Standards of Conduct Rulemaking, *see supra* note 9). *See, e.g., Tenneco Gas v. FERC*, 969 F.2d 1187, 1197 (D.C. Cir. 1992) (affirming FERC’s conclusion that utilities [in that case, pipelines], “which have market power over transportation service, give their marketing affiliates an undue competitive advantage when they give their affiliates information they do not also make available to other marketers”).

The Commission cited as examples of affiliate concerns several proceedings initiated to address alleged affiliate abuse. Order No. 2003-C P 30 n. 26, JA 984 (citing *Entergy Services, Inc.*, 111 FERC ¶ 61,145 P 10 (2005) (initiating hearing to examine “credible concerns” regarding transmission market power by failing to provide interconnections or blocking alternative generation sources); *Southern Companies Energy Marketing, Inc.*, 111 FERC ¶ 61,144 P 16 (2005) (initiating hearing to examine “credible concerns” regarding unduly preferential treatment afforded affiliates in accessing generation sites); *Entergy Services, Inc.*, 103 FERC ¶ 61,256 P 44-53 (2003) (initiating a hearing to examine concerns regarding affiliate dealing in a bidding process for power purchase agreements)).

Thus, the disparate treatment of affiliate and non-affiliate Interconnection Customers is justified because of non-theoretical concerns about affiliate abuse. Order No. 2003-C P 30, JA 984. The affiliate relationship is a factual difference that justifies the different treatment. *Id. See, e.g., Town of Norwood*, 202 F.3d at

402 (“differential treatment does not necessarily amount to *undue* preference where the difference in treatment can be explained by some factor deemed acceptable by the regulators (and the courts).”) (emphasis in original). The Commission’s approach reasonably balanced the need to treat affiliated and non-affiliated Interconnection Customers alike with the need to adhere to the Code of Conduct and Standards of Conduct requirements to address concerns regarding preferential treatment of affiliates. Order No. 2003-B P 137, JA 946. *See also* Order No. 2003-C P 30, JA 984.

**D. The Commission Appropriately Required Transmission Providers To Pay Interconnected Generators For Providing Reactive Power In Certain Circumstances.**

Reactive power is necessary to maintain the proper transmission line voltage on the transmission system. Under the name Reactive Supply and Voltage Control, it is one of the ancillary services that a Transmission Provider must offer under Order No. 888. *See* Order No. 888 at 31,706; Order No. 888-A at 30,227-228; Order No. 888-B at 62,093-94. In Order No. 2003, the Commission held that a Transmission Provider was required “to pay the Interconnection Customer for providing reactive power within the specified range if the Transmission Provider so pays its own generators or those of its Affiliates.” Order No. 2003-B P 119, JA 942. This was necessary, the agency determined, to ensure that “an

Interconnection Customer [would] be treated comparably with the Transmission Provider and its Affiliates.” *Id.*

Utility Petitioners object to this provision of Order No. 2003, arguing that it makes generators eligible for reactive power compensation “in the absence of a Transmission Provider’s full operational control,” which is an alleged departure from Order No. 888 requirements. Utility Br. 30.

As the Commission explained, however, there is no inconsistency in the treatment of reactive power by Order No. 888 and Order No. 2003:

[W]hile the transmission provider cannot demand that the Interconnection Customer operate its Generating Facility solely to provide reactive power, it may require the Interconnection Customer to provide reactive power from time to time when its Generating Facility is in operation. The requirement to pay exists only as long as the Generating Facility follows the Transmission Provider’s reactive power instructions. This is a sufficient level of control to warrant compensation for reactive power as described in Order Nos. 888-A and 888-B.

Order No. 2003-C P 43, JA 986; *see also* Order No. 2003-B P 118, JA 942.

This is precisely the type of difficult, technical ratemaking judgment that is entitled to deference. *See Entergy I*, 319 F.3d at 541.

**E. The Optional Liquidated Damages Provision In The Standard Interconnection Agreement Represents A Reasonable Exercise Of The Commission’s Judgment.**

Article 5 of the Standard Large Generator Interconnection Agreement governs matters relating to the engineering, procurement and construction of Interconnection Facilities and Network Upgrades. Under Article 5.1, JA 270, the

Interconnection Customer and Transmission Provider entering into the Agreement may “mutually agree[]” to a schedule for the completion of the Interconnection Facilities and Network Upgrades necessary to begin interconnection service. If the parties are not able to negotiate a schedule, the Interconnection Customer may choose among several options to proceed with the facilities. Under one option (Article 5.1.2, JA 270-271), if the Transmission Provider fails to complete the Interconnection Facilities and Network Upgrades by the required deadlines, it is liable to the generator-customer for liquidated damages, in accordance with Article 5.3 of the Agreement. Article 5.3, JA 272-273.

Utility Petitioners complain that the Commission “erred by granting Generators the right to select the construction timeline dates in certain instances and hold the Transmission Provider liable for liquidated damages if it fails to meet those dates.” Utility Br. 31. However, the relevant sections of the Large Generator Interconnection Agreement contemplate that the parties will negotiate a mutually-acceptable agreement. A liquidated damages provision is an option for negotiation, not a requirement. Thus, the Commission could reasonably state that “[w]hile we expect that the liquidated damages provision will play an important role in the parties’ negotiations, they need not agree to liquidated damages.” Order No. 2003-A P 250, JA 639.

Utility Petitioners also claim that liquidated damages may be assessed under the rule even if the Transmission Provider “acted reasonably or if the Generator was not harmed.” Utility Br. 31. However, the Commission found that construction and in-service date delays could jeopardize the Interconnection Customer’s funding, its opportunity to enter into long-term contracts, and its ability to make energy sales. Order No. 2003-A P 252, JA 639. Furthermore, the rule offers additional protection to the Transmission Provider “against unfair imposition of liquidated damages by Article 16.1 [of the Large Generator Interconnection Agreement (JA 292-293)], which allows it to declare a Force Majeure event if circumstances beyond its reasonable control prevent it from meeting the agreed upon milestones.” *Id.* P 266, JA 641. In these circumstances, the option of a liquidated damages clause is entirely reasonable.

## CONCLUSION

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

Respectfully submitted,

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### CERTIFICATE OF COMPLIANCE

In accordance with Circuit Rule 28(d)(1), and this Court's order of February 21, 2006, ordering that Respondent's Brief not exceed 20,000 words, I hereby certify that this brief contains 18,629 words, not including the tables of contents and authorities, the certificate of counsel, the glossary, this certificate and the addendum.

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